October 28, 2008

Lindsay Valdeon
Deputy Executive Secretary
Department of Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

Re: Request for Comments: Development of a Guarantee Program for Troubled Assets

Dear Ms. Valdeon,

The Securities Industry and Financial Markets Association ("SIFMA")[1] and the American Securitization Forum ("ASF")[2] are pleased to respond to the request for comments, dated October 10, 2008, by the United States Department of Treasury ("Treasury") relating to the development of a program (the "Guarantee Program") to guarantee the timely payment of principal of, and interest on, troubled assets originated or issued prior to March 14, 2008, as authorized by Section 102 of the Emergency Economic Stabilization Act of 2008 (the "Act"). Our members have a vested interest in the success of any program to restore liquidity and stability to the financial system of the United States. Due to the importance of this goal, SIFMA and ASF have been studying and discussing with our members the type and breadth of a Guarantee Program that would meet one or both of these stated goals and we respectfully request that Treasury consider the following comments in establishing and structuring a Guarantee Program.

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[1] 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.

[2] ASF is a broad-based professional forum of over 370 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 working on securitization transactions. ASF's mission includes building consensus, pursuing advocacy and delivering education on behalf of the securitization markets and their participants. Additional information about the ASF, its members and activities may be found at ASF's internet website, located at www.americansecuritization.com. ASF is an adjunct forum of SIFMA.

Please note that due to the breadth of the Treasury's request for comments and the interrelationship of a number of the key considerations we wish to address in this letter, we have not attempted to answer each of your questions raised in the request for comments. We also recognize that clarity from relevant regulatory and accounting bodies may be required, and additional discussions may be warranted, in order to implement some of the suggestions set forth in this letter.

I. GENERAL

SIFMA and ASF support the development of a Guarantee Program under the Act that promotes the stability of financial institutions and increases liquidity, provided that it is a scalable, revenue neutral program that minimizes risk to taxpayers. In addition, we believe that a Guarantee Program may require significant infrastructure to correctly price insurance for eligible assets, monitor performance and ensure timely reimbursement of losses. In this respect, (1) the potential liquidity and stability that could be provided by the Guarantee Program must be weighed against the liquidity and stability that could be provided by the purchase program, (2) the duration and complexity of a Guarantee Program must be weighted against the duration and complexity of the purchase program and (3) the risk to taxpayers under a Guarantee Program must be weighed against the risk to taxpayers under the purchase program. Notwithstanding these considerations, we specifically do not advocate the use of one program over the other.

This is particularly important in light of the limited resources available under the Act. Section 102(c)(4) of the Act provides that "the purchase authority limit in Section 115 is required to be reduced by an amount equal to the difference between the total of the outstanding guaranteed obligations and the balance in the Troubled Assets Insurance Financing Fund[3]." Section 115 limits the amounts of troubled assets that may be purchased under the Act to the aggregate of the purchase prices of the troubled assets held by Treasury at any one time. If troubled assets that are purchased are later sold, the amount available for the purchase of additional troubled assets would be increased upon such sale. In other words, it can be employed as a revolving purchase facility. In contrast, the extent to which the Guarantee Program utilizes the purchase authority set forth in Section 115 under the Act would decrease only (1) if a guaranteed obligation is no longer outstanding or (2) by the amount of premiums and reinvestment earnings, in the Troubled Assets Insurance Financing Fund (net of claims paid from the fund). Additionally, a Guaranty Program does not directly inject capital into the markets, although it would indirectly free up capital of financial institutions by potentially lowering capital charges.

Therefore, since the amounts guaranteed under the Guarantee Program will reduce the purchase authority for the purchase of troubled assets, and guarantees may remain outstanding for a substantial period of time, SIFMA and ASF recommend that the Guarantee Program be utilized in circumstances where it is clearly a more efficient and more advantageous use of the

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[3] We interpret "total of outstanding guaranteed obligations" to mean the "total principal amount of outstanding guaranteed obligations," and we do not interpret the statutory language to include accrued interest or other amounts payable on the applicable obligation.

purchase authority under the Act. We believe that in some instances or markets, the Guarantee Program may indeed offer Treasury such efficiency.

Furthermore, the complexity of the Guarantee Program and the ease of utilizing it should be considered to ensure that it meets the stated goals of the Act to provide assistance to all financial institutions regardless of size, geography, form of organization, or the size, type, and number of assets.

II. EXTENT OF GUARANTEES TO BE PROVIDED

SIFMA and ASF believe that the Guarantee Program allows for guarantees on the full outstanding principal amount of, and interest on, the asset being guaranteed or, alternatively, on a portion of the principal amount and/or interest. Given the limited purchase authority under the Act, Treasury may not want to guarantee credit-sensitive assets that have a currently existing market due to sufficiently high yields to attract investors. Rather, Treasury may consider only providing full principal guarantees for those assets and in those circumstances where there is no investor demand. In circumstance where no current investor demand exists at any risk level, the guarantees will have an immediate and significant impact in promoting liquidity and/or financial stability.

Another option that Treasury should consider is a full guarantee on a portion of the risk inherent in the troubled asset. This can be accomplished by either insuring against all losses above a given threshold or insuring only a percentage of losses above a given threshold or attachment point. For example, assuming a security has a $100,000 balance, and the assumed loss is determined to be $20,000, the guarantee would be for a specified percentage of losses, or alternatively all losses, on the asset in excess of the first $20,000 of losses. This would provide additional credit support to the senior $80,000 portion of the asset. The senior $80,000 portion of the asset could then either be held on the books of the financial institution at a higher value and thus reduce the capital reserves requirement for that asset and free additional capital for lending, or be sold at a higher price as a result of the guarantee. By using this model rather than guaranteeing the entire principal amount of a troubled asset, these guarantees may effectively utilize the limited purchase authority available under the Act and may allow Treasury to guarantee a larger number of troubled assets, thereby encouraging private investment in both guaranteed and unguaranteed assets and increasing overall liquidity. In essence, the program authority should be used to identify and guarantee assets only up to the risk levels sufficient to attract investors. Such use of the guarantees will lessen the risk of the unintended consequence that the existence of significant amounts of United States government guaranteed debt outstanding may actually reduce demand for lower yielding assets for which demand exists currently (e.g. agency MBS).

III. TYPES OF ASSETS TO BE GUARANTEED

SIFMA and ASF support the use of a Guarantee Program to cover assets with high illiquidity premiums relative to their expected losses. In such instances, the assets are unable to be sold at prices that are reasonable based on the quality of the asset. SIFMA and ASF believe that the Guarantee Program should be considered for use with a full spectrum of financial assets, including both securities and whole loans. Treasury may consider whether identifying frequently referenced assets (such as RMBS referenced in multiple CDO transactions) may present an opportunity to magnify the benefits of any purchase or guarantee program

For example, the Guarantee Program could greatly improve liquidity for a variety of troubled assets such as mortgage-backed securities ("MBS"), including both residential MBS and commercial MBS (particularly commercial MBS with substantial concentrations of multifamily loans), consumer assets, asset-backed securities ("ABS") backed by consumer assets such as credit cards, auto loans and student loans, auction rate securities, bank trust preferred securities and municipal bonds, among other securities. The program may be especially effective for highly rated senior securities as well as subordinated securities[4] that are not expected to experience material losses due to government guarantees on all or a substantial portion of the underlying assets, or as a result of other credit enhancements (such as ABS with a monoline wrap). Using the Guarantee Program in this manner may increase liquidity for these types of assets, as well as present less risk to the taxpayers.

The Guarantee Program could also be used to guarantee whole mortgage loans, particularly to promote loan modifications according to terms that could be outlined by Treasury, or in circumstances in which the modified loan would not be eligible for purchase by Freddie Mac or Fannie Mae or eligible for a guarantee under another existing program such as the Federal Housing Administration's existing programs or the United States Department of Veterans Affairs loan guarantee program.[5] This could take the form of a traditional loan insurance program, similar in nature to that of FHA, or it could take the form of a standing commitment by the Treasury to purchase defaulted loans that were current at the initiation of the insurance, or a loss sharing arrangement where the Treasury would pay to the insured an agreed-upon percentage of the losses on consumer loans or mortgage loans that are not delinquent at the time of entering into the Guarantee Program.

In either instance, setting the payout from the Treasury to the holder at less than 100% would encourage participating financial institutions to use all available loan modification, foreclosure-avoidance and loss-mitigation procedures to keep deserving borrowers in their

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[4] For instance, many regular issuers of securities have been unable to place investment grade subordinated securities as a result of the current market disruption. Often these securities must be issued to support the much larger senior tranches that provide the bulk of the issuer's securitization funding, and the issuers have used capital to hold these securities on balance sheet to allow their securitization programs to continue. A guarantee that allowed the issuer to move these securities off balance sheet might provide a very efficient way of enhancing the issuer's overall funding.

[5] We note that Section 109 of the Act gives Treasury the authority to provide guarantees and credit enhancement to promote loan modifications. Although perhaps beyond the scope of the request for comment, the Section 109 guarantee authority, to the extent that it is not subject to the Section 115 purchase authority limit, could be utilized for loans in securitized pools of mortgage loans. If the securitized loan as modified were guaranteed under Section 109 authority, the net present value of the loan as modified would not have to be reduced to account for risk of further default and the related servicers would be more likely to be able to offer the loan modifications consistent with the governing documents for the securitization. This would both enhance the stability and liquidity of the securities and to promote the stated goal of homeowner relief and foreclosure prevention. Furthermore, if the Section 109 guarantee authority is not subject to the Section 115 purchase authority limit, the Guarantee Program should only be used when Section 109 is not available or appropriate for use.

homes. Care should be taken with the design of any whole loan guarantee program to ensure that the interest of the Treasury and the servicers of the guaranteed loans are aligned in the goals of promoting modifications that mitigate losses, perhaps by requiring the use of servicing standards similar to those already in place for FHA, Freddie Mac and Fannie Mae.

IV. GUARANTEE PAYMENT CONSIDERATIONS

A variety of guarantee payment proposals have been suggested to SIFMA and ASF by their members. Some involve payments on a monthly basis, triggered by shortfalls in interest or scheduled principal payments indicated on the monthly trustee or servicing reports for the security or mortgage loan. Others involve payments upon maturity or liquidation or upon realization of loss on the underlying asset. Either methodology may be appropriate for a particular asset.

In any event, we believe Treasury should have the flexibility to adopt one or more of these specific approaches, and we believe each of them would be consistent with the statutory language in Section 102(a)(3) of the Act to the effect that "the Secretary may guarantee the timely payment of, and interest on, troubled assets ... ."

V. TRANSFERABILITY AND IRREVOCABILITY OF GUARANTEES

SIFMA and ASF believe that any guarantees under a Guarantee Program should be transferable to future holders, should be irrevocable and should be in effect for the life of the guaranteed asset. We believe that these features would maximize the effectiveness of the program. Utilizing the Guarantee Program to provide transferable credit support for a troubled asset will allow potential investors to more readily purchase these assets and may help to restore and/or increase investor confidence in these assets. This is particularly the case for certain types of assets that have not to date experienced actual losses and are not anticipated to experience losses based on conservative loss models, but are still illiquid due to general market conditions and loss of confidence. Any increase in the marketability of those assets would be helpful for purposes of price discovery and would also encourage long term investors to purchase those assets from the financial institutions that currently hold those assets, improving the capital positions of those financial institutions.

Transferable guarantees would also facilitate the financing of such assets. Investors not only consider the current price and expected loss on any asset when considering a purchase, but also the availability of financing for the asset as all of these factors contribute to the calculation of the ultimate yield for many investors. A transferable guarantee would encourage financing of these assets and thus would serve to increase liquidity in the market for these types of assets.

VI. ACCOUNTING AND CAPITAL CONSIDERATIONS

The inseparability of the guarantee from the asset is important in that it will allow financial institutions to avoid markdowns on securities for credit deterioration, which are currently causing tremendous stress on financial institutions (if less than the full asset were insured, presumably the credit deteriorations would still result in markdowns if they were so significant as to exceed the amount of the insurance coverage). Thus, an important consideration for the successful implementation of the Guarantee Program will be how guaranteed assets are accounted for, and the impact of the guarantee on risk-based capital requirements for financial institutions.

When an existing asset is insured by a surety bond or other type of insurance after its original issuance, the accounting treatment for that asset does not change. Assets required to be marked to market will still be required to be marked to market as a standalone financial instrument (i.e., excluding the guarantee). The surety bond or other insurance is accounted for separately from the asset according to insurance accounting rules. Given that the asset will still be marked to market as a non insured asset, it faces potentially the same volatility that existed before the Guarantee Program, regardless of the fact that the asset is backed by the full faith and credit of the United States. However, if financial institutions participating in the Guarantee Program were able to achieve unitary accounting treatment, that is, if they were able to account for the newly insured asset as if it were originally issued with the full faith and credit of the United States behind it (i.e., one instrument comprised of the asset and guarantee), these financial institutions would receive much more beneficial accounting treatment. Instead of marking the asset to market as a non-insured asset and accounting for the guarantee separately the insured asset could be marked as United States government-backed debt, which would presumably result in much more stable valuations.

SIFMA and ASF members believe it will be difficult, if not impossible, to achieve unitary accounting treatment for guaranteed assets under current accounting rules, short of Treasury issuing new guaranteed securities to replace the assets proposed to be guaranteed,[6] or the original transaction documents being amended to incorporate the guarantee (which would be an extraordinarily inefficient and realistically impossible task for securities held by numerous investors). The best outcome might be achieved if the Securities and Exchange Commission (the "SEC") and the Financial Accounting Standards Board were to issue guidance that clarifies that the insurance and the insured asset should be viewed as unitary assets given the characteristics and design of the program.

A similar situation arises with respect to bank regulatory risk-based capital rules. United States government-guaranteed debt achieves lower risk weighting under risk-based capital rules than uninsured debt. For example, GNMA MBS carry a 0% risk weight.[7] It seems logical that a similar treatment should be afforded to debt guaranteed under the Guarantee Program. While presumably guaranteed assets will remain on balance sheets of the holders, at least for a period of time, favorable adjustments to risk weights by banking regulators and the SEC would provide immediate balance sheet relief to participating financial institutions.

VII. PREMIUMS

[6] This can possibly be accomplished by using a custodian to hold both the guaranteed asset and the guarantee and to issue custodial receipts evidencing ownership of both the guaranteed asset and the guarantee. For those assets that are securities, a new CUSIP number could be obtained with respect to these custodial receipts.

[7] MBS issued by Freddie Mac or Fannie Mae carries a 20% risk weight, but the banking agencies have recently proposed lowering that to 10%. Uninsured private market debt carries risk weights of up to 100%.

One concern raised by some members of SIFMA and ASF is the complexity of determining pricing mechanics that would enable the Guarantee Program to be self-funding but still ensure that the premiums would be low enough that the Guarantee Program could be effectively utilized by the market. The determination of a risk level of each guaranteed troubled asset will be critical in assessing the appropriate premium. The more complex any such troubled asset is, the more analysis and modeling would be required to put into place the guarantee. One of the parameters used in selecting a manager for the Guarantee Program should be its experience and expertise in such analysis and modeling.

Calculation of expected losses and the pricing mechanics should be industry-accepted and transparent to allow for consistent pricing and to instill market confidence. Pricing of guarantees for mortgage-related assets should be based upon an actuarial model similar to that used by Freddie Mac and Fannie Mae, or an industry-accepted third-party model. Treasury should apply "stress case" scenario modeling when projecting losses to protect taxpayers against overly optimistic "base case" projections. Given the ongoing market turbulence, actuarial models should be carefully scrutinized to determine whether they still adequately reflect risk, and premiums should be set on an asset-by-asset basis.

Premium payments could be required to be paid upfront, on an ongoing basis or a combination of the foregoing. Upfront premiums would minimize the reductions required to be made to the capacity availability under the purchase authority established under the Act. In the event that any guarantee is terminable by the holder, the premium should be upfront, as less risky assets would be more likely subject to cancellation than the more risky assets, which would reduce the diversity of the mix of assets being guaranteed under the Guarantee Program and increase the risk level of the remaining pool of guaranteed assets, with the result that the Guarantee Program would not be able to properly price its risk. Upfront premium collection would also serve to isolate the Guarantee Program from counterparty risk and allow use of the premiums until payment (if any) is required under the guarantee, permitting additional investment income to flow into the Guarantee Program. On the other hand, ongoing premiums would require less initial outlay by financial institutions, which could be beneficial to the institution. Moreover, the periodic premium payments could be made out of cash flow on the underlying guaranteed asset (if sufficient), although this could increase the burdens and costs of implementing the Guarantee Program[8].

VIII. USE OF GUARANTEE PROGRAM FOR REINSURANCE

Another suggestion of some members of SIFMA and ASF is to use the Guarantee Program to provide reinsurance to insurance companies for surety bonds backing municipal bonds and a wide variety of other structured products. Due to ratings downgrades affecting certain financial guarantors engaged in the business of insuring municipal bonds and structured securities, many securities are being downgraded by the rating agencies, reducing liquidity and, in many cases, forcing the holders that are statutorily required to only hold bonds with certain

[8] To the extent that the premiums are ongoing and are paid out of cash flow of the guaranteed asset, the duties of the custodian for a custodial receipt program could include the collection of payments on the asset and the payment of the applicable premiums to Treasury prior to making payments to investors.

ratings to sell these bonds. The New York State Insurance Department has required certain insurance companies to obtain reinsurance for many of these surety bonds. Even though the reinsurers have stepped in and guaranteed such surety bonds, reinsurers themselves have also been downgraded; thus the reinsurance has not increased stability or liquidity in these markets.

Those companies that have obtained reinsurance have given up the majority of the original premiums paid for the surety bond to the reinsurer. However, if the reinsurer is unable to meet the claim, the original insurer is still liable for the claim. As a result, there is fear that the original insurers may be required to pay claims, without reimbursement from the reinsurers or from general funds because they no longer have any unearned premium reserves to pay the claim. This has increased uncertainty to equity holders in these insurance companies and hampered the ability of these companies to recapitalize due to the uncertain nature of the full amount of claims that may actually be required to be paid. If the Guarantee Program were used to provide reinsurance, the liquidity of these markets for municipal bonds and structured securities, as well as the stability of the insurance industry, would improve. With reinsurance provided by the Treasury, the ratings downgrades would end and presumably the bonds would be upgraded. As a result, the current holders who are restricted to investing in highly rated instruments would no longer be forced to sell and liquidity would be improved. Additionally, the financial stability of the original insurers would be improved. Use of the Guarantee Program in this manner would also help protect taxpayers in the case of municipal bonds, as municipal bonds are typically purchased only by United States taxpayers.

IX. USE OF GUARANTEES AS AN EXIT STRATEGY FOR ASSETS PURCHASED BY TREASURY

A Guarantee Program might be useful as an exit strategy to be used in conjunction with the troubled asset purchase program established under the Act, to the extent the Guarantee Program has not been fully utilized to guarantee other assets. Assets purchased under the Act could be repackaged with a Treasury guarantee and resold. Such guarantee would become effective only at the time of sale, perhaps after Treasury-directed loan modifications or other homeowner relief initiatives, and as such purchase program limits could be maximized. As discussed above, these repackaged assets would be more liquid than the currently existing assets and would enable Treasury to use the proceeds of such sale to purchase additional troubled assets. An added benefit would be to reduce the amount of time troubled assets remain on the books of Treasury. A pre-existing exit strategy for troubled assets purchased under the Act could greatly enhance the success and reach of the Act.

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SIFMA and ASF appreciate this opportunity to comment on the development of the Guarantee Program under the Act. We would welcome the opportunity to provide any additional information that could be of assistance in considering the issues discussed in this letter. If you have any questions concerning these comments, or would like to discuss the issues raised herein, please feel free to contact Sean Davy at (212) 313-1118 or via email at sdavy@sifma.org or George Miller at (212) 313-1116 or via email at gmiller@americansecuritization.com.

Sincerely,

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