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Ms. Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 205651

Re: Docket No. OP-1254

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Attention: Comments/OES

Office of the Comptroller of the Currency
250 E Street, S.W.
Mail Stop 1-5
Washington, DC 20219

Re: Docket No. 06-06

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, N.W.
Washington, DC 20552

Re: No. 2006-20

Ms. Nancy N. Morris, Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File Number S7-08-06

Re: Proposed Interagency Statement on Sound Practices Concerning Elevated Risk Complex Structured Finance Activities

Ladies and Gentlemen:

I am submitting these comments in response to the agencies' request for comments on their proposed Interagency Statement on Sound Practices Concerning Elevated Risk Complex Structured Finance Activities. My comments are based, in part, on my hands-on experience in the establishment of and participation in a complex structured finance transaction ("CSFT") committee of a major multinational financial institution. The revised proposal is a significant improvement over the prior proposal.

One of the Statement's main strengths is that it provides financial institutions the flexibility to carry out the recommended sound practices in a manner consistent with each institution's business. The term "CSFT" is not defined, and that is appropriate. What is a complex structured finance transaction for one institution might not be for another. "Elevated risk" is not defined, and that also is appropriate. Similarly, what is an elevated or heightened risk for one institution might not be for another.

The appropriate risk management structure will also vary depending on the characteristics of the institution. The recommended sound practices can be carried out within an institution's existing risk-management framework. While the general principle that the control area should be independent of the profit center is appropriate as a general principle, the identity of personnel or groups that exercise that control should be determined by management. For example, because of its smaller size, a United States branch or agency of a foreign bank might not have separate profit centers, but nonetheless, the branch or agency may have an "independent" risk management function. This part of the Statement is too prescriptive. When the Statement refers to "control areas that are independent of the business line(s) involved in the transaction",¹ it suggests that the "independent" staff should not be within the profit center. Some institutions

¹ 71 Fed. Reg. 28326, 28333 (May 16, 2006).

might desire to structure a review mechanism at the profit center level and require further review for some transactions at a more senior level of the organization.

In sum, the appropriate structure to identify, analyze, and authorize an elevated risk CSFT will vary from institution to institution depending on the institution's size, business focus, and management depth. It may be useful for the agencies to state more explicitly in their Statement that the definition of CSFTs should be a part of each institution's risk management process. The agencies should avoid setting forth prescriptive examples.

The Statement identifies as a transaction presumptively being of elevated risk one "designed or used primarily for questionable accounting, regulatory or tax objectives."² Accomplishing accounting, regulatory or tax objectives is not inappropriate as such and whether they are questionable begs the question. Frequently in complex transactions there may be no clear answer as to whether the transaction complies with all applicable rules. Indeed, expert opinion may differ, and the particular accounting, regulatory, or tax purpose may constitute only one of the business objectives of the complex transaction. There is no reason why institutions should not be able to apply the usual risk/reward analysis in considering a transaction, accepting that the risks – reputational and legal – may transcend economic and credit considerations. For this reason, I do not believe that this is a helpful example. I suggest that either that "questionable" as used in the example above be clarified or that the example be deleted.

As noted above, on occasion, a financial institution structuring a transaction may learn that different firms have differing opinions on whether a transaction complies with a given rule. It should be sufficient for that institution to inform its customer of the differing interpretations and for the customer to decide whether to proceed. The Statement should not contain a subliminal message that it is not appropriate to proceed where the law or rule is not perfectly clear.

The Statement provides: "Institutions should not conclude that a transaction identified as being an elevated risk CSFT involves minimal or manageable risks solely because another financial institution will participate in the transaction...."³ Whether the transaction is a loan or a

² Id. at 28332.

³ Id. at 28332.

June 1, 2006

Page 4

heightened risk CSFT, an institution participating alongside others, including the institution leading the transaction, should perform adequate due diligence. However, the participating institution should be able to rely on the expert advice of recognized attorneys and accountants brought into the transaction by the lead. By recommending that the participant "carefully" consider the opinions prepared, are the agencies suggesting a legal standard of care or that the institution must employ its own experts?

The Statement details suggested documentation requirements when a transaction is reviewed by senior management. One item may be problematic. If senior management decides to impose a condition, the condition should, of course, be documented. I question whether it is desirable to set out the reason for the condition. Recognizing that these documents may become the subject of discovery, it may not be in the best interest to document a reason. Indeed, there may be no single reason but separate reasons held by each member of management.

Finally, as I read it, the Statement is not intended to suggest that a transaction should not proceed if, after review, management determines that the risks are acceptable. United States financial institutions have been leaders in financial innovation. There is nothing improper with a cutting-edge transaction with significant risks that has been scrutinized by experts. The appropriate level of management should determine whether the game is worth the candle. After concluding that a transaction involves significant legal or reputational risks, senior management may nonetheless conclude that the institution should engage in the transaction without any alteration if the risks are acceptable.

Respectfully submitted,



Ernest T. Patrikis

ep/rw/gc