March 14, 2008

The Honorable Jim Davnie
545 State Office Bldg
100 Rev. Dr. Martin Luther King Jr. Blvd.
St. Paul, MN 55155-1606

Dear Representative Davnie:

We are writing on behalf of the American Securitization Forum ("ASF")[1] and the Securities Industry and Financial Markets Association ("SIFMA") [2] to inform you of our opposition to H.F 3612, the Minnesota Subprime Foreclosure Deferment Act of 2008. While well-intentioned as a means of helping distressed mortgage borrowers, this legislation would, if enacted, impose substantial costs and threaten the future availability of mortgage credit to ALL Minnesotans with those the legislation is intended to help being harmed the most.

Historically, the majority of mortgage loans, whether made to "prime" or "subprime" borrowers, are funded through the securitization markets. In simple terms, a "securitization" involves the sale of pools of mortgage loans by a mortgage originator into a specialized financing vehicle. This vehicle then sells securities (known as mortgage-backed securities, or MBS) to institutional investors such as public employee pension and mutual funds. The payments on the MBS are supported by cash flows generated by the pooled mortgage loans. In effect, these institutional investors become the new "owners" of the mortgage loans, returning capital to lenders who then are able to make more loans. Through this process, securitization has created a cost-efficient mechanism for funding mortgage loans for homeowners throughout the nation.

---

[1] ASF is a broad-based professional forum of over 375 organizations that are active participants in the U.S. securitization market. Among other roles, ASF members act as issuers, investors, financial intermediaries and professional advisers engaged in the financing and securitization of residential mortgage loans throughout the United States. ASF's mission includes building consensus, pursuing advocacy and serving as an informational and educational resource on behalf of the multi-trillion dollar securitization market in the United States. Additional information about ASF, its members and activities may be found on ASF's website, located at www.americansecuritization.com.

[2] SIFMA brings together the shared interests of more than 650 securities firms, banks, and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services, and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London. Its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong.

ASF and SIFMA support and have promulgated industry guidance to prevent foreclosures wherever possible as foreclosures are generally the most costly means of resolving a defaulted mortgage loan, and results in the highest losses to securitization investors. As such, there are strong economic and commercial incentives to avoid residential foreclosures on securitized loans. Unfortunately, in some situations no reasonable alternatives to foreclosure exist. In those situations, for the reasons outlined below, it is essential that the foreclosure process be allowed to proceed without delay, and without a governmentally-imposed diminution of the borrower's contractual payment obligation.

H.F 3612 would operate to delay the foreclosure process and to reduce the contractual payment obligation of a borrower during the period of that delay. There is already an existing legal process that has been institutionalized to protect the rights of borrowers and lenders, and the additional deferment included in this legislation is unnecessary and harmful in light of its costs. The imposition of such a delay and reduction in payments due will introduce a significant degree of uncertainty in whether and when an investor will be able to realize the value of the security for their investment. In the face of this uncertainty, investors will either require higher yields on mortgage-backed securities going forward, or investors will withdraw their participation from the market entirely. In either case, ALL mortgage borrowers in Minnesota will bear substantially greater costs and find fewer opportunities for affordable mortgage financing in a market environment already deprived of adequate access to affordable credit.

Investors value mortgage-backed securities by estimating the cash flows on the underlying mortgages. There are a variety of factors that can introduce risks into the predictability of those cash flows, and each of those factors is a source of risk for MBS investors. For example, most mortgage loans allow the borrower to prepay their loan at any time. Or, borrowers can default on their loans, which can affect both the timing of cash flows and the overall repayment of principal as the property securing the loan will be sold or auctioned to recover the proceeds of the loan. However, while investors holding these securities expect that foreclosures will proceed in accordance with current state law, H.F 3612 would work against investor expectations by legislatively imposing loan modifications and payment reductions, thus usurping the contractual duties of servicers charged to collect amounts owed on the mortgage loan. Recent data indicates that servicers have significantly increased their help to troubled borrowers in the forms of temporary payment deferrals, workout plans, interest and principal loan modifications, and other foreclosure prevention measures. In cases where a servicer has concluded that foreclosure is the only viable option and is lawfully permitted to initiate such proceedings, the servicer should be allowed to do so. Legislative interference would have grave consequences by introducing additional unpredictability to an already fragile mortgage finance environment. For future lending, the uncertainty of the recovery on a given loan will lead lenders to charge significantly higher rates, as investors in MBS would expect significantly higher yields to compensate for the additional risk.

Instituting a delay in the foreclosure process will also create uncertainty as to the recovery value for a loan, and in a declining home price environment such as we see today, it is very likely that a home will sell for less one year from now than it will today. A delay in foreclosure proceedings in today's housing market will reduce expectations of recovery on foreclosed properties. Thus for current mortgages, the institution of a foreclosure delay would likely cause an immediate drop in the value of loans held in a bank's portfolio, as well as for MBS in cases where loans have been securitized. Pension and mutual funds are large buyers of AAA MBS, and any reduction in the value of these securities will be reflected in the value of those pension and mutual funds. Since the foreclosure delays and principal write-downs that are proposed in the bill would reduce cash flows and devalue MBS that are collateralized by loans to Minnesota residents, the bill would essentially pull value from pension funds and 401(k) plans in order to temporarily benefit homeowners who go to foreclosure, with the added negative effect of drying up affordable credit to all Minnesotans who are looking to either refinance into a better mortgage product or finance a first-time home purchase.

While all mortgage borrowers would suffer from higher mortgage rates and reduced access to credit, the effect would be particularly pronounced for subprime borrowers who pose the greatest risk for entering foreclosure during the life of their mortgage. This increased risk, and the resulting increased costs of borrowing would be felt even more keenly in areas where home prices are declining, local economic conditions are poor, or a borrower tends to have a riskier credit profile. Given the current conditions in the mortgage market—lenders tightening credit standards, or lenders going out of business entirely—it is already becoming difficult for some borrowers to access mortgage credit at all. The changes proposed in the bill will exacerbate this problem and will harm those whom it intends to help by making it even more difficult and expensive for imperiled borrowers to obtain affordable new financing. Most importantly, potential Minnesota borrowers will face a significant decrease in the availability of affordable credit.

For the foregoing reasons, we oppose H.F 3612, the Minnesota Subprime Foreclosure Deferment Act of 2008. We thank you for your consideration of our views on this important legislation. For additional information on this issue, please contact Tom Deutsch at 212.313.1135 or at tdeutsch@americansecuritization.com or Scott Defife at 202.962.7300 or at sdefife@sifma.org.

Sincerely,

Tom Deutsch

Tom Deutsch
Deputy Executive Director
American Securitization Forum

Scott Defife

Scott Defife
Senior Managing Director, Government Affairs
Securities Industry and Financial Markets Association

CC: Representative Joe Atkins, Chair
Representative Leon M Lillie, Vice Chair
Representative Sarah Anderson
Representative Tom Anzelc
Representative John Berns
Representative Jim Davnie
Representative Chris DeLaForest
Representative Augustine Dominguez
Representative Sheldon Johnson
Representative Kate Knuth
Representative Tim Mahoney
Representative Joe Mullery
Representative Erik Paulsen
Representative Aaron Peterson