March 22, 2020

The Honorable Jerome H. Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, D.C. 20551

The Honorable Steven T. Mnuchin
Secretary
Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, D.C. 20220

Re: <u>Solutions to Power the Advancement and Revitalization of Consumer Credit ("SPARCC")</u>

Dear Chairman Powell and Secretary Mnuchin:

As you are aware, the U.S. economy is facing sudden and momentous headwinds unprecedented in modern times due to the national health emergency posed by the COVID-19 pandemic. The global COVID-19 crisis and resultant mandatory quarantines and business closures have disrupted daily economic life across the country for millions of Americans. At the same time, uncertainty as to the future path of the pandemic has significantly disrupted the normal functioning of credit markets. With unemployment expected to rise dramatically and many sectors of the economy on virtual lockdown, a meaningful percentage of American households and businesses will face hardships making payments on their mortgage, rent, lease, student loan and other debt obligations. In response, our American lenders and servicers are providing assistance to consumers and small businesses through extensive forbearance programs, fee waivers and other flexible repayment programs as quickly and efficiently as they can. In order to facilitate this ongoing assistance while also providing the financial markets needed calm, it is the view of the Structured Finance Association (the "SFA")[1] and its 370 corporate members that it is essential to immediately enact a new version of the Term Asset-Backed Securities Loan Facility ("TALF"), which we refer to as Solutions to Power the Advancement and Revitalization of Consumer Credit ("SPARCC"). SPARCC, which would in many respects be a TALF 2.0, should be updated as soon as possible to address the unique needs resulting from the economic dislocation brought on by the COVID-19 pandemic.

As many economists routinely note, the Federal Reserve should lend freely as a form of economic disaster assistance to our economy in times of unique crises. The COVID-19 crisis is very different from the 2008 financial crisis. We are suffering massive cash flow and liquidity problems because we are shuttering our economy for the benefit of our nation's health. To date, this is not primarily a credit crisis. We encourage you to

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[1]SFA is a member-based, trade industry advocacy group focused on improving and strengthening the broader structured finance and securitization market. SFA provides an inclusive network for securitization professionals to collaborate and, as industry leaders, drive necessary changes, be advocates for the securitization community, share best practices and innovative ideas, and educate industry members through conferences and other programs. Members of SFA represent all sectors of the securitization market including issuers, investors, financial intermediaries, law firms, accounting firms, technology firms, rating agencies, servicers, and trustees. Further information can be found at www.structuredfinance.org.

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move as quickly as possible to implement a SPARCC, or TALF 2.0, program to forestall the worst effects of this crisis. We also detail recommendations for adjustments to bring SPARCC current, which we urge you to make as soon as possible thereafter. Key among these change are permitting legacy asset-backed securities ("ABS") of all eligible asset classes to be pledged as collateral, and updating the list of eligible asset classes to include those that did not exist in 2008 or were ineligible at that time for reasons that are not relevant to the current situation, including but not limited to private label residential mortgage-backed securities ("RMBS"), certain forms of high grade mortgage credit risk, such as credit risk transfer ("CRT") bonds, and ABS backed by unsecured consumer loans, mortgage servicing rights ("MSRs"), and other types of receivables. The larger the Federal Reserve's willingness to provide liquidity assistance, the more effective the result will be for our economy.

The uncertain magnitude and length of these financial burdens on U.S. consumers and businesses as a result of the national health emergency has placed a corresponding and considerable strain on those same American lenders and servicers as well as the fixed income investors (many of which are pension plans, insurance companies and asset managers of 401(k) plans) who finance loans to consumers and businesses in the credit markets. As a result of this uncertainty, new issue and secondary credit markets have essentially stalled, with significant implications for the availability of affordable credit to small businesses and individuals, particularly to those with low- to moderate- income, which is fundamental to our economic recovery following this national emergency.

While the causes of the current crisis are very different from the financial crisis of 2008, that crisis also resulted in a *de facto* closure of the credit markets, significantly limiting the availability of credit for U.S. small businesses and households and exacerbating the weaknesses in the U.S. economy. To help ameliorate these problems, at that time the Board of Governors of the Federal Reserve System and the U.S. Department of Treasury created the TALF, a credit facility designed to restore liquidity to the frozen credit markets.

The membership of the SFA believes that a program substantially based on TALF, which again, we refer to as the SPARCC program, will support American households and businesses through this difficult time and help aid our nation's economic recovery following this temporary health emergency by enhancing the liquidity and functioning of crucial credit markets that provide essential credit to all Americans. In particular, we believe that the prompt implementation of SPARCC, with modest but critical adjustments to the legacy TALF program, would especially support low- and moderate- income Americans and others whose credit needs are not well-served by traditional banks. Also, it will importantly help circumvent the domino impact on U.S. lenders and servicers – who employ countless American workers – and mitigate a liquidity crunch on fixed income investments held by our pension and saving plans, insurance companies and asset managers.

Background

The TALF program was announced by the Federal Reserve Bank of New York (the "FRBNY") in November 2008 and was intended to make credit available to consumers and small businesses on more favorable terms by facilitating the issuance of ABS backed by these loans and improving the market conditions for ABS more generally. Under TALF, the FRBNY loaned up to $200 billion on a non-recourse basis to holders of certain AAA-rated securities backed by newly and recently originated consumer and small business loans. The FRBNY

extended loans in an amount equal to the market value of the securities less a haircut and these loans were always secured by the underlying collateral. TALF began operations in March 2009 and operated for new issuance until June 2010. In our members' view, TALF was a great success on all counts, serving to backstop market uncertainty and helping to generate new issuance in an otherwise disrupted market. Over the life of the program, all TALF loans were repaid in full at or before their maturity dates. The FRBNY did not incur a loss on any TALF loan. As all TALF loans were repaid in full, no TALF collateral was surrendered. TALF LLC, a limited liability company formed to purchase and manage any securities received by the FRBNY in connection with the decision of a borrower not to repay a TALF loan, never ended up acquiring any such assets.

Since the economic recovery of capital markets from the financial crisis, those markets have operated effectively and efficiently, serving as an important source of capital for the extension of credit, particularly to low- to moderate- income individuals. The cause of today's issues in the credit markets is directly related to the economic disruptions from COVID-19 public health measures – the social distancing measures needed to stop the virus's spread are also bringing much economic activity to a screeching halt, impacting borrowers, their employment, and their ability to repay, as well as the uncertainty over the length of time the U.S. economy will be adversely affected by the COVID-19 pandemic. We must give individual borrowers a bridge across the resulting income chasm by allowing lenders and investors to continue to use their capital to finance loans.

To avoid a longer-term drop in the availability of credit to small businesses and consumers, we strongly urge the FRBNY to quickly implement a SPARCC program. SPARCC would share many characteristics with the legacy TALF program but, as soon as possible, should be tailored to effectively address the unique challenges brought on by the COVID-19 crisis and the changes to the credit markets since the original TALF program.

The following is a high-level summary of the changes we recommend for a SPARCC program from the requirements of the legacy TALF program implemented during the financial crisis.

Permit Legacy ABS and Assets to be Eligible Collateral

TALF initially only permitted new-issue ABS to be eligible collateral. Towards the end of the program, legacy commercial mortgage-backed securities ("CMBS") were permitted as collateral. This addition was intended to promote price discovery and liquidity for legacy CMBS, with the expectation that a reinvigorated legacy CMBS market would stimulate the extension of new credit by helping to ease balance sheet pressures.

The same policies apply today. As noted, today's economic crisis is primarily one of liquidity, not inherent credit quality. The ABS market is interconnected – uncertainty arises when the trading markets for legacy ABS are severely disrupted, and that uncertainty serves as a disincentive to purchasing new-issue ABS, which results in reduced credit availability and increased borrowing costs for consumers and businesses. Our members believe that an effective SPARCC program should not be restricted to new-issue ABS, and should include both those trading in the secondary market or retained at closing by the sponsor and later sold to investors. The procedures for SPARCC lending should be tailored to permit borrowing collateralized by legacy ABS. This might include, for example, repurchase financing with mark-to-market protections.

TALF also placed limits on the age of receivables that could serve as pool assets for eligible ABS. For similar reasons, we do not support fixed limits on the age of securitized receivables for SPARCC.

Expand the Types of ABS that are Eligible Collateral

Over the life of the TALF program, permitted collateral types included ABS backed by auto loans and leases, student loans, consumer and corporate credit card receivables, small business loans fully guaranteed as to the principal and interest by the SBA, equipment loans and leases, floorplan loans, commercial, governmental and rental fleet leases, mortgage servicing advance receivables, and CMBS. Since the pre-crisis problems of the private label RMBS market have been addressed, that asset class also should be a permitted type of collateral in SPARCC. In our members' view, the types of permitted collateral for SPARCC should include not only all of the types of ABS that were permitted under TALF, but should be expanded to include ABS of asset classes that did not exist or were uncommon in 2008, including but not limited to ABS backed by unsecured personal loans, MSRs, and various other types of receivables.

RMBS

In order to promote the continued availability of mortgage capital during the COVID-19 crisis, private label RMBS should be included as a permitted collateral type. Many if not all of the poor underwriting practices and information asymmetry that existed before 2008 have been eliminated through Dodd-Frank rulemaking and other regulatory actions (such as the ability-to-repay rules, the credit risk retention rules, and the NRSRO due diligence rules), as well as more rigorous market practices in private label underwriting as well as balance sheet lending. While the private label RMBS market remains much smaller than those sponsored by the government-sponsored enterprises ("GSEs") Fannie Mae, Freddie Mac and Ginnie Mae, private-label RMBS represent a growing source of capital for mortgage loans, particularly for "non-qualified" mortgage borrowers such as the fast-growing non-W-2 gig economy workers. Inclusion of these assets for purchase by the FRBNY to provide liquidity would help to unfreeze the mortgage credit markets in a meaningful way, allowing servicers and lenders to focus on making new loans and providing meaningful assistance to struggling borrowers.

Unsecured Consumer Loan ABS

Americans rely on personal credit to make ends meet today more than ever before. The ways consumers choose to borrow have changed since the 2008 crisis, in that unsecured personal loans have become a common way to access credit in situations where consumers might formerly have chosen credit card borrowing. According to the credit bureau TransUnion, personal loan balances rose to $138 billion in 2018, and $82 billion in personal loan ABS were issued that same year. Personal installment loans are most important to borrowers with limited savings, and the Federal Reserve has released data asserting that 40% of Americans cannot afford a $400 emergency.

Unfortunately, the partial shutdown of the economy to protect America from COVID-19 is impacting these Americans the hardest, who tend to have lower wages, little savings, and work in the very economic sectors that have been most impacted. Marketplace and consumer lenders who provide unsecured personal loans want to

continue to extend credit to these borrowers, particularly those whose credit needs are poorly served by traditional banks. Marketplace lenders and consumer finance companies focused on personal loans did not exist in large numbers in 2008, nor did marketplace loans or unsecured personal loans exist as an asset class in the securitization market. It is important for SPARCC to include ABS backed by these loans as eligible collateral to support these lenders in providing much-needed financing to consumers during challenging economic times.

MSR and CRT ABS

Since the last financial crisis, many banks shed their mortgage origination and servicing operations mortgage, resulting in a dramatic shift to non-bank servicers after. Non-bank servicers had traditionally relied on bank loans to finance their servicing portfolios, but as their portfolios grew the ABS market responded with financing vehicles for the largest non-bank servicers, collateralized by their rights to receive servicing fees (typically an interest rate strip off the mortgage loans they service). Six of the largest non-bank servicers have issued term ABS and revolving ABS backed by MSR fees. To date GNMA servicing is the largest component, but these facilities, more efficient than bank loans, have also gained traction in Fannie Mae, Freddie Mac and private label servicing. Interest rate volatility is causing volatility in MSR values, in turn limiting the availability of traditional financing to non-bank servicers. As a result of mortgage forbearance programs implemented and the additional relief to homeowners contemplated in light of the COVID-19 crisis, dependence on servicers to make an unprecedented amount of advances on mortgage loans will increase the strain on their resources and make their access to capital a critical component of market stability. These servicers desperately need financing and liquidity to continue performing their critical function intermediating between mortgage credit and the secondary markets. As such, allowing for the inclusion of MSRs in SPARCC would also enhance the ability of servicers to provide assistance to their customers.

Fannie Mae and Freddie Mac have been issuing credit risk transfer, or CRT, securities over the past several years. These bonds are purchased by mortgage investors to help facilitate the GSEs' growth in the secondary mortgage market. While these CRT instruments are designed to withstand very large unemployment spikes due to most economic recessions and business cycle fluctuations, payment forbearance as a result of government closures of business is not something they had in mind. As such, providing liquidity to these instruments during this unique moment would also help to allay panic in the mortgage markets.

Other Asset Classes

By going into more detail on the foregoing asset classes, we do not minimize the need to expand SPARCC expeditiously to encompass the other asset classes that have urgent needs.

These include transportation-related ABS, including those collateralized by containers, rail cars, aircraft and shipping assets. Our transportation industry is critical to the efficient functioning of our economy through supply chain operations, and plays a key role in connecting individuals and small businesses to goods from around the world – among other things, this sector is responsible for the delivery of cars, machinery, and other consumer staples.

Another important ABS category to consider is whole-business securitizations, including restaurant and franchise securitizations. Restaurants in particular have been immediately impacted by closures intended to limit the spread of the virus, to the detriment of the workers who depend on shifts for their income, many of whom who are low- and moderate- income Americans.

Small businesses also are suffering as a result of closures and restrictions on travel, so unguaranteed small business loans are another ABS asset class that should be considered as soon as possible.

Device payment plan securitizations finance the purchase of wireless devices, which principally include cell phones. They are used by consumers for both voice and data communication and are especially important for the millions of self-employed Americans that participate in the gig economy. This is particularly important during the pandemic as social distancing policies prevent in-person communication. Providing liquidity to this market will help ensure continued credit to consumers to acquire wireless devices, particularly during this time of enforced social isolation.

Other important ABS asset classes include, but are not limited to, renewable energy assets (such as solar loans), insurance premium finance agreements, consumer refinance loans, re-performing and seasoned performing mortgages, triple-net leases, and timeshares.

Expand Credit Ratings Criteria

TALF required that any collateral ABS must have the highest long-term or short term investment grade rating from at least two nationally-recognized statistical rating agencies (an "NRSRO"), chosen from only three permitted NRSROs.[2] In our members' view, this requirement should be expanded to also include the highest-rated tranche in any securitization, so long as that tranche is rated at least investment grade, subject to an appropriate haircut reflective of the lower rating. We also believe that the rating should be required to be obtained from only a single NRSRO, and that SPARCC should not mandate the use of any particular NRSRO or NRSROs.

Marketplace lenders and other similar lenders who sponsor ABS transactions tend to have less than AAA credit ratings on the senior bonds issued in their ABS transactions, and they may only be rated by one NRSRO. For marketplace lenders to continue to provide essential unsecured lending to low- and moderate- income individuals, our members think it is important that an overly restrictive rating requirement does not foreclose access by this important newer asset class.

Not all NRSROs rate ABS of all asset classes, and there are some asset classes that are primarily rated by only a single NRSRO. Given the post-crisis focus of many regulators on increasing competition among NRSROs, it would be counterproductive to adopt a SPARCC program that limits collateral to ABS rated by only a small subset of NRSROs. We also note the greatly increased regulatory focus on NRSROs since the financial crisis, including many rulemakings designed to strengthen them and make them more independent.

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[2] At the time, Fitch Ratings Inc., Moody's Investors Service, Inc. and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc.

Eliminate Certain Time-Consuming Requirements and Expedite Operational Start

TALF was an important program and ultimately served its purposes, but our members' experience with TALF has identified several requirements that we believe should be eliminated or modified to produce an effective SPARCC program that is appropriately tailored to address the unique market issues arising as a result of the COVID-19 pandemic. Today's crisis is immediate and sharp and is not driven by concerns about the underwriting quality of ABS collateral. For this reason, SPARCC needs to be implemented quickly and without burdensome requirements that do not commensurately increase the safety or functionality of the program.

It took several months for TALF to become operational after it was announced in 2008. A good deal of the delay was due to the requirement for the ABS sponsor to deliver an attestation opinion, in the form prescribed by the FRBNY, from a nationally recognized independent accounting firm (indicating that the sponsor's assertion that the notes are "eligible collateral" under TALF is fairly stated in all material respects). In our members' view, this requirement should not be brought forward to SPARCC. The underwriting quality of securitized assets is not a primary driver of the current crisis, which is purely driven by the unintended effects of our country's efforts to contain the COVID-19 pandemic. As noted above, we are facing an urgent liquidity crisis. The preparation time needed for accounting firms to determine how to implement these attestations delayed the effect of TALF on the markets, and the benefits that a TALF sponsor could pass on to consumer borrowers were limited by the expense associated with these attestation opinions. SPARCC should not have any such heavy burdens to entry in this time of urgency. ABS sponsors that did not participate in TALF would experience additional time burdens, as obtaining an attestation opinion would be an entirely new process to implement. This would further delay the positive impact of SPARCC on our nation's economy.

There were several documents required by TALF, including loan and security agreements and agreements among underwriters and investors. In particular, the months spent on customer agreements resulted in significant delays, and other issues with the customer agreements kept many traditional ABS investors out of the program while inadvertently favoring non-traditional ABS investors. The expedition of the operational start of the program could be facilitated if the transaction documents could be pre-reviewed and approved so as to be available in final, non-negotiable form at the time that SPARCC is implemented.

TALF had several other operational and timing requirements that may not be well-calibrated towards today's regulatory and market environment, including limited pricing and settlement dates that did not line up well with timing. We hope to work with you in the future to assist in the development of an effective and cost-efficient SPARCC program.

More Flexible Terms to Provide More Benefit to the Economy

TALF imposed "haircuts" on the market value of ABS that were pledged as collateral for loans under the program, which varied by asset class and expected life of the ABS from five percent to 16 percent. TALF loans had a maximum five-year maturity for longer-lived CMBS, student loan and SBA loan ABS, and a maximum three-year maturity for all other eligible ABS.

STRUCTURED FINANCE ASSOCIATION

Since we are facing an urgent liquidity crisis, it would be helpful if SPARCC could be calibrated even more precisely to quickly deliver lower cost credit to consumers, with a commensurately greater benefit to our troubled economy. In our members' view, the more flexibility that SPARCC allows in financing terms, including haircuts, terms and even interest rates, the greater the benefits will accrue.

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The SFA greatly appreciates the opportunity to provide our members' views on an issue of urgent importance to the U.S. economy, particularly to the interests of small businesses and low- to moderate- income individuals. The economic impacts of the COVID-19 crisis are acute and looming, and we believe a SPARCC program along the lines we have outlined would help to forestall economic disaster for those that are most financially vulnerable. We urge the Federal Reserve to take prompt action to initiate a SPARCC, or TALF 2.0, program that can be implemented quickly, and as soon as possible thereafter ensure that it is tailored to the current health crisis and resulting economic dislocations. By supporting the ABS markets, we can help restart the stalled economy and avert a surge in unemployment.

Our country's financial markets are very strong and very liquid, and they can and do deliver economic opportunity to communities and businesses all across our country. But the necessary government response to this emergency – particularly the unknown depth and duration of the effects of the pandemic – are stretching the private markets' ability to deliver the needed relief to borrowers. We stress in strongest terms that we know this crisis will pass, and that our economy can come through this. That said, this is a classic, albeit massive, liquidity trap, and immediate liquidity assistance will go far in facilitating the return of a functioning market and the ability of our markets to get back to serving borrowers and consumers across the country and aid in the swift economic recovery following this emergency health crisis.

Should you have any questions or desire any clarification concerning the matters addressed in this letter, please do not hesitate to contact me at Michael.Bright@structuredfinance.org or 202-524-6301.

Sincerely,

Michael Bright
Chief Executive Officer