24 October 2011

Mr. William Coen
Mr. Neil Esho
The Joint Forum
c/o Bank for International Settlements
CH-4002 Basel, Switzerland

Dear Mr. Coen and Mr. Esho:

Securitisation market members of the Association for Financial Markets in Europe (AFME), the Securities Industry and Financial Markets Association (SIFMA) and Asia Securities Industry and Financial Markets Association (ASIFMA), working together as the Global Financial Markets Association[1] (GFMA) read with interest the Joint Forum's July Report on Asset Securitisation Incentives (the "Report"). Although the report is not a consultation, the securitisation industry is keen to maintain an active dialogue with the Joint Forum. As sovereign, covered bond and unsecured funding markets have shown signs of strain in recent weeks, our members believe that it is even more important to recognise and support sensibly regulated and prudently deployed securitisation as a key funding tool to provide liquidity for banks and funding for the real economy. Our members would therefore like to offer some constructive comments that we hope will serve as part of that ongoing dialogue.

The Future Prospects for Securitisation

The industry welcomes the G-20's November 2010 report that notes that "re-establishing securitisation on a sound basis remains a priority in order to support provision of credit to the real economy and improve banks' access to funding in many jurisdictions." This high-level statement of support is very helpful, and the industry is committed to working with global policymakers on continuing to develop the infrastructure and business practices necessary for a sound, long-lasting and sustainable securitisation market.

[1] The Global Financial Markets Association (GFMA) joins together some of the world's largest financial trade associations to develop strategies for global policy issues in the financial markets, and promote coordinated advocacy efforts. The member trade associations count the world's largest financial markets participants as their members. GFMA currently has three members: the Association for Financial Markets in Europe (AFME), the Asia Securities Industry & Financial Markets Association (ASIFMA), and, in North America, the Securities Industry and Financial Markets Association (SIFMA).

The industry agrees with Report observations that many complex structures are unlikely ever to return, and that at least in the short to medium term issuance volumes for all products are likely to be significantly lower than immediately prior to the crisis. This is unfortunate because, however justified the criticism of certain types of complex and highly levered structures, it remains the case that before the crisis securitisation played a very significant role in financing "real economy" assets.

In 2006, in the US market, securitisation outstandings provided USD 725.6 billion[2] to residential homebuyers and USD 81.9 billion to auto manufacturers. In Europe, the residential mortgage-backed securities market provided some USD 306.4 billion equivalent of funding. These funding sources have fallen substantially since the crisis: for example, non-agency prime and near-prime RMBS outstandings in the US have shrunk to USD 12.1 billion. In Europe, issuance remains heavily reliant on "repo trades" with the European Central Bank and the Bank of England and we believe there are no more than 50 or so active investors remaining.

Traditional multi-seller ABCP conduits continue to struggle to provide cost-effective funding to real-economy businesses for various asset classes including trade receivables and auto loans.

In light of the above, the industry particularly agrees with the Report's observation that it is important to remove the negative perception attached to securitisation products. This is essential if securitisation is to begin to recover to pre-crisis levels, and deliver the funding that is urgently needed to help finance economic recovery across the US and European economies.

Although many improvements have already been made with respect to disclosure, quality of reporting, CRA practices and investor due diligence, it is acknowledged that many senior investors have simply stopped participating in the sector due to the "headline risk" associated with certain discredited products such as US subprime and CDOs squared, which in turn has tainted the entire sector. This is despite the very strong credit performance of many other securitisation asset classes globally. An additional significant challenge to significant improvements to the robustness of securitization markets, especially those that are mortgage-related,

[2] This figure represents "non-agency" prime and near-prime MBS.

is the generally unsettled regulatory environment that surrounds securitization more generally.[3]

Measures to Increase Disclosure and Transparency

The report notes that a number of regulatory as well as industry initiatives are improving the quality of disclosure and transparency. The industry fully supports the need for investors to have the data they need, including the analytical tools to process that data. This work is a high priority for the industry and will continue. Indeed, many of our members have been actively involved in a number of the initiatives, and the industry looks forward to continuing to work with regulatory and central banking authorities to make relevant data more widely available.

Credit Rating Agencies

Much has been written and said on the role of the CRAs. Considerable legislation has been implemented globally to address certain business practices in order to reduce or eliminate perceived conflicts and to reduce reliance on the CRAs. However, it should be noted that in many global securitisation "real economy" asset classes credit performance and rating migration has been good and well within expectations, despite the stresses of the financial crisis.

We believe that there is a clear need to ensure that any further regulatory reform of the CRAs, including the finalization of existing regulatory proposals, is undertaken based on evidence, with due care, and at a considered pace. Many CRAs have already improved business practices which were perceived to have led to "conflicts of interest". It is also important that implementation of CRA regulations should be consistent globally, since otherwise overlapping rules could lead to considerable uncertainty for issuers, which may restrict the availability of finance and thereby constrain economic growth.

[3] For example, in the United States, regulators and policymakers currently are discussing rules, regulations, and standards regarding: credit risk retention, mortgage lending and underwriting, mortgage servicing, the future role of government support for housing finance, capital requirements, permitted activities of banks, removal of credit ratings from financial and other regulations and a variety of rules regarding credit rating agencies more broadly. There are proposed rules at varying stages of completeness (but not final) in each of these areas. Many similar discussions are occurring in Europe and other regions. The impact of this is felt not only by issuers, but also investors.

As far as types of CRA business models are concerned (for example, "issuer-pay" vs "investor pay" or some other model), we believe that it is important for the global regulatory regime to continue to support a plurality of business models and maintain a level playing field for CRAs based on market demand. In particular, regulators should not legislate to reduce or prohibit use of the "issuer-pays" model where conflicts can be shown to be managed effectively, and there is no compelling evidence to suggest that alternative models would be more effective.

Document Standardisation and Reduction in Complexity

The industry notes the Report's comments on the benefits of reduced product complexity and greater document standardisation. The Report also notes that it could be useful to standardise most securitisation products to some extent. We note that the phrase "standardisation" is understandably used frequently by policymakers as a goal.

While we are broadly sympathetic to standardisation as a concept, we ask the Joint Forum to note there is an important difference between standardisation of securitisation transaction documents and disclosure, and standardisation of the underlying products or assets which are securitised.

The industry is very supportive of the standardisation of securitisation transaction documents and disclosure, since consistent usage of definitions, formatting, amount and placement of content can save time and costs for all participants at both the document development as well as at the investor/credit monitoring user level.

On the product side, certain complex structures are unlikely to return. However, an important question is whether further standardisation of securitisation structures which support core "real economy" asset classes such as residential mortgages, auto loans, credit cards, consumer loans and simple CLO structures is either necessary or desirable. Further, attempts to standardise the underlying "real economy" assets themselves could reduce consumer choice and flexibility[4].

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[4] That said, to the extent that standards are created we note generally the importance of clear standards, wherever they may be positioned by policymakers, in order that market participants are able to discern with certainty the credit quality or other features of a particular asset that may be securitized.

There are a number of potential constraints in this area which should be borne in mind. Firstly, national legal and tax/fiscal issues, which necessarily must be different across national borders. Secondly, there are commercial reasons for differences in underlying products originated by lenders, since structures must be designed to reflect and accommodate the cash flows from those specific assets. Thirdly, IT systems are frequently designed to comply with an institution's overall accounting and processing systems, and/or national regulatory reporting standards[5]. From a practical standpoint, many issuers may simply be unwilling to incur the cost of changing their computer systems to match the exact cash flows of their competitors' structures. Investors might not be willing to pay a sufficiently higher price for standardised cash flows, than for slightly less standardised cash flows. The industry will continue to work with investors in seeking to achieve the right balance between investors' inherent need for sufficient simplicity and standardisation, which at least in theory should help liquidity, and the practical constraints of matching issuers' and consumers' needs.

Review of Recent Regulatory Initiatives

In the Appendix, the Report lists a wide variety of recent global regulatory initiatives which impact securitisation investment, issuance, trading, risk management, capital allocation, record keeping and other important areas. These regulations are rightfully intended to reduce reliance on credit rating agencies, align investor and issuer interests, improve transparency, and remove regulatory capital arbitrage opportunities which can distort market behaviour. Inevitably, these regulations will raise issuance and investor costs.

The industry recognises that up to a certain point, this may be a necessary part of the overall need to address past business practices that have been perceived to have fallen short. However, even if the marginal cost of each regulatory change may be manageable, we urge the Joint Forum to bear in mind the cumulative impact of successive layers of new regulation. This can occur within one jurisdiction, or globally across different jurisdictions. Not only can this lead to a substantially increased regulatory burden, in terms of administrative time, personnel and technical resources and cost, but there is a danger that over-regulation can send

[5] For example, in the RMBS context, the definition of "current balance" can vary from one originator to another, and is difficult to define proscriptively without considerable IT implications. A "comply or explain" approach has been found to be the most suitable work-around in this context.

negative signals to investors and issuers that securitisation issuance and investment is actually discouraged.

Further, in certain instances GFMA members are concerned that regulation may go beyond increasing cost and make certain kinds of securitization transactions impossible. This could happen for a variety of reasons. One is that the variety of underlying assets and structures is vast – and different markets often require different, or at least nuanced, regulatory solutions. For example, a regulatory solution that works for mortgage securitization may not work for corporate loan securitization, or securitization of airplane lease revenue, or a securitization of commercial loans.

In the market for European CLOs, issuance ground to a halt during the first 9 months of 2011. While this was largely due to spread conditions, the continuing uncertainty over the application of the risk retention requirements of Article 122a had a discouraging effect. Greater clarity in this area is of considerable assistance in helping to revive this important market and we welcome the publication in September by the European Banking Authority of its "Q&A" regarding Article 122a[6]. We will continue to engage with them on any remaining questions. In the US, similar concerns have been expressed about various provisions of the proposed risk retention regime and its impact on certain markets.

The worst case outcome is that a well-intentioned regulatory action directed toward one market would make transactions in a related market, which have proven their value, impossible.

In order to send more positive signals, and to try to reduce the costs of required regulation to a reasonable minimum so as to preserve the economics of a sustainable business model, the industry strongly encourages global regulators to make global regulations consistent. This would include European, American and Australian regulations on risk retention, credit rating agencies regulation, capital and liquidity charges, bank liquidity buffer eligibility, insurance and fund investment regulation, and many other issues. This ties in to the need for an

[6] "Q&A on Guidelines to Article 122a of the Capital Requirements Directive" published on 29th September 2011, see http://www.eba.europa.eu/cebs/media/Publications/Standards%20and%20Guidelines/2011/EBA-BS-2011-126-rev1(QA-on-guidelines-Artt122a).pdf

overall review of shadow banking activities, which is another important Financial Stability Board initiative. The industry agrees that improved transparency in the shadow banking sector is an important part of the review of all securitisation-related regulatory initiatives.

Again, we look forward to an ongoing dialogue on these important industry issues.

Regards,

T. Timothy Ryan, Jr.
CEO
GFMA