U.S. TREASURY DEPARTMENT OFFICE OF PUBLIC AFFAIRS

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FACT SHEET: TREASURY RELEASES BEST PRACTICES FOR RESIDENTIAL COVERED BONDS

"As we are all aware, the availability of affordable mortgage financing is essential to turning the corner on the current housing correction. And so we have been looking broadly for ways to increase the availability and lower the cost of mortgage financing to accelerate the return of normal home buying and refinancing activity. We are at the early stages of what should be a promising path, where the nascent U.S. covered bond market can grow and provide a new source of mortgage financing."

\- Treasury Secretary Henry M. Paulson, Jr.

- The Administration is focused on pursuing a range of initiatives to help homeowners avoid preventable foreclosures and to speed the recovery from the housing correction. Covered bonds have the potential to help homebuyers and those seeking to refinance by increasing mortgage financing. Covered bonds can also help strengthen U.S. financial institutions by providing a new funding source that will diversify their overall funding portfolio.

- Treasury today issued Best Practices for Residential Covered Bonds in response to market participants' request for clarity from regulators regarding the covered bond market. A robust covered bond market exists in Europe, and in preparing this Best Practices Guide, Treasury consulted with our European counterparts as well as with potential U.S. market participants, including issuers, investors, underwriters and rating agencies.

- While in Europe specific legislation often defines the debt instrument, the U.S. regulatory environment is different and does not require legislation.

- On July 15, 2008, the Federal Deposit Insurance Corporation issued a Final Covered Bond Policy Statement which specified actions that the FDIC will take during an insolvency or receivership if the covered bond meets certain minimum requirements. The Best Practices Guide is a complement to the FDIC statement because it introduces standards in areas such as collateral and disclosure that will help to start the covered bond market with very high quality securities. Treasury and the FDIC issued their guides to bring clarification on these issues.

- The Treasury Department believes that there should be a variety of financing alternatives within the U.S. mortgage market. The housing government-sponsored enterprises, Fannie Mae, Freddie Mac and the Federal Home Loan Banks, and the Federal Housing Administration are fulfilling their public policy missions by providing mortgage financing during these months of market stress. They must continue to do so. Treasury also expects private-label securitization to return to the U.S. mortgage market, enabling homeowners to benefit from a broad, global investor base. Given the size of the U.S. residential mortgage market, Treasury believes there will be a role for all sources of mortgage funding in the future.

- A covered bond is a secured debt instrument that provides funding to a depository institution, or issuer, that retains residential mortgage assets and related credit risk on its balance sheet. These assets are known as the cover pool. Interest on the covered bond is paid to investors from the issuer's cash flows, while the cover pool serves as secured collateral. Covered bonds provide dual recourse to both the cover pool and the issuer. In the event of an issuer default, covered bond investors first have recourse to the cover pool. In the event the cover pool returns less than par in a liquidation, investors maintain an unsecured claim on the issuer.

- Covered bonds differ from mortgage backed securities in several ways. First, mortgages securing covered bonds remain on an issuer's balance sheet, unlike mortgage backed securities. Second, pools of loans securing covered bonds are dynamic, and non-performing or prepaying loans must be substituted out of the cover pool. Finally, if a covered bond accelerates and repays investors at an amount less than the principal and interest owed, investors retain an unsecured claim on the issuer.

- Covered bonds differ from unsecured debt because of the absence of secured collateral underlying the obligation of the issuer. While unsecured debt investors retain an unsecured claim on the issuer in the event of issuer default, covered bond investors possess dual recourse to both the underlying collateral of a covered bond and to the individual issuer. Accordingly, covered bonds provide investors with additional protection on their investment compared with unsecured debt.

- In conjunction with the release of this Best Practices Guide, Treasury will update its own collateral acceptability policy to include covered bonds as an approved asset category for securing the Treasury's investments and deposits of public money with commercial counterparties.

SUMMARY OF BEST PRACTICES

To be consistent with Treasury's Best Practices, a covered bond program must conform to all the provisions throughout the life of the program. The following is a summary of key provisions found in the Best Practices Guide. A complete description of all provisions can be found in the document.

Issuer

- The Issuer may be either:
    - A newly created, bankruptcy-remote special purpose vehicle; or
    - A depository institution and/or wholly-owned subsidiary of a depository institution

Security

- In both the special purpose vehicle structure and the direct issuance structure, the cover pool must be owned by the depository institution. Issuers must provide first priority claim on the assets to bond holders and the assets in the cover pool must not be burdened by other liens. The cover pool's assets and liabilities must be clearly identified on its books and records.

Maturity

- The maturity for covered bonds shall be greater than one year and no more than 30 years.

Eligible Cover Pool Collateral

- Collateral in the cover pool must meet certain requirements at all times to be eligible. The template outline the complete criteria for eligible mortgages which includes, but is not limited to:
    - One-to-four family residential properties
    - Underwritten at the fully-indexed rate
    - Underwritten with documented income
    - Current when they are added to the pool and any mortgages that become more than 60-days past due must be replaced
    - First lien only
    - Maximum loan-to-value of 80 percent at the time of inclusion in the cover pool
    - Negative amortization are not eligible for the cover pool

Overcollateralization

- Issuers must maintain an overcollateralization value at all times of at least 5 percent of the outstanding principal balance of the covered bonds.

Specified Investment Contract

- Each covered bond must have a specified investment to prevent an acceleration of the covered bond due to the insolvency of the Issuer.

Cover Pool Disclosure

- Issuers must make available descriptive information on the cover pool with investors at the time an investment decision is being made and on a monthly basis after issuance. The SEC's

Regulation AB provides a helpful template for preparing pool level information, such as presenting summary information in tabular or graphical format and using appropriate groups or ranges

Issuers must make this information available to investors no later than 30 days after the end of each month.

Asset Coverage Test

- The Issuer must perform an asset coverage test on a monthly basis to ensure collateral quality and the proper level of overcollateralization and to make any substitutions that are necessary to meet the provisions of the Template. The results of this asset coverage test and the results of any reviews by the asset monitor must be made available to investors.

Regulatory Authorization

- Issuers must receive consent to issue covered bonds from their primary federal regulator.

Issuance Limitations

- Covered bonds may account for no more than 4 percent of an issuers' liabilities after issuance.