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MetLife

October 30, 2013

By Electronic Submission

Office of the Comptroller of the Currency
Legislative and Regulatory Activities Division
400 7th Street, SW, Suite 3E-218, Mail Stop 9W-11
Washington, DC 20219
Docket Number OCC-2013-0010

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attn.: Robert deV. Frierson, Secretary
Docket No. R-1411

Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attn.: Comments, Robert E. Feldman, Executive Secretary
RIN 3064-AD74

Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
Attn.: Elizabeth M. Murphy, Secretary
File Number S7-14-11

Federal Housing Finance Agency
Constitution Center
(OGC) Eight Floor
400 7th Street SW
Washington, DC 20024
Attn.: Alfred M. Pollard, General Counsel
RIN 2590-AA43

Department of Housing and Urban Development
Regulations Division
Office of General Counsel
451 7th Street, SW
Room 10276
Washington, DC 20410-0500
Docket Number HUD-2013-0090

Re: Credit Risk Retention Re-Proposal

Ladies and Gentlemen:

As one of the largest investors in the securitization market in the United States, we are pleased to submit this comment letter (this "Comment Letter") in response to your request for comments regarding the re-proposed rule on credit risk retention (the "Re-Proposal"), [1] which was issued jointly by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the Securities and Exchange

[1] 78 Fed. Reg. 57928 (2013).

Commission and the Department of Housing and Urban Development (collectively, the "Agencies") pursuant to Section 941(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank").

MetLife, Inc. and its insurance affiliates (collectively, "MetLife") invest in structured finance securities primarily to fund core insurance products, which provide critical financial protection for over 90 million customers worldwide. As of June 30, 2013, the general accounts of MetLife's insurance companies held approximately $69 billion of structured finance securities, comprised of $36 billion of residential mortgage-backed securities ("RMBS"), $17 billion of commercial mortgage-backed securities ("CMBS") and $16 billion of asset-backed securities ("ABS"). Given the relevance of structured finance securities in our overall investments portfolio, MetLife has a vested interest in the long-term soundness of this market.

We are also responding to your request for comments as one of the largest holders and originators of real estate loans in the United States. As of June 30, 2013, MetLife's real estate loan portfolio totaled $54 billion, which is comprised of $39 billion of commercial mortgages, $13 billion of agricultural mortgages, and $2 billion of residential mortgages.

While we are encouraged to see the Agencies move forward to implement measures designed to better align incentives between issuers of and investors in securitized products, we are disappointed that some of the requirements contained in this Re-Proposal are looser than the original proposal on credit risk retention (the "Original Proposal").[2]

Most importantly, with respect to risk retention for RMBS, we are concerned about the proposed alignment of the Qualified Residential Mortgage ("QRM") and the Qualified Mortgage ("QM") definitions as set forth in the Re-Proposal. It is MetLife's position that the new standards to qualify a loan for the QRM exemption from the risk retention requirement are too loose, and will deprive investors of key protections set forth in the Original Proposal, which effectively aligned issuer and investor incentives – a much-needed change in the RMBS market.

In the sections below, we first comment on aspects of the Re-Proposal that relate to all securitized products, and we then provide specific commentary on items related to RMBS and to CMBS. We also discuss our concerns and recommendations with respect to the rules as they apply to sponsors of securitizations involving collateral consisting of the securitizer's own unsecured obligations, rather than obligations of third parties.

[2] 76 Fed. Reg. 24090 (2011).

Recommendations Related to All Securitized Products

Fair value basis for retention calculation

MetLife supports the Re-Proposal's requirement for the use of fair value as the basis for determining the risk retention amount when securities have been issued (in the aggregate) at or above par value. We make the following key observations in this regard:

1. In order to properly determine the risk retention amount, regardless of whether ABS were issued above, at, or below par value in the aggregate, the base amount for calculating risk retention should be the greater of (x) fair value and (y) par value.

2. The base amount should apply to all forms of risk retention, not just horizontal retention. This is both for simplicity reasons and to reflect the fact that, economically, the size of the vertical retention should be at least the same as the horizontal retention given the somewhat lower risk associated with the former.

We also support disclosing to investors the key components that were used to determine fair value. Such disclosure would provide transparency regarding the general reasonableness of the fair value assessment.

Rule compliance monitoring and enforcement

We respectfully request the Agencies to further consider how compliance with the final risk retention rules will be monitored and enforced and how these responsibilities will be allocated and coordinated among the Agencies. In our view, approaches to monitoring and enforcement should be carefully developed to avoid unintended consequences that may burden investors – the constituency that these rules are designed to protect – or could negatively impact market liquidity. For example, a non-compliant securitization could affect the pricing or liquidity of securities issued in such securitization, especially when there is no corrective action required to be taken by the sponsor of the securitization.

Support for vertical risk retention

As we indicated in our June 2011 comment letter on the Original Proposal (the "MetLife Comment Letter on the Original Proposal")[3], we believe the vertical form of risk retention is the most effective solution for the industry for the following reasons:

- Vertical risk retention aligns the incentives of the sponsor with those of all investors, rather than having an outsized alignment with the incentives of junior investors, who may have conflicting interests with senior investors.

[3] *See* Letter from Jonathan L. Rosenthal, Senior Managing Director – Core Securities, Metropolitan Life Insurance Company, to the Agencies, dated June 27, 2011.

- Vertical risk retention is the retention alternative with the lowest cost of capital for sponsors and the lowest likelihood of leading to consolidation issues.

We recognize the differences across ABS asset classes and understand the need for alternatives such as a combination between vertical and horizontal risk retention (subject to a minimum percentage for the vertical tranche). We also believe that a static cash-collateralized reserve account that is fully funded at the inception of the transaction may be considered risk retention, as set forth in the Re-Proposal, provided that it has a first loss position in the transaction's waterfall.

Synthetic securitizations

We note that the Re-Proposal does not address risk retention for synthetic securitizations. In the absence of rules to cover this market, there is the potential unintended consequence of fostering a synthetic market away from the current cash market. An example is the CDO/CLO sector where there is a pre-existing synthetic market. In these situations, sponsors might determine it is economically advantageous to avoid the cost of risk retention by issuing in the synthetics market.

International convergence

As a final general comment, we note that non-U.S. securitization transactions are an important part of the investment portfolios of many U.S. institutional investors, including MetLife. We are concerned that some of the re-proposed rules that apply to non-U.S. securitizations may conflict with existing risk retention rules in other jurisdictions (e.g. European Union Capital Requirement Directive.), which may prevent non-U.S. issuers from offering this valuable investment alternative to U.S. investors. We respectfully request that the Agencies coordinate with their international counterparts to address any conflicts between applicable risk retention rules that could disrupt the active market for non-U.S. securitizations.

Recommendations for RMBS

As indicated earlier, MetLife is disappointed by the proposed alignment of the QRM and the QM definitions as set forth in the Re-Proposal. In our view, this approach results in an overbroad QRM definition and does not adequately ensure that originators and issuers will retain "skin-in-the-game" on products where the underwriting process and diligence are key aspects of risk management.

As noted in the Re-Proposal, a number of commenters argued that the narrower QRM definition contained in the Original Proposal "would prevent recovery of the housing market by restricting available credit, and as a result the number of potential homebuyers."[4] We believe this argument is neither accurate nor persuasive. Unfortunately, the Agencies appear to have accepted this argument because the new QRM definition set forth in the Re-Proposal is now broad enough to capture almost all

[4] *See* the Re-Proposal at 57988.

residential mortgage loans. While the Re-Proposal states that Section 15G of Dodd-Frank provides that the QRM definition is not permitted to be broader than the QM definition – hence the alignment of the definitions in the Re-Proposal – nothing contained in Section 15G would prohibit the Agencies from implementing a QRM definition (such as the one contained in the Original Proposal) that is more restrictive than the QM definition. MetLife continues to believe that the narrower QRM definition would better protect RMBS markets from excessive risk taking and, therefore, would be the most beneficial to home owners, sponsors, and investors.

Unfortunately, instead of QRM being an exception for very high-quality loans as originally intended, the new definition ensures that all but less than average-quality mortgage loans could fit under the QRM umbrella. We do not believe this was the intent of risk retention or QRM, and now results in a "bright line" for lenders that will ultimately define underwriting guidelines for most sponsors.

We believe risk retention is appropriate for those loans where the underwriting process is essential to the quality of the loan. We do agree with many commentators that borrowers with lower down payments or a credit record with limited bad marks may still be acceptable credit risks. However, the underwriting process, rather than any specific quantitative factor, is the key risk management tool for these types of borrowers. In our view, the best way to ensure that sponsors manage these qualitative risks and maintain a disciplined lending process is to require that they retain a portion of the risk of the loans that are included in RMBS securitizations that they sponsor.

For example, a "low down payment mortgage loan" should require strong underwriting processes and checks based on multiple factors to ensure that a borrower has both the willingness and the ability to repay the loan. Likewise, a borrower with recent marks on their credit report may still be a reasonable credit risk, but the lender should perform additional due diligence to analyze the specific credit history of the borrower in order to make a good credit decision.

In our view, in order for risk retention to have a meaningful impact on the quality of RMBS, the QRM exemption must not permit low-quality loans. By excluding lower-quality loans from QRM, risk retention would align the interests between sponsors and investors and would enforce the incentive for sponsors to remain diligent regarding the underwriting process.

A hallmark of lower-quality loans is underwriting that is more reliant on subjective determinations (such as an income/asset verification process or an analysis of past credit management) because of the lower credit quality of the borrowers. In order for risk retention to be effective in RMBS, the QRM exemption should include only very high-quality loans where objective guidelines play a much larger role in the underwriting decision due to the higher credit quality of the borrowers.

Moreover, as an institution, MetLife's demand for securitizations backed by QRM loans that have low down payments or imperfect credit histories would likely be markedly lower. As discussed above, we would not be comfortable with the risk of a "low down payment mortgage loan" where the lender does not keep some "skin-in-the-game".

Recommendations for CMBS

<u>Operating Advisor</u>

We are encouraged to see that the Agencies have retained the operating advisor requirement for CMBS transactions that use the third-party risk retention option. MetLife offers the following observations:

1. *Operating advisor should be required for all transactions:* For the following reasons, MetLife believes that the operating advisor requirement is a very helpful governance mechanism that should be expanded to cover all CMBS transactions (not just those relying on the third-party risk retention option):

    a. Regardless of which party is satisfying the risk retention requirement, there is a significant misalignment of incentives between B-piece buyers that control special servicing decisions and all other investors. Requiring an operating advisor for all transactions would enhance the positive impact that risk retention can have in aligning incentives in CMBS transactions.

    b. Requiring an operating advisor for all transactions would improve the uniformity in the CMBS market and create an even playing field for all transactions regardless of who is the retaining party. We also note that current market practice is generally to have an operating advisor, but incorporating the provisions in the Re-Proposal would introduce much-needed governance enhancements across all deals.

2. *Recommendation to replace the special servicer:* We believe it is extremely important that, as proposed, the operating advisor retains the ability to recommend the replacement of the Special Servicer when the latter has not acted in the best interest of all investors. However, for this requirement to be truly effective, the Agencies should consider the following:

    a. Providing operating advisors with safe harbor protection if they decide to recommend a special servicer replacement so that, except in the case of gross negligence, fraud or willful misconduct, operating advisors would not be subject to the threat of lawsuits. Without such protection, operating advisors will be disincentivized from making such recommendations.
    b. Requiring the maintenance of an investor registry so that investors can be easily contacted if the operating advisor makes a replacement recommendation that requires a vote.
    c. Adding to the 5% minimum quorum requirement for a vote to replace the special servicer a requirement that no less than 3 unaffiliated investors participate in the vote.

d. Defining a process for selecting a replacement special servicer, where the B-piece buyer does not have the ability to reappoint the original special servicer or an affiliate to this role.

3. *Trigger for consultation rights:* The Re-Proposal states that the operating advisor's consultation rights take effect once the B-piece buyer's principal balance is 25% or less of the original amount. We request that the Agencies clarify that this threshold should be calculated after accounting for appraisal reductions (not just realized losses), which would be consistent with current market practice. Otherwise, special servicers would be conflicted because they have the ability to time loss realizations that could trigger the operating advisors' consultation period.

Non-conduit CMBS transactions

MetLife agrees with the Agencies' decision not to create an exemption for non-conduit CMBS transactions. We believe risk retention is an effective tool to align sponsors' and investors' interests, regardless of the type of CMBS transaction in which it is applied. Unfortunately, there are many examples of non-conduit CMBS transactions that were aggressively underwritten in the previous economic cycle, reflecting the prevailing misalignment of interests between sponsors and investors.

Qualifying Commercial Real Estate Loans ("QCRE")

As a matter of principle, we believe the QCRE exemption should only be available for a very small population of top-quality CRE loans. For this reason, we are very concerned that the Re-Proposal has loosened the debt service coverage ratio ("DSCR") and combined loan to value ("CLTV") parameters from the Original Proposal – to 1.5x DSCR (from 1.7x) and 70% CLTV (from 65%) - because these changes could effectively undermine the risk retention rules for CMBS.

It is our understanding that the QCRE exemption set forth in the Original Proposal was intended for only the highest quality loans. Under the Original Proposal, a significant number of leased CRE transactions would have been subject to 1.7x DSCR because they would not have been eligible for 1.5x DSCR, which was only available where properties involved at least 80% triple-net leases. However, by eliminating the triple-net lease requirement, the Re-Proposal has effectively reduced the required DSCR for leased CRE from 1.7x to 1.5x. Unfortunately, this is not a high bar for a sponsor to meet. In fact, based on our own review of reported data available on Intex,[5] some of the key underwriting criteria contained in the Re-Proposal for QCRE — 1.5x DSCR and 70% CLTV — are consistent with approximately the bottom quartile of loans in CMBS deals issued since 2010.[6]

[5] *See* Intex US CMBS Deal Model Library.
[6] We note that, in our experience, CLTV is not usually defined in sources that report on CMBS data, including Intex. Therefore, we have used reported data on LTV as a substitute for CLTV in this context.

Accordingly, we recommend that the DSCR and CLTV criteria for QCRE be made consistent with the spirit of an exemption that is reserved for only the highest-quality CRE loans. As a reference, and based on our own review of reported data available on Intex,[7] approximately the top decile of CMBS loans securitized since 2010 had both a 2.4x DSCR and a 52% CLTV.[8]

As the Agencies consider the terms of the final rule on credit risk retention, we respectfully request that the QCRE exemption is not loosened any further. Specifically, we caution the Agencies against permitting loans with "interest only" periods or reducing the minimum permissible term of loans to less than 10 years. We believe that any such loosening would open the door further to the inclusion of lower-quality loans than is warranted under the QCRE exemption.

Number of Third-Party Purchasers

Finally, we observe that the Re-Proposal allows up to two third-party purchasers to fulfill the risk retention requirement in CMBS transactions. This is another area that we believe diminishes the rule's effectiveness. We believe the practical effect of this change is that the magnitude of "skin in the game" that a single third-party purchaser would have otherwise had will be significantly diluted. As a result, the incentives of such third-party purchasers are likely to be misaligned with those of investors. We caution against further easing of the requirements – such as allowing the two third-party purchasers to satisfy the retention requirement through a senior/subordinated structure instead of the Re-Proposed *pari passu* structure. MetLife is concerned that any further easing of the requirement may render risk retention ineffective in CMBS.

Exemption for Securitizations Involving Collateral Consisting of the Securitizer's Own Unsecured Obligations

MetLife fully supports the intent of the risk retention rule as it relates to the ABS, CMBS and RMBS markets. Consistent with the MetLife Comment Letter on the Original Proposal, we note, however, that the risk retention rule may unintentionally capture certain transactions that are not part of the ABS market as conventionally defined.[9] These transactions, which do not involve the securitization of an interest in any assets other than an obligation created by the securitizer itself, are commonly utilized by insurance enterprises, and include the issuance of trust securities, as well as securities backed by obligations uniquely issued by insurance companies such as funding agreements and surplus notes. MetLife supports an exemption from the risk retention rule for such transactions.

Such transactions generally involve the issuance of securities to investors by a special purpose vehicle ("SPV") and the use of the proceeds to acquire direct, unsecured obligations of the securitizer itself or its affiliates that have terms similar to those of the

[7] *See* Intex US CMBS Deal Model Library.
[8] *See* supra note 6.
[9] *See* the MetLife Comment Letter on the Original Proposal at 13.

securities issued by the SPV. In such cases, the investor does not acquire an indirect interest in receivables or other assets of a third party the quality of which can be monitored by the securitizer. Applied in these circumstances, the risk retention rule would not address in any way the goal of providing securitizers with an incentive to monitor and ensure the quality of third party assets underlying a securitization transaction and thereby align the interests of the securitizers with the interests of investors.
Like other insurance enterprises, MetLife utilizes, to the benefit of its policyholders and other stakeholders, financing structures that would be unnecessarily burdened under the proposed risk retention rule. These financing structures do not serve to transfer third party risk accumulated by MetLife to investors by bundling obligations and selling them. Instead, the risk they represent is recognizable to investors as a risk related directly to the enterprise.

Based on these considerations, MetLife respectfully requests that the Agencies add a general exemption to the risk retention rule to exempt from the application of the rules any securitization transaction in which the Collateral, as defined in §___.2, consists primarily of unsecured direct obligations of the Securitizer, as defined in §___.2, or its affiliates, in structures such as those described above.

* * *

Thank you in advance for providing MetLife with the opportunity to comment on the risk retention rule. If you have any questions concerning the views or recommendations that MetLife has expressed in this Comment Letter, please feel free to contact Jonathan Rosenthal of our Investments Department (at 973.355.4777; jrosenthal@metlife.com) or Jason Cole of our Government and Industry Relations Department (at 202.785.2252; jcole5@metlife.com).

Respectfully submitted,

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