Superior℠ Bank FSB

"Working With You"

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President, CEO

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Manager, Dissemination Branch
Information Management and Services Division
Office of Thrift Supervision
1700 G Street, N.W.
Washington, DC 20552
Attn: Docket No. 2000-70

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Docket No. 00-17
Communications Division, Third Floor
Office of the Comptroller of the Currency
250 E Street, S.W.
Washington, DC 20219

Robert E. Feldman, Executive Secretary
Attn: Comments/OES
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, DC 20429

Re: Notice of Proposed Rulemaking: Residual Interests in Asset Securitizations or Other Transfers of Financial Assets Published at 65 Fed. Reg. 57993 (September 27, 2000)

Dear Ladies and Gentlemen:

Superior Bank FSB appreciates the opportunity to submit these comments on the above-referenced proposed rule ("the proposal"). The proposal, issued collectively by the Office of Thrift Supervision, the Office of the Comptroller of the Currency, the Federal Reserve System, and the Federal Deposit Insurance Corporation ("the agencies"), would amend the capital treatment of certain retained residual interests and securitization assets created in securitization activities, as well as impose significant portfolio limitations on such retained assets.

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Superior Bank engages in the nationwide origination, purchase, and servicing of consumer finance loans, consisting primarily of one-to-four family residential mortgage loans, with many of our customers not conforming to traditional credit standards or characteristics. Since January 1, 1993 Superior has funded its mortgage originations primarily through quarterly issuance of credit-enhanced, triple-A asset-backed securities. From 1985 until December 31, 1992 mortgage originations were funded through a subsidiary of our parent holding company with whole loan sales to banks from 1985 through the end of 1989 and with securitizations from January 1990 until December 1992.

Superior and its parent holding company have been in the business of originating and securitizing these mortgage loans for over a decade and have developed stable securitization structures that have stood the test of time and market volatility. We are proud to be offering single family residential home loans and refinancings to many borrowers who cannot access more traditional financing sources. Superior's securitization activities have generated the type of residual interests and securitization assets that would be covered by the proposal.

We are strongly of the view that the present proposal is deficient in several critical respects:

* It adopts an inappropriate "one-size-fits-all" approach to a problem that is complex and institution-specific.

* It imposes requirements that are excessive and damaging.

* It will have an adverse impact on both the availability and cost of credit for nonconforming borrowers such as those Superior lends to - effectively banishing these borrowers from the insured banking system.

* It fails to provide for grandfathering and transition rules that are essential to avoid unfairness and unnecessary harm.

Each of these points is discussed further below.

1. The proposal would inappropriately impose a uniform response to issues that can and should be addressed on an individualized basis.

The fact that some institutions may have experienced losses resulting from assets created in their securitization activities and exposed the Federal Deposit Insurance funds to losses does not, we believe, provide an adequate reason for subjecting all institutions that engage in such activities to substantial new capital requirements and portfolio restrictions. The present proposal imposes requirements that take no account of the circumstances of individual institutions or differing securitization structures, the risks from which vary significantly.

In December 1999, the agencies issued guidance on asset securitization activities that highlighted the importance of institutions ensuring that they have in place adequate risk management, modeling and valuation methodologies governing securitization activities.

The individualized supervisory approach reflected in the December 1999 guidance is the appropriate way to address this set of issues. We fully support the content and spirit of the December 1999 guidance.

If the agencies' December 1999 guidance is adhered to, the new restrictions in the current proposal are unnecessary and inappropriate. They would impose stringent capital limits and penalty capital requirements on institutions whose practices do not warrant any such treatment. At the same time, they will not appropriately correct the deficiencies that exist in institutions that do not engage in adequate valuation and risk management practices in connection with their securitization activities.

We understand that, in international discussions aimed at revising the overall risk-based capital framework, the banking agencies are seeking to move away from a "one-size-fits-all" approach and to utilize instead a case-by-case evaluation of each institution's risk-based capital needs based on the institution's business profile and risk management approach. There is, we believe, no good reason to move in the opposite direction in the present proposal.

2. Even if the imposition of uniform requirements were warranted, the specific terms of the proposal still would be excessive and harmful.

The proposal would have the effect of requiring less capital if a loan remains on the books than if the loan is securitized and sold. This introduces inequities, inefficiencies and a bias against the general use of securitization.

Dollar-for-dollar capital requirements far above the present required capital levels is a penalty risk weight. There are no new risks introduced when a bank transfers a loan off the balance sheet unless the valuation and management of any retained interest is deficient. As already noted, issues relating to appropriate valuation and management of retained interests can and should be addressed on an individualized basis under existing agency guidance.

Existing risk-based capital regulations also take appropriate note of, and provide lower capital requirements for, the secured nature of single family residential mortgage loans. We note that the proposed capital regulations in effect revoke the favorable capital treatment presently afforded to residential, owner-occupied mortgage loans. Further, revoking the favorable present risk-based capital treatment for residential mortgage loans would effectively be in direct conflict with decades of public policy which has encouraged thrift institutions and federal savings banks to make mortgage financing more available and at lower costs to consumers.

The risk-based capital regulations were adopted by the banking agencies (and maintained by OTS) in accordance with a Congressional mandate that was intended, not to impose a dollar-for-dollar capital requirement on certain assets, but to ensure that an institution generally would carry a reasonable amount of capital against an asset and to reduce capital requirements whenever the amount of capital required was greater than it could potentially lose. The present proposal would be squarely inconsistent with this objective by presuming that all retained residual interests and securitization assets are worthless when in fact these assets represent net monthly cash flows of interest and principal collected from borrowers emanating from secured mortgage obligations.

Moreover, by eliminating the use of existing risk based capital rules which allow for adjustments related to the benefit of mortgage security and reasonable reductions whenever a low-level recourse approach is warranted, for a focus on singular, adverse capital treatment of residual assets, the proposal would drive banks away from securitization. There is a meaningful place in the business plans of financial institutions for use of securitization structures which have provided an efficient and beneficial means of funding the origination of mortgage credit, managing risks, and meeting customer needs over the past decade.

3. The proposal will harm a class of borrowers whose interests should be of ongoing concern - those borrowers who have difficulty obtaining credit.

The agencies have noted in the proposal that they are particularly concerned about residual interests that are generated from the securitization of certain assets, such as low-quality loans. Indeed, securitization and the creation of residual interests often play a vital role in funding which allows for the creation of viable lending programs to non-conforming borrowers.

There has been much talk lately about the risks of so-called "sub-prime" lending. A supervisor may of course be more comfortable when banks make loans only to highly rated borrowers with conforming characteristics and with proven track records. Clearly, residual interests generated from sales of loans that have been made to sub-prime and non-conforming borrowers can present greater valuation challenges, which if mishandled can be particularly dangerous during periods of market volatility. For this reason, it is not surprising that many institutions, particularly those that have entered this business relatively recently, have encountered problems.

However, the appropriate public policy response is not to drive non-conforming borrowers out of the banking system. Doing so would have two effects. First, people who need a mortgage to own or keep their own home but have nonconforming credit histories will not be able to obtain mortgage credit from regulated institutions that are supervised and have high standards of behavior. Second, the sources of lending that will be open to them will require much higher rates and /or unacceptable or potentially predatory terms.

The basic policy objectives reflected in the fair lending laws and the Community Reinvestment Act require that the agencies give substantial weight to the likely adverse impact the present proposal would have on these categories of non-conforming or sub-prime borrowers.

4. If the proposal were to be adopted, prior transactions must be accorded grandfathering treatment and a suitable transition period must be provided.

For the reasons already indicated, we believe the appropriate course is for the agencies to withdraw the present proposal in its entirety and instead address the issues presented by residual interests and securitization assets in any institution in an individualized manner suited to the particular institution.

If, contrary to our views, the agencies were to adopt the present proposal in whole or in significant part, then at a minimum the agencies must provide for grandfathering of existing residual interests and securitization assets resulting from securitizations entered into prior to the time the new rule becomes effective, and for a substantial transition period to allow institutions to come into conformity with these new capital requirements.

The grandfathering of assets already on the books would clearly be required as a matter of basic fairness. Institutions that entered into transactions in good faith reliance on the prior rules should not be subjected retroactively to drastically different capital treatment. They obviously cannot now undo past transactions that they might have done differently, or might not have done at all, if they had known of the capital penalties that the transactions would entail.

Moreover, unless appropriate grandfathering treatment and transition rules are provided, the adoption of the proposal will further cause damage to the environment for these assets in the capital markets and cause unnecessary losses that are likely to transform potential problems in certain specific institutions into a problem effecting a much larger number of institutions - thereby creating unnecessary harm to all of those institutions and unnecessary difficulties for the agencies that regulate them.

Without grandfathering and reasonable transition rules, the one-size-fits-all approach will have deleterious effects on the capital markets, thereby precipitously depressing the value of residual interests and securitization assets currently held by insured institutions. The inevitable result will be to impair balance sheets and safety and soundness without regard to the quality of individual assets and without regard to the demonstrated capabilities of institutions which have effected valid securitization programs.

If the agencies determine to adopt the present proposal, only suitable grandfathering and transition provisions can provide institutions with the time they deserve to adapt to the new requirements without facing such unnecessary problems and significant adverse effects of the present proposals.

5. Conclusion.

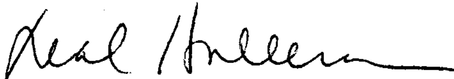
We understand the agencies' concerns about potential risks that retained residual interests and securitization assets can pose to financial institutions, and in turn, to the FDIC. However, the current proposal, which would simultaneously prevent the use of current risk based capital rules as well as impose a highly restrictive concentration limit, seems to us to be an overreaction that will have adverse consequences for many financial institutions and will drive borrowers with non-conforming profiles or imperfect credit records to unregulated lenders. The fact that there have been some egregious cases of deficient management of retained interests and securitizaton programs does not justify subjecting the system as a whole to rules that ignore the above concerns.

Institutions with proven track records and depth of expertise in securitization activities have a valid and valuable role in the financial marketplace. At Superior Bank, we have given large numbers of borrowers an opportunity not only to own their own homes, but also to prove they can be creditworthy. And we have done so without taking on undue liquidity, credit, or interest rate risk.

We urge the agencies to withdraw the proposed rule and emphasize the December 1999 Securitization Guidance instead. If, contrary to our views, the proposed rule is adopted, we urge that provisions be made to grandfather existing residual interests and securitization assets that are now on the books and to allow institutions to establish a long-term transition plan for meeting the new capital requirements.

This comment letter has been submitted on behalf of the Board of Directors of Superior Bank FSB.

Sincerely,



Neal T. Halleran
President and Managing Officer

cc: Board of Directors, Superior Bank FSB