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September 12, 2008

Ms. Florence E. Harmon
Acting Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Release Nos. 33-8940; 34-58071 (File No. S7-18-08);
Release No. 34-58070 (File No. S7-17-08);
Release Nos. IC-28327; IA-2751 (S7-19-08)

Ladies and Gentlemen:

This letter is submitted on behalf of the Committee on Federal Regulation of Securities and the Committee on Securitization and Structured Finance (the "Committees") of the Section of Business Law of the American Bar Association in response to the request for comments by the Securities and Exchange Commission (the "Commission") in its July 1, 2008 releases referenced above, Release Nos. 33-8940; 34-58071 (the "Securities Act Release"), Release Nos. IC-28327; IA-2751 (the "Investment Company Release"), and Release No. 34-58070 (the "Exchange Act Release," and together with the Securities Act Release and the Investment Company Release, the "Proposing Releases").[1] This letter focuses on the Proposing Releases as they relate to or otherwise affect asset-backed securities ("ABS"). An additional letter from the Committee on Federal Regulation of Securities addressing the non-ABS aspects of the Proposing Releases will be submitted separately.

The comments expressed in this letter represent the views of the Committees only and have not been approved by the American Bar Association's House of Delegates or Board of Governors and therefore do not represent the official position of the American Bar Association (the "ABA"). In addition, this letter does not represent the official position of the ABA Section of Business Law, nor does it necessarily reflect the views of all members of the Committees.

[1] 73 Fed. Reg. 40088 (July 11, 2008).

As we noted in our July 28, 2008 comment letter to the Commission on Release No. 34-557967, Proposed Rules for Nationally Recognized Statistical Rating Organizations (the "June 16 Release")[2], we agree with the Commission that credit rating agencies have played a significant role in the recent crises in the capital markets, and that certain regulatory enhancements, including increased regulation of conflicts of interest and requirements for better track-record reporting by the credit rating agencies, may provide significant long-term benefit to the markets. Improving the quality, objectivity and transparency of such credit ratings will be an important aspect of economic recovery. The June 16 Release addressed core problems with the ratings process, and even where we did not support the Commission's proposed solutions we supported its efforts and tried to suggest alternative approaches.

On the other hand, in discussing the Commission's Proposing Releases to minimize the use of ratings by nationally recognized statistical rating organizations ("NRSROs") in its rules, our drafting committee has found itself struggling with the fundamental premise. NRSRO ratings provide an important objective measure of the credit risk of rated securities, and while they are neither flawless nor appropriate as the sole means by which to evaluate an investment, we are not aware of any reasonable alternative that provides better objective guidance as to risk. Nor, do we feel, has the Commission proposed a viable alternative to the use of credit ratings. In debating the relative burdens and benefits of changes the Commission now seeks to make, we have felt consistently that the Commission's efforts to eliminate its reliance on NRSRO ratings in its rules would lead to more subjective risk assessments, greater challenges to liquidity in the structured finance markets, and erosion of the value of public registration of the offer and sale of securities without any corresponding benefit to investors. The Commission is proposing a substantive overhaul of its rules to address an issue essentially of perception, and we are particularly reluctant to see such fundamental changes adopted at a time when the current market crisis has already created both significant obstacles to capital formation and significant uncertainty about the safety of investments.

We have two primary areas of concern:

- First, that the proposed rules will have the effect of causing significant amounts of structured finance securities to be issued privately or offshore, rather than through the public registration process which would have the effect of reducing transparency at a time when there is a greater call for it; and
- Second, that, notwithstanding the current problems with the credit rating agencies the Commission has identified, the elimination of references to such ratings effectively will eliminate all objective indicia of credit quality and will provide greater opportunity for abuse.

We understand the Commission's concern that its use of NRSRO ratings in its rules may have had the effect of bestowing on those credit rating agencies the imprimatur of the Commission. But we believe that the role of credit ratings in the structured finance markets was

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[2] 73 Fed. Reg. 36212 (June 25, 2008).

already well established prior to the inclusion of NRSRO ratings for these securities in the Commission's rules, and we do not believe that the Commission's use of references to such ratings has materially enhanced that role. With respect to asset-backed securities, for instance, an investment grade credit rating has been an essential component of structuring since before ABS became eligible for registration on Form S-3 and before the adoption of Rule 3a-7. We note, as well, that we believe the use of NRSRO ratings has become so pervasive in regulatory standards, investment guidelines, and the like, that the elimination of them from the Commission's rules will have no discernible effect on investors' need to invest in securities bearing such ratings.

In addition to the Commission's proposed rules under the June 16 Release, there are a number of ongoing initiatives—within the securitization industry, among investors, and within the rating agencies themselves—that are intended both to enhance the reliability of ratings and, in some instances, to diminish undue reliance on those ratings. Our drafting committee feels that, given these initiatives, it is premature to conclude that NRSRO ratings are irreparably broken. On the contrary, we are hopeful that credit ratings will over the long term again become an invaluable investment tool when viewed with appropriate circumspection and independent investor analysis. We would prefer to see the Commission take an approach that allows the implementation of these initiatives, while continuing to evaluate the role of NRSRO ratings in its rules.

Form S-3 Eligibility for Asset-Backed Securities

The Commission has proposed, among other things, replacing the current requirement that asset-backed securities have an investment grade rating from an NRSRO with a restriction that such securities be offered only to qualified institutional buyers ("QIBs") and in minimum denominations of at least $250,000. We do not support this proposal.[3]

As we discuss above, although we understand the issues that have been raised by the Commission with regard to undue investor reliance on credit ratings in certain of its rules, we do not feel that removing references to NRSRO ratings from the Commission's rules is in the best interest of the investors or the markets. We understand that these ratings have not provided the indicia of quality for certain types of structured finance securities that they were intended to provide. We understand, further, that there are significant failures of the rating process that must be addressed. As we have previously discussed, we support the Commission's efforts to strengthen the integrity of the credit rating process; to educate investors about the risks in credit ratings, especially of asset-backed securities; to more closely monitor NRSRO track records; and to encourage competition and new credit rating agencies. But we believe that credit ratings continue to provide the best available source of third party evaluation of creditworthiness of investment securities, and are the best means for determining qualification to register on Form S-3. In other words, we support fixing the procedures and disclosure about the ratings themselves,

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[3] The Commission has also proposed making correlative changes to Rule 415, as that rule applies to delayed offerings of mortgage-backed securities. For the same reasons we articulate with respect to the proposed changes to Form S-3 Eligibility for Asset-Backed Securities, we do not support such changes.

without altering the ways in which such ratings are used. But we believe these proposals would have the incongruous effect of discouraging registration of asset-backed securities at a time when the transparency and protection of the public registration process, including enhanced disclosures about ratings, are important to rehabilitation of the structured finance markets.[4]

We are reluctant to see the Commission change its important and long-standing position that registration has a consistent meaning across all types and classes of securities, and that securities for which the offer and sale have been registered with the Commission are freely tradable without regard to investor qualifications or other restrictions.[5] Such registration has never been indicative of the suitability of particular investments for particular investors, but has only indicated that the issuer has completed the Commission's registration process, especially with respect to required disclosures and assumption of liabilities. Although we agree that there can be complexities to structured finance securities that are difficult for inexperienced investors to grasp, this is true also of a variety of other investments, including common and preferred stock and high-yield debt securities. The Commission appears to be making a suitability judgment here that we feel is both unjustified and is itself potentially misleading as to the risks of all the other securities for which the Commission does not impose such restrictions.

In addition, we note that the difference between registration on Form S-1 and registration on Form S-3 in terms of line-item disclosures is *de minimis* for asset-backed securities, but the difference in speed of market access—especially for experienced issuers with established securitization programs—is substantial. The Commission certainly has the ability to revisit its own procedures for selecting registration statements on Form S-3 for review and for declaring those registration statements to be effective prior to the first takedown, if one of the Commission's concerns reflected in these proposals is the ability to enhance Staff review of registration statements.[6] But at a time when lack of liquidity in the structured finance markets is

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4 The Commission notes, elsewhere in the Securities Act Release, that it "believes that, for the most part, non-convertible securities that were issued in a registered offering constitute higher quality securities than securities issued under an exemption under, for example, Securities Act Rule 144A, and then subsequently exchanged for registered securities *because such securities are subject to the Securities Act.*" 73 Fed. Reg. 40106 at 40114 (July 11, 2008) (emphasis added). Although we disagree with this conclusion about "quality," we nonetheless feel that discouraging registration is not in keeping with the Commission's goals.

5 We feel it necessary here to distinguish the suggestion that a prior ABA drafting committee made in responding to the proposed regulations that ultimately became Regulation AB. That drafting committee believed there were strong benefits to investors from the registration of asset-backed securities and suggested ways to encourage such registration for securities that have traditionally been privately placed. It proposed allowing registration of non-investment grade classes with QIB and minimum denomination requirements as a means of expanding Form S-3 eligibility to classes of securities that did not meet the NRSRO rating requirement, while balancing that expansion with a more restrictive approach to sales of those securities. However, for the reasons discussed above, we feel that such an approach would be inadvisable outside the narrow context in which it was proposed.

6 For example, the Staff could change its policies so that a registration statement on Form S-3 selected for review would be declared effective only following review of a completed prospectus supplement (other than pricing information) for a particular tranche of securities to be issued promptly after effectiveness. In other words, the process for the first takedown off a Form S-3 selected for review could look very similar to that for a Form S-1. Although this would present a "speed-bump" for first issuances off of Form S-3, such an approach would

contributing to credit crises in the global markets, an approach that either constrains the liquidity of registered asset-backed securities (by restricting investors and minimum denominations) or encourages issuers to pursue exempt rather than registered offerings in order to avoid registration on Form S-1 or the investor limitation, thereby depriving investors of the benefits of the registration process and the issuer liabilities that come with registration, seems unwarranted.

The possibility that issuers will pursue exempt rather than registered offers—one of our greatest concerns with these proposals—may have the counterintuitive effect of making publicly registered asset-backed securities less liquid than their privately offered counterparts. We are concerned that the current proposals—not only with respect to Form S-3 but also with respect to Rule 3a-7—may diminish the benefit of public registration to a point where securities that are currently publicly offered will instead only be offered through private placements and overseas offerings. We believe that investors in these securities would be harmed by the loss of Section 11 and Section 12(a)(2) liability, and we believe that market liquidity as a whole would be diminished as investors with baskets for "liquid securities" would fill these more quickly with unregistered asset-backed securities.[7] In addition, we believe that the Commission's better goal is to encourage more issuers to subject themselves to the disclosure requirements of Regulation AB, and we would prefer efforts made to enhance, rather than diminish, the desirability of registration in this regard.

Not only do we believe that the proposed changes will not address the Commission's qualitative concerns about ratings, we are not even sure what potential harm the Commission is trying to prevent with the proposed investor and denomination restrictions. For instance, in the current market turmoil, those investors bearing the greatest burden of the collapse of the mortgage-backed securities market have been experienced institutional investors that underestimated the risks of the securities they were acquiring. And, although most asset-backed securities are not marketed to individual investors and are sold in large denominations, the market for these securities is by no means limited to QIBs. Further, there are certain categories of such securities that are specifically targeted to retail investors and may be sold in denominations as small as $25. For instance, there are structured finance securities that repackage corporate bonds into $25 units to make them available to smaller investors who do not wish to invest in, or do not have access to, such securities in $1,000 minimum denominations. To the extent the Commission is concerned about unsophisticated investors purchasing ABS, those concerns could be addressed more simply through a requirement for an additional legend for structured products to be included on the front page of the prospectus supplement along the

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preserve the benefits of shelf registration for subsequent offerings. The Staff would, of course, continue to have discretion as to which registration statements merited such review or deferred effectiveness.

7 Our understanding is that, for many investors, the "liquid securities" basket may require more than public registration—for instance, that the securities be freely tradable—and many have concerns that the limited form of public registration proposed by the Commission would not satisfy those requirements. In addition, the spread between public and private securities has traditionally been quite small, leaving little incentive for issuers to pursue public registration when registration would narrow, rather than expand, the permissible range of investors.

following lines, where applicable[8]: "The securities offered by this prospectus supplement and the accompanying prospectus are complex structured securities that have different risks than those of corporate equity and debt securities. These securities may not be suitable for investors who are not experienced in or knowledgeable about investing in complex structured securities."

We appreciate that the Commission has proposed that its requirement that asset-backed securities offered on Form S-3 be sold only to QIBs would apply only to initial sales. The Commission has also asked whether that requirement should be expanded beyond such initial sales. We are opposed to such an expansion because, we believe, it would pose numerous logistical, liquidity and other market challenges—again, with no substantial benefit to investors. For instance, such a change would presumably:

- require investment banks, clearing houses such as The Depository Trust Company, and other participants in the settlement of securities to monitor the sales and resales of asset-backed securities differently from other publicly registered securities (and also differently from securities issued in private and offshore offerings);
- require legending such as typically applies to non-registered securities; and
- create confusion in the resale markets, where securities issued pursuant to Rule 144A would become freely transferable after a specified period but those that were publicly offered would incongruously remain permanently restricted.

If, notwithstanding the above, the Commission decides to proceed with eliminating the NRSRO references, we suggest the following alternative proposals (with the proviso that we view none of them as an improvement over the current system), which could provide several different options for achieving Form S-3 eligibility:

- as with certain of the market regulation proposals the Commission has made concurrently with the Form S-3 proposals, retain an NRSRO rating as one means, but not an exclusive means, of obtaining Form S-3 eligibility;
- create an "experienced ABS issuer" category for Form S-3 eligibility[9]; and/or
- provide Form S-3 eligibility for securities that are expected to be concurrently listed on a national securities exchange.

With respect to developing an "experienced ABS issuer" category, we appreciate the potential difficulties in defining such a category, given that that the sponsor, servicers, originators of assets and depositor each often play a more significant role than the issuing entity (which may be newly formed), and may have different roles in different securitization offerings.

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8 We feel this sort of legend would not be accurate in the case of certain securities that technically fall under the rubric of "asset-backed security" but do not carry these more complex risks. We would therefore wish to see any legend requirement implemented in a way that retained flexibility to exclude the legend where inapplicable.

9 We wish to clarify that we are not suggesting an expansion of benefits for such a category similar to that for well-known seasoned issuers, but simply the ability to use Form S-3 for offerings (for which there is no current experience requirement at all).

Our initial view is that the sponsor would be the critical entity to evaluate in developing such a category, and that we would define "experienced ABS issuer" by whether the sponsor has completed an offering on either Form S-1 or Form S-3, in either case relating to asset-backed securities. Other criteria might include:

- origination and performance history of financial assets similar to those backing a class of securities (e.g., the availability of three or five years of static pool data);[10]
- a minimum market capitalization and/or prior history of issuance of ABS of the same or similar financial assets for cash; and/or
- prior history of the relevant securitization program, including the absence of events of default, early payouts or loss of ratings, in each case where investors have lost or are expected to lose principal as a result of such events, occurring within the prior 2 years.

Given the current market disruptions, however, great care will need to be exercised with respect to any proposed standard that relies on volume of recent market issuances. The market for asset-backed securities has been sharply curtailed in the past 12 months, and even well-seasoned issuers have publicly offered and sold relatively small dollar amounts of asset-backed securities in that period. If the Commission were to change its rules for eligibility to use Form S-3, we would wish to see all registration statements on Form S-3 that were then effective or in the midst of the registration process be grandfathered under the old rules to minimize disruption and preserve the value of registration fees that have already been paid. We also would wish to see private issuances considered for any volume standard, to better encourage sponsors to begin to register securities that have historically been offered and sold only through exempt offerings.

Proposed changes to Item 1100(c) of Regulation AB

Under existing Item 1100(c) of Regulation AB, an issuer of asset-backed securities may provide the required financial disclosures with respect to a "significant obligor" for the pool of assets by reference to the financial information of the obligor filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), rather than by presenting the full financial information of the obligor, so long as certain conditions are met, including that the significant obligor meets the registrant requirements for Form S-3 or Form F-3 or the relevant pool assets are non-convertible investment grade rated securities. In the Securities Act Release, the Commission proposes to amend Item 1100(c) by removing the ratings requirement and replacing it with a requirement that the pool assets have been issued in a primary offering for cash that was registered under the Securities Act. The Commission then explains its position that securities

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10 We note that several members of our drafting committee have expressed concern that a definition of "experienced ABS issuer" that depended on availability of a performance history or prior offerings with similar assets might result in loss of Form S-3 eligibility even for sophisticated participants in the structured finance markets. We therefore request that, if the Commission were to pursue this alternative in a form that would impose conditions other than completion of an ABS offering on Form S-1 or Form S-3, the Commission issue a separate release for comment setting forth the proposed definition prior to adopting such conditions.

registered under the Securities Act are of "higher quality" than those issued in exempt offerings.[11]

We do not support this change. The requirement that the Commission now seeks to amend, which was adopted as part of the broader adoption of Regulation AB and codified prior Staff positions, has never to our knowledge been presented as reflecting a quality judgment about the assets to which it applied; rather, as with provisions involving eligibility for registration on Form S-3 and Form F-3, it has reflected the availability of information about the significant obligor.[12] As we also noted in our comment letter on the June 16 Release, the Commission's adoption of Regulation AB was pursuant to a very thoughtful, deliberate and comprehensive process during which there was broad-based participation from many participants in the structured finance markets. The Commission does not suggest that any problems have arisen or that investors have been harmed as a result of the reference to financial statements permitted by existing Item 1100(c). We do not believe it is appropriate to make a change to a standard that was deemed sufficient just a few years ago simply based on a desire to eliminate references to credit ratings. Nor, as noted above, do we agree with the Commission's proposition that securities that are issued under an effective registration statement constitute "higher quality" securities than those issued under an exemption from registration[13]—or the corollary position that a provision designed to facilitate disclosure should be twisted into a provision regulating the purported "quality" of the pool assets.

As with many of the other proposals in the Proposing Releases, the proposed change will make it more difficult for issuers to issue publicly registered asset-backed securities. We do not feel such a result would be in the best interests of investors, issuers or the capital markets.

Rules 15c3-1 and 2a-7

In the Exchange Act Release, the Commission has proposed to remove references to ratings in the net capital rule, Rule 15c3-1 promulgated under the Exchange Act, and instead require broker-dealers to make independent evaluations of the securities they hold to determine if those securities carry "minimal credit risk" or "moderate credit risk." Similarly, the Commission has proposed to eliminate the requirement in Rule 2a-7 that investments by money market funds be rated in one of the two highest rating categories by an NRSRO, and to replace that with a

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11 See footnote 4 above.

12 Other provisions adopted in connection with Regulation AB have required that where assets in the pool are unregistered securities, these securities must be freely tradable at the time of inclusion in the pool. *See* Rule 190 of the Securities Exchange Act of 1933, as amended.

13 As we noted in our comment letter on the June 16 Release, in our experience, issuers have a variety of reasons for deciding to undertake exempt offerings rather than registered public offerings. Most such reasons relate to the speed of the offering or a desire to limit disclosure of confidential, proprietary or otherwise sensitive information to a limited number of sophisticated investors who assume express confidentiality obligations. The "quality" of such securities is neither intrinsically lower than nor higher than registered securities.

different level of analysis by the money market fund's board of directors. We believe these proposals are unwise for several reasons.

With respect to Rule 15c3-1, we believe that while some of the largest and most sophisticated broker-dealers may be able to make such an independent credit evaluation, many U.S. broker-dealers may not have this ability. As the Commission staff has noted, even among the Consolidated Supervised Entity (CSE) broker-dealers, which are the largest and most sophisticated of U.S. firms, there was a substantial variation in the quality of independent risk management. Recent market events, including the failure of one CSE firm, support this concern. This leads us to doubt whether the overwhelming majority of U.S. broker-dealers which are not CSE firms have the ability to develop and apply adequately and reliably the credit evaluation proposed by the Commission.

We also believe there is an inherent conflict of interest involved in allowing broker-dealers to evaluate the credit risk of the securities they hold, and thereby determine how much capital they must hold against those securities. Such a system creates an incentive for broker-dealers to overestimate the creditworthiness of those securities so as to minimize the amount of required capital and thereby to minimize the broker-dealers' costs. Behavioral finance teaches that all market participants, including broker-dealers, have a natural psychological tendency to overestimate the creditworthiness of securities they hold, and to delay recognizing declines in that creditworthiness. We are concerned that this proposal would lead some broker-dealers to maintain too little capital and thereby increase market-wide systemic risk. Moreover, recent events have indicated that many market participants are concerned whether major financial institutions, including broker-dealers, have adequate capital and liquidity resources, and those market participants fear that they do not have adequate visibility concerning their counterparties' capital and liquidity. We believe a proposal that allows broker-dealers to rely on their own credit evaluations in determining their regulatory capital requirements will tend to exacerbate this systemic concern about the adequacy of counterparty capital and liquidity, especially in times of market stress. For all of these reasons, we urge the Commission to continue to maintain objective standards in Rule 15c3-1, rather than allowing broker-dealers to rely on their own subjective credit risk determinations.[14]

We have similar concerns with respect to the proposed amendments to Rule 2a-7. The Commission's proposed amendments would place the burden of determining whether a security is an "Eligible Security" on a fund's board of directors. This would mandate a financial sophistication and level of expertise which we believe is beyond the average director's qualification. It would also go beyond the traditional oversight role of the director under the Investment Company Act and necessitate that directors become involved in a key component of the security selection process and immerse themselves in day-to-day decision making of the type generally reserved for fund management.

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[14] If the Commission is convinced that NRSRO ratings are no longer appropriate standards, then we suggest that it consider other objective standards, such as WKSI status or Form S-3 eligibility, as it has in its other proposals to eliminate references to NRSRO ratings.

Under the proposed amendments to Rule 2a-7, if members of the board of directors did not have the necessary expertise to determine the credit quality of a security, the board would be obliged to either delegate the determination process to the fund's investment adviser or hire a third party to perform the analysis. Delegating the determination to the investment adviser would decrease shareholder protections by giving too much discretion to a fund's investment adviser, while at the same time removing the "floor" provided by third-party credit ratings. Hiring a third party would increase costs to the fund and could be unworkable. In either case, the delegation with no reference to an external standard raises the likelihood that different funds will make conflicting determinations about the same securities, which will increase investor confusion.

As noted in the Investment Company Release, in its current form, Rule 2a-7 already requires that a fund's board of directors make a determination that the investment presents minimal credit risks, based on "factors pertaining to credit quality in addition to any ratings assigned to such securities by an NRSRO." The current test contains both an objective standard (the NRSRO rating requirement) and a subjective standard (the board's separate analysis of factors pertaining to credit quality). In our view, the combination of these standards has served investors well, providing a level of protection to investors in those funds that the Commission's proposed alternative—which shifts solely to a subjective standard—lacks. Although we appreciate that the board could still consider credit ratings in evaluating the appropriateness of the investment, permitting such consideration is very different than constraining the board's action by imposing a rating requirement. As noted elsewhere in this letter, we strongly believe that if the Commission is concerned about the credibility of the ratings which play a role in the current test, a better solution would be the enhancement of oversight and transparency of third party credit ratings processes, not the elimination of the use of such ratings. At a time of substantial liquidity crises, bank failures, and other market disruptions, we are very concerned about eliminating, and urge the Commission not to eliminate, one of the safeguards for money market funds.

Rule 3a-7

The Commission proposes in the Investment Company Release changes that would restrict the availability of Rule 3a-7 to those issuers whose investors are solely QIBs and accredited investors—a restriction that would apply for the life of the issuer. Such changes would go even further than those proposed for Form S-3 eligibility, and in our view would eliminate all benefits of public registration for those issuers who would otherwise rely on Rule 3a-7. We strongly encourage the Commission to preserve Rule 3a-7 in its current form.[15]

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15 If there were nonetheless to be a rule change, we note that it would be essential to grandfather existing issuers and other vehicles that were formed in reliance on current Rule 3a-7. Many structured finance transactions include a provision that causes early paydowns if the vehicle becomes an investment company. Any change that fails to grandfather existing vehicles, therefore, would cause such structures to unwind, exacerbating the current liquidity crisis, potentially causing losses to investors, and jeopardizing the capital adequacy of depositors who are financial institutions.

In the Investment Company Release, the Commission states that it believes few issuers of asset-backed securities rely on the exclusion from investment company status provided by Rule 3a-7. On the contrary, since the adoption of Rule 3a-7, we understand that a significant portion of publicly registered and private offerings have relied on Rule 3a-7 and that offerings only rely on Section 3(c)(7) where Rule 3a-7 or another exemption is unavailable (for instance, because of active trading of the vehicle's assets). Most importantly, Section 3(c)(7) by its terms is not available for publicly-registered offerings. Prior to the adoption of Rule 3a-7, many asset-backed securities relied on Section 3(c)(5) of the Investment Company Act of 1940 (the "Investment Company Act"), but as noted in the final adopting release for Rule 3a-7, the Commission had issued over 125 exemptive orders addressing structured finance securities that did not meet the requirements of Section 3(c)(5).[16] Asset-backed issuers who neither satisfied Section 3(c)(5) nor had an exemptive order relied either on Section 3(c)(1) or sold their securities overseas. Rule 3a-7 was the Commission's attempt to clarify that structured financings generally were not within the scope of the Investment Company Act and was "intended to exclude virtually all structured financings from the definition of investment company, subject to certain conditions."[17]

We believe the amendments the Commission has proposed with respect to Rule 3a-7—and in particular the requirement that only issuers of securities to QIBs and accredited investors fall within the rule—will defeat the intended purpose of Rule 3a-7. Issuers of certain structured finance securities that are intended to be marketed to retail investors—for instance, bond-repackaging transactions and hybrids—will need either to obtain an exemptive order or forgo registration and limit their offerings to overseas investors. As discussed above in connection with the Form S-3 eligibility for asset-backed security proposal, such a change also would require development of infrastructure and procedures to monitor investors in publicly-registered securities that rely on this exemption. The proposed changes to Rule 3a-7 may create an even stronger disincentive for issuers of asset-backed securities to undertake public offerings than would the proposed Form S-3 eligibility changes. Because the proposed Rule 3a-7 changes would apply both to initial sales and to resales, issuers of asset-backed securities which rely on Rule 3a-7 would have no incentive to undertake a public offering.

Rather than eliminating the exclusion for securities sold to the public, the Commission would do better to retain the exclusion and simply eliminate the rating requirement, relying on the other aspects of the rule that distinguish ABS vehicles from traditional investment companies. (However, we strongly recommend retaining the rating requirement). For instance, the Rule 3a-7 restriction on asset trading to capture changes in market price has always been a sufficient means to distinguish securities relying on Rule 3a-7 from the types of investment companies the Commission typically regulates.

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[16] 57 Fed. Reg. 56248, 56248 (November 27, 1992).

[17] Id. at 56249.

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The Committees appreciate the opportunity to comment on the proposal and respectfully request that the Commission consider the recommendations set forth above. We are prepared to meet and discuss these matters with the Commission and its Staff and to respond to any questions.

Respectfully submitted,

Keith F. Higgins/sk

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