

U.S. Structured Finance Newsletter

Volume 8 Issue 28, August 3 2009



Claire Mezzanotte
Managing Director, ABS/RMBS
U.S. Structured Finance,
+1 212 806 3272
cmezzanotte@dbrs.com

Jan Buckler
Senior Vice President,
Research and Modeling
U.S. Structured Finance
+1 212 806 3925
jbuckler@dbrs.com

David Hartung
Senior Vice President, ABS
U.S. Structured Finance
+1 212 806 3269
dhartung@dbrs.com

Quincy Tang
Senior Vice President, RMBS
U.S. Structured Finance
+1 212 806 3256
qtang@dbrs.com

Kathleen Tillwitz
Senior Vice President,
Operational Risk, ABS/RMBS
U.S. Structured Finance
+1 212 806 3265
ktillwitz@dbrs.com

Toronto
DBRS Tower
181 University Avenue
Suite 700
Toronto, ON M5H 3M7
+1 416 593 5577

New York
140 Broadway, 35th Floor
New York, NY 10005
+1 212 806 3277

Chicago
101 North Wacker Drive
Suite 100
Chicago, IL 60606
+1 312 332 3429

ASF PROPOSES ENHANCED RMBS REPRESENTATIONS AND WARRANTIES

On July 15, 2009, the American Securitization Forum (ASF) released a request for comment on its recommendations for the Model RMBS Representation and Warranties (reps and warranties).¹ Many market participants believe that the traditional reps and warranties and their related remedy provisions have not sufficiently provided a means to return defective loans to the originator of the loans resulting in realized losses on the issued RMBS. As a result, the ASF has sought to better align interests in future securitization transactions by enhancing and standardizing the reps and warranties as well as developing stronger repurchase obligation provisions.

The Model Reps were developed primarily to (i) appropriately allocate origination risks between issuers and investors, (ii) express customary market reps and warranties in the same, transparent language across transactions, (iii) provide a “market norm” against which investors and rating agencies can measure the reps and warranties contained in a particular transaction and (iv) provide enhanced investor protections over what had been previously provided in “precrisis” transactions. Highlights of the most important Model Reps are addressed below.

Fraud:

Historically, reps and warranties related to fraud have not been universally included in securitization transactions. In strong economic times, increasing home values and the ability of a borrower to refinance can effectively mask fraud that may have occurred. Because of this, “fraud reps” were scarce and the ones that existed only covered fraud in limited situations or they were subject to an expansive knowledge qualifier. For example, a past fraud rep might only cover fraud on the part of the depositor or seller or the liability of the depositor or seller might be limited to situations where the depositor or seller knew of the fraud, which would severely decrease repurchases due to fraud by third party originators, appraisers or other parties involved in the origination process. Consequently, the Model Fraud Rep covers fraud by any party to the origination, including originators, borrowers and appraisers.

Income/Employment/Asset Verification:

The Model Income/Employment/Asset Verification Rep requires that verification be done in accordance with an originator’s underwriting standards, that an originator employ procedures reasonably designed to authenticate the documentation and that the originator test the reasonableness of a borrower’s income where W-2s or tax returns are not provided.

Property Valuation:

The Model Property Valuation Rep requires that the appraiser be licensed by an appropriate government body, have no interest in the property and receive no benefit from or compensation for the mortgage loan’s approval or disapproval. Similar qualification and independence requirements are also applicable to real estate brokers providing broker price opinions.

Occupancy:

The Model Occupancy Rep requires that the originator test the reasonableness of the borrower’s statement of owner-occupancy, including consideration of other real estate owned, commuting distance to work and appraiser notes.

Data:

In addition to ensuring conformity of the information to the ASF RMBS Disclosure Package, the Model Data Rep also requires that the most recent FICO score for each mortgage loan be no more than four months old and that all appraisals listed on the mortgage loan schedule be no more than six months old.

Early Payment Default:

The Model EPD Rep standardizes the concept for the industry and requires repurchase of loans that become delinquent during the first three months after origination.

The Model Reps are being proposed by the ASF to provide a “market norm” against which investors and rating agencies can measure the reps and warranties contained in a particular transaction. Given the significance of the enhancement and standardization of reps and warranties to restoring investor confidence in the RMBS markets, the development of these reps is an important phase and vital to drawing investor capital back to the residential securitization industry. As a result, DBRS will continue to work with the ASF and the industry to finalize the recommendations in an effort to get them issued by the Fall of 2009.

For questions or comments, please contact Kathleen Tillwitz at ktillwitz@dbrs.com.

1. http://www.americansecuritization.com/uploadedFiles/ASF_RESTART_Representations_RFC_071509.pdf