

**MEMO# 26456**

September 4, 2012

# **ICI and Banks File Joint Supplemental Comment Letter on Credit Risk Retention Proposal's Application to Tender Option Bond Programs**

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TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 56-12  
FIXED-INCOME ADVISORY COMMITTEE No. 19-12  
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 38-12  
SEC RULES MEMBERS No. 79-12 RE: ICI AND BANKS FILE JOINT SUPPLEMENTAL COMMENT LETTER ON CREDIT RISK RETENTION PROPOSAL'S APPLICATION TO TENDER OPTION BOND PROGRAMS

On August 31, 2012, the Investment Company Institute, along with Wells Fargo Bank N.A., Citibank, N.A., Société Générale, New York Branch, and Deutsche Bank AG, New York Branch ("banks"), filed a supplemental comment letter addressing the applicability of the proposed credit risk retention requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") to tender option bond programs ("TOB programs"). [\[1\]](#) ICI had submitted a comment letter on the Proposal in July 2011 that, among other things, requested clarification that TOB programs were not within the scope of the Proposal or, alternatively, that they be exempted from the Proposal's risk retention requirements. [\[2\]](#) The supplemental comment letter, which was filed at the Agencies' request, is attached, and is described briefly below.

The supplemental comment letter asserts that TOB programs should be exempt from the Proposal's risk retention requirements because, among other reasons: (i) TOB programs are almost uniformly used to finance municipal securities, not to transfer risk; (ii) the TOB program structure ensures that the interests of the securitizer are closely aligned with those of the holders of the TOB floating rate certificates and provides all participants with transparency regarding the TOB program assets; (iii) TOB program assets are high quality and are typically publicly issued, rated debt securities that are subject to the anti-fraud provisions of the federal securities laws; and (iv) TOB programs are vital to both the municipal securities market and the tax-exempt money markets. [\[3\]](#)

The supplemental comment letter requests that if the Agencies determine that, despite

these reasons and those provided in the initial comment letters submitted by ICI and the banks, a full exemption from the risk retention requirements for TOB programs is not permitted or appropriate, the Agencies should develop risk retention requirements specifically designed for TOB programs. TOB programs would not meet any of the existing proposed risk retention options included in the Proposal. Accordingly, the comment letter suggests the Agencies provide a choice among one or more of three risk retention options described in the letter.

Under the first risk retention option described in the letter, a TOB program transaction in which the residual interest holder is either (i) the same as, or an affiliate of, the entity that provides a liquidity facility in connection with the TOB program, or (ii) an unaffiliated entity that agrees to reimburse the liquidity facility provider for any losses incurred in providing the liquidity facility, would have a risk retention requirement of zero percent. This option recognizes the fact that all of the market risk associated with the underlying assets is already borne by the residual interest holder. Under the second risk retention option, the credit risk retention requirement would be satisfied by purchasing and retaining a residual interest having an up-front cash investment value equal to five percent of the initial market value of the municipal securities in the TOB program. Under the third risk retention option, TOB program transactions would be subject to a credit risk retention amount equal to the excess of five percent of the initial market value of the municipal securities in the TOB program over the initial market value of municipal securities that the residual interest holder owns directly outside the TOB program that have the same credit risk (that is, securities issued by the same issuer with the same source of payment and same payment priority), up to and including a full offset (i.e., the risk retention amount inside the TOB trust may be zero percent).

The letter urges that any risk retention requirements apply prospectively only. It argues that these requirements or any others the Agencies establish should not apply to TOB program trusts in existence on the effective date of the implementing rules.

The letter also suggests that the Agencies require the securitizer of a TOB program to provide, or cause to be provided, to potential purchasers of floating rate certificates a reasonable time prior to the sale of those certificates and, upon request, to the SEC and to the appropriate Federal banking entity (if any) specified information about the risk retained pursuant to the three options described above. It also recommends that the disclosure include the material assumptions and methodologies used to determine the aggregate dollar amount of floating rate certificates issued by a TOB trust.

Sarah A. Bessin  
Senior Counsel

[Attachment](#)

#### **endnotes**

[\[1\]](#) Last year, the Securities and Exchange Commission, the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, and the Department of Housing and Urban Development (“Agencies”) issued proposed rules to implement the credit risk retention requirements of Section 15G of the Securities Exchange Act of 1934, as

added by Section 941 of the Dodd-Frank Act. Credit Risk Retention, 76 Fed.Reg. 34010 (June 10, 2011) ("Proposal"), available at <http://www.sec.gov/rules/proposed/2011/34-64603fr.pdf>. The Proposal generally would require a sponsor of asset-backed securities to retain not less than five percent of the credit risk of any asset that the sponsor, through the issuance of the asset-backed securities, transfers, sells, or conveys to a third party. For a discussion of the Proposal, see ICI memorandum No. 25162 (May 2, 2011), available at [http://www.ici.org/my\\_ici/memorandum/memo25162](http://www.ici.org/my_ici/memorandum/memo25162).

[2] For a description of ICI's July 2011 comment letter, see ICI memorandum No. 25368 (July 29, 2011), available at [http://www.ici.org/my\\_ici/memorandum/memo25368](http://www.ici.org/my_ici/memorandum/memo25368). The banks that participated in the supplemental comment letter also submitted a prior comment letter. That letter, dated August 1, 2011, solely addressed application of the proposed risk retention requirements to TOB programs.

[3] A TOB trust typically holds one or more high-quality municipal bonds, and issues two classes of tax-exempt securities: a short-term floating rate certificate that is supported by a liquidity facility, and an inverse floating rate security, or residual interest. Tax-exempt money market funds are the principal holders of the floating rate certificates. Holders of residuals are typically long-term investors, such as the TOB program sponsor bank or an affiliate, tax-exempt bond funds, closed-end funds, or other institutional investors in municipal bonds.