Brazos Higher Education Authority, Inc.
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July 5, 2011

Office of the Comptroller of the Currency
250 E. Street, SW.
Mail Stop 2-3
Washington, DC 20219
Docket No. OCC-2011-002
Via E-Mail: regs.comments@occ.treas.gov

Alfred M. Pollard
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Federal Housing Finance Agency
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1700 G Street, NW.
Washington, DC 20552
RIN 2590-AA43
Via E-Mail: regcomments@fhfa.gov

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave., NW.
Washington, DC 20551
Docket No. R-1411
Via E-Mail: regs.comments@federalreserve.gov

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 7th Street, SW.
Room 10276
Washington, DC 20410-0500
Docket No. FR-5504-P-01
Via Federal eRulemaking Portal: www.regulations.gov

Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
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Washington, DC 20429
RIN 3064-AD74
Via E-Mail: comments@fdic.gov

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE.
Washington, DC 20549-1090
File Number S7-14-11
Via E-Mail: rule-comments@sec.gov

Re: Credit Risk Retention

Ladies and Gentlemen:

Brazos Higher Education Authority, Inc. ("Brazos") appreciates the opportunity to submit this letter in response to the request of the agencies listed above (the "Agencies") for comments regarding *Credit Risk Retention; Proposed Rule, 76 F.R. 24090* (April 29, 2011) (the "Proposed Rule").

The Proposed Rule was published by the Agencies pursuant to the requirements of Section 941(b) of the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd–Frank Act"), which was codified as new Section 15G of the Securities Exchange Act of 1934 (the "Exchange Act").

Background

Brazos is a nonprofit corporation organized in 1975 under the Texas Nonprofit Corporation Law and is exempt from federal income taxation under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the "Code"). For over thirty years, Brazos has been dedicated to providing assistance to the families of students who seek the opportunity for higher education and, in carrying out this vital role to society, Brazos has financed more than 2 million student loans.

In recent decades, the costs of higher education have increased dramatically. Budget constraints under state sponsored student loan programs, as well as the limits on available funds under the federal government's Federal Direct Loan Program ("FDLP")[1], have created a growing gap between the funds available to families under such programs and the amounts necessary for students to pay skyrocketing tuition. Therefore, even with the existence of state and federal aid, families are often unable to meet tuition costs without further resources. Brazos and other nonprofit student loan companies are established and designed to serve the necessary and important public policy goal of providing a means for families to bridge this gap in order for students to be able to realize the benefits of an education.

Accordingly, Brazos has been and continues to be committed to the nonprofit mission of assisting families in the all important pursuit of higher education. Brazos fulfills this commitment by originating student loans or buying student loans from originating banks, savings and loans and credit unions, which has the added benefit of increasing the lending capacity and liquidity of those institutions. The activities of Brazos are governed by the Texas Nonprofit Corporation Law.

In order to meet the increasing needs of students and their families and to perform its mission, Brazos accesses the capital markets by issuing student loan-backed securities. Brazos, like most nonprofit companies, does not issue bonds through a second step special purpose vehicle. Instead, the bonds are issued directly by Brazos under an indenture as "limited recourse obligations" that are payable solely from, and secured solely by, the student loans that are financed.

Brazos is governed by a Board of Directors currently consisting of ten directors. The directors of Brazos serve without compensation. The Articles of Incorporation and the Section 501(c)(3) designation of Brazos both provide that, after the payment of expenses and debt service, all remaining revenue must be utilized to finance additional student loans. Upon dissolution, all funds and property of Brazos are required to be (a) transferred to another organization which is exempt from federal income taxation under the Code, and which is engaged in activities substantially similar to the activities of Brazos, or (b) paid to the Federal government. Brazos has no members or equity owners.

[1] As of July 1, 2010, all subsidized and unsubsidized Stafford Loans, PLUS loans and Consolidation loans are made under FDLP.

Authority for Exemptions from the Risk Retention Requirement

Section 941(b) of the Dodd-Frank Act is intended to help align the interests of key participants in securitization transactions with the interests of investors in those securitization transactions. The Dodd–Frank Act requires, as a general matter, that the securitizer retain a portion of the credit risk of the assets being securitized. By retaining a portion of the credit risk, the Dodd–Frank Act seeks to improve the alignment of incentives among various participants in securitization transactions by requiring that securitizers maintain exposure to the credit risk of the assets that they securitize. This requirement is often referred to as "skin in the game."

Although the Dodd-Frank Act applies to securitizations generally, many of the risks it was designed to reduce arose out of the mortgage loan industry. However, both within the mortgage loan context, and with other assets classes and industries, the Dodd–Frank Act expressly recognizes that there are many circumstances in which this "skin in the game" and the regulations contemplated by the Dodd-Frank Act may not be necessary or appropriate.

Accordingly, the Dodd-Frank Act contemplates various exemptions from the risk retention requirement. For example:

- Well-Underwritten Assets. Pursuant to Section 15G(e) of the Exchange Act, permits the Agencies to issue exemptions for securitizers of assets that satisfy the underwriting standards and risk management practices specified by the Agencies.

- Qualified Scholarship Funding Bonds. Pursuant to Section 15G(c)(1)(G)(iii), of the Exchange Act contemplates an exemption for any asset-backed security that is "a security defined as a qualified scholarship funding bond in section 150(d)(2) of the Internal Revenue Code of 1986."

- Public Interest. Pursuant to Section 15G(c)(1)(G)(i) of the Exchange Act, authorizes the Agencies to provide "a total or partial exemption of any securitization, as may be appropriate in the public interest and for the protection of investors."

Pursuant to the statutory authority summarized above, the Proposed Rule contains a number of exemptions. Many of these exemptions are well-considered and will serve to further the public interest and protect investors. Given the wide variety in the types of organizations that sponsor securitizations, the classes of assets that are securitized and the structural features of securitization transactions, the Agencies have understandably and appropriately requested comments on numerous aspects of the exemptions contained in the Proposed Rule, including whether additional exemptions are appropriate.

The Agencies, therefore, have the clear statutory authority to recognize and clarify exemptions from the risk retention requirement. In particular, in connection with matters which are in the public interest such authority is set forth in Section 15G(c)(1)(G)(i) of the Exchange Act. As described above, Brazos and other nonprofit student loan companies have been long recognized (including through tax exempt status and exemptions from registration under securities laws) by federal and state agencies, as entities designed to serve and promote the necessary and vital public purpose of assisting students and families in a goal crucial to society. This goal of higher education, and the role of nonprofit student loan companies therein, is clearly something the Dodd-Frank Act intended to promote by creating the public interest exemption.

Accordingly, the risk retention requirement should not apply to Brazos and other nonprofit originators and purchasers of student loans because their function is critical to the public interest. In addition, the risk retention requirement should not apply to securitization transactions in which the securitized assets consist of student loans guaranteed under the Federal Family Education Loan Program ("FFELP Loans"). Finally, the risk retention requirement should not apply to securitization transactions in which the securitized assets consist of private student loans ("Private Student Loans") that satisfy specified underwriting criteria.

Analysis

The Risk Retention Requirement Should Not Apply to Nonprofit Student Loan Companies

As described throughout this letter, Brazos and other nonprofit student loan companies provide an essential role in helping families obtain affordable financing to cover the cost of higher education. This function is critical to the public interest because the skyrocketing cost of higher education often exceeds the amount of loans available under the federal government's FDLP and under the student loan programs of the various states and, therefore, leaving families unable to pay the full amount of tuition. Nonprofit student loan companies already have the resources, infrastructure, staff and expertise necessary to establish, implement, administer student loan programs designed to provide the necessary gap financing to families. Reducing financial barriers and encouraging deserving persons to realize their aspirations for education beyond high school is an important public purpose. Indeed, because of their critical role in furthering this important public purpose, nonprofit student loan companies already receive recognition from the federal and state government in several forms, including status as tax-exempt entities and exemption from registration requirements under the securities laws.

Brazos strongly believes that the Agencies should provide a total exemption from the risk retention requirement for student loan companies that have received Section 501(c)(3) designations under the Code. Without an exemption, nonprofit issuers of student loan-backed securities may be completely prevented from accessing the capital markets and fulfilling their important nonprofit missions.

1. Brazos and Other Nonprofit Student Loan Companies are Required to Fulfill their Public Purpose Mission

Nonprofits are required under the Code to devote their economic resources to fulfill their public missions. As such, nonprofit student loan companies are generally thinly capitalized, with all available resources devoted toward, and utilized in the advancement of, their charitable purpose. As a result, nonprofits have not retained or accumulated the large amount of capital necessary to finance a retained interest in their securitization transactions. Indeed, maintaining surplus capital is inconsistent with the very public mission that nonprofit student loan issuers such as Brazos are organized to fulfill.

Applying risk retention to Brazos and other nonprofit student loan companies threatens to put nonprofits at a distinct disadvantage relative to for-profit finance companies. For-profit finance companies, however, may engage in other business activities to generate capital and can also raise capital in the public equity markets. Nonprofit student loan companies, however, are only permitted to engage in their limited educational missions of providing affordable student loan financing to families who need educational support and are not permitted under the Code to raise equity capital in the capital markets.

2. <u>There is Already an "Alignment of Interest" Between Nonprofit Student Loan Companies and Securitization Investors</u>

In the Proposed Rule, the Agencies note that the basis of the "skin in the game" principle, as evidenced by the legislative history of the Dodd-Frank Act, is that it serves to align the economic interests of the securitizer with those of investors. Securitizers who operate on a for-profit basis are understandably motivated by economic interests that are rooted in the pursuit of maximum profits. Clearly, after the events of 2007-2008, there is cause for Congress and the Agencies to be concerned about the potential misalignment of the economic interests of profit-seeking securitizers, on the one hand, and securitization investors, on the other hand.

Brazos and other nonprofit student loan companies are motivated by completely different interests than those that motivate for-profit student loan companies. These completely different interests necessarily lead to a completely different conclusion with respect to the alignment of interests analysis.

First, there is no profit motive to tempt a nonprofit student loan company to risk its long-term reputation in the capital markets by surreptitiously lowering underwriting standards for its securitized assets in order to maximize short-term profits.[2] The Agencies should not impose a risk retention requirement to countervail a temptation that does not exist.

Second, the interests of Brazos and other nonprofit student loan companies are not only aligned, but are intertwined, with the interests of investors. Brazos and other nonprofit student loan companies are mandated by charter to provide a reliable source of affordable higher education financing for families. The only way Brazos and other nonprofit student loan companies can achieve this mandate is through continuous, long-term, access to the capital markets. It is manifestly not in the interest of Brazos or other nonprofit student loan companies to jeopardize access to the capital markets due to poor underwriting or lax monitoring of securitized assets.[3]

Third, there is no "sponsor" or "securitizer" to hold the retained risk in securitizations conducted by Brazos. Under §__.3(a) of the Proposed Rule, the "sponsor" of a securitization transaction is required to comply with the risk retention requirements set forth in the Proposed Rule. The Proposed Rule defines sponsor as "a person who organizes and initiates a securitization transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuing entity." The term "securitizer" under the Dodd-Frank Act refers to the sponsor and the depositor.

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[2] As explained by the Board of Governors of the Federal Reserve System in its Report to the Congress on Risk Retention (October 2010) (the "<u>FRB Risk Retention Report</u>"), "[o]ver time, if an originator sells relatively bad loans to securitizers, or a securitizer markets poorly structured securities or securities backed by relatively bad loans to investors, its reputation will suffer and securities with which the entity is associated will fetch lower prices. In the short run, however, investors, credit rating agencies, and other market participants might find it hard to detect bad loans or bad behavior because differences in loan quality across securities may become apparent only in downturns and may require several years of data to detect. As a result, this reputation effect may not be sufficient to overcome the "adverse selection" problems associated with securitization." *See* FRB Risk Retention Report, at 14.

[3] Similarly, the operating income of Brazos and other nonprofit student loan companies is dependent on their ability to attract and retain investors for their securitization transactions. Brazos and most nonprofit student loan companies act as primary servicers and administrators in their securitizations, thereby earning fees over the life of those transactions. In addition, the securitization residual interests held by Brazos and other nonprofit student loan companies provides operating income that is highly dependent on asset quality and diligent asset monitoring. Without this operating income, Brazos and other nonprofit student loan companies could not continue to operate.

Like many nonprofit student loan companies, Brazos originates and acquires student loans directly with the proceeds of taxable or tax-exempt bonds that it issues. Unlike a traditional securitization, Brazos does not sell or transfer assets directly or indirectly to the issuing entity; rather, Brazos itself is the issuing entity. Therefore, neither Brazos nor any other entity involved in securitization transactions conducted by Brazos, is a sponsor under the Proposed Rule or a securitizer under the Dodd-Frank Act. In a transaction without a sponsor or a securitizer, neither the Proposed Rule nor the Dodd-Frank Act requires risk retention.

The conclusion that no risk retention should apply in a securitization transaction without a sponsor or a securitizer is not the result of a mere technicality. Brazos, as the issuing entity and as the party who organizes and initiates securitization transactions, does not transfer the securitized assets (and their attendant risk) to another entity for securitization by that other entity. Rather, Brazos continues to own all of the securitized assets and pledges those assets in support of the student loan-backed securities that Brazos itself issues. Thus, Brazos effectively retains far more than 5% of the credit risk of the securitized assets. Indeed, Brazos retains all of the securitized assets and is vulnerable to losing them to foreclosure under the indenture if there is a default in one of its securitization transactions. This result is completely different than the result in a traditional securitization structure, in which the sponsor sells the securitized assets, directly or indirectly, to the issuing entity for cash, with the issuing entity, and not the sponsor, having "skin in the game."

3. <u>The Exemption for Qualified Scholarship Funding Bonds Strongly Suggests that an Exemption for all Nonprofit Student Loan Companies was Intended in the Public Interest</u>

Section 941(b) requires the Agencies to provide an exemption for "qualified scholarship funding bonds" as defined in Section 150(d)(2) of the Code.[4] Pursuant to this requirement, §__.21(a)(4) of the Proposed Rule provides that the risk retention requirement does not apply to "any asset-backed security that meets the definition of a qualified scholarship funding bond, as set forth in Section 150(d)(2) of the [Code]."

Brazos believes that this exemption under Section 941(b) strongly suggests an acknowledgement under the Dodd-Frank Act of the public interest served by nonprofit student loan companies. Accordingly, and for the reasons described throughout this letter, the language in §__.21(a)(4) should be clarified so that it applies to all nonprofit student loan companies. Such clarification could be made by the Agencies directly within §__.21(a)(4) of the Proposed Rule or as a separate section, in either case, pursuant to the statutory authority created under the Dodd-Frank Act in connection the exemptions for public interest set forth in Section 15G(c)(1)(G)(i) of the Exchange Act.

The Risk Retention Requirement Should Not Apply to Securitization Transactions Collateralized by FFELP Loans

[4] The term "qualified scholarship funding bond" is defined in Section 150(d)(2) of the Code as "a bond issued by a corporation which – (A) is a corporation not for profit established and operated exclusively for the purpose of acquiring student loan notes incurred under the Higher Education Act of 1965, and (B) is organized at the request of the State or 1 or more political subdivisions thereof or is requested to exercise such power by 1 or more political subdivisions and required by its corporate charter and bylaws, or required by State law, to devote any income (after payment of expenses, debt service and the creation of reserves for the same) to the purchase of additional student loan notes or to pay over any income to the United States."

Brazos and other student loan financing companies issue securities collateralized by FFELP Loans. Although no new FFELP Loans may be made after June 30, 2010,[5] the Department of Education has stated that approximately $450 billion of FFELP Loans remain outstanding.[6] Therefore, there will be an urgent need for some time to finance these remaining FFELP loans through new securitization transactions or restructurings of legacy securitization transactions.

The application of the risk retention requirement to securitizations of FFELP Loans does not further the policy objectives of risk retention, does not serve the public interest and does not further the interest of investors. Therefore, Brazos strongly believes that the risk retention requirement should not apply to securitization transactions collateralized by FFELP Loans.[7]

1. FFELP Loans are Guaranteed by the Federal Government and Pose Negligible Credit Risk

Pursuant to the guaranty program administered by the Department of Education, FFELP Loans benefit from a federal government guaranty of 97% to 100% of the outstanding principal amount of the loan (plus accrued interest) depending upon the year of origination and other factors. This "near full" guaranty by the federal government virtually eliminates any credit risk concern in securitization transactions collateralized by FFELP Loans.

The Proposed Rule contains a variety of full exemptions for securitization transactions in which the asset-backed securities or the securitized assets are guaranteed by the federal government. For example, §__.21(b)(2) of the proposed rule exempts asset-backed securities that are "collateralized solely (excluding cash and cash equivalents) by assets that are *fully insured or guaranteed* as to the payment of principal and interest by the United States or an agency of the United States by obligations issued by the United States" (emphasis supplied).

However, other full exemptions from the risk retention requirement are based on federal government guarantees that are not "full" guarantees. For example, §__.21(a)(1)(i) exempts any securitization transaction that "is collateralized solely (excluding cash and cash equivalents) by residential, multifamily, or health care facility mortgage loan assets that are insured or guaranteed as to the payment of principal and interest by the United States or any agency of the United States." The Agencies provide two examples of assets that would qualify for a full exemption under §__.21(a)(1)(i) despite being only partially guaranteed by the federal government:

- loans under a Department of Veterans Administration Program in which the federal government guarantees between 25% and 50% of lender losses in the event that the residential borrower defaults;[8] and

[5] On March 30, 2010, President Obama signed into law H.R. 4872 – the Health Care and Education Reconciliation Act of 2010 ("HCERA"). Effective July 1, 2010, the HCERA eliminated the Federal Family Education Loan Program. HCERA provides that after June 30, 2010, no new student loans may be made under the Federal Family Education Loan Program.
[6] *See* Department of Education "Fiscal Year 2011 Budget Request" at page T-20.
[7] If the Agencies are not inclined to provide an exemption for securitizations collateralized by FFELP Loans, the Agencies should apply the risk retention requirement to only that portion of the securitized pool of FFELP Loans not covered by the federal government guarantee as described below.
[8] *See* Proposed Rule, at 24136.

- loans under a United States Department of Agriculture Rural Development program in which the federal government guarantees a sliding amount against loss up to 90% of the original loan amount for single family loans.[9]

FFELP Loans benefit from a higher level of federal government support than the examples cited above. In addition, the practical elimination of credit risk achieved through a government guaranty is not the only rationale for exempting securitization transactions collateralized by assets guaranteed by the federal government. As the Agencies have noted, "the federal department or agency issuing, insuring or guaranteeing ABS or collateral would monitor the quality of the assets securitized, consistent with the relevant statutory authority."[10] With respect to FFELP Loans, the Department of Education clearly has the statutory authority and the institutional interest to monitor asset quality.

2. Risk Retention Will Have No Effect on the Standards Used to Underwrite FFELP Loans

As noted above, the Federal Family Education Loan Program was ended in 2010. No new FFELP Loans have been made or will be made since June 30, 2010. The application of a risk retention requirement to new securitizations (or restructurings of legacy securitizations) will not (and can not) have any effect on the standards used to underwrite FFELP Loans.

The FFELP Loans that remain outstanding were required to be underwritten and serviced in accordance with the requirements of the Federal Family Education Loan Program. Among other criteria, a student was eligible for a FFELP Loan only if he or she:

- was a United States citizen, national or permanent resident;
- had been accepted for enrollment or was enrolled in good standing at an "eligible institution" of higher education; and
- met the applicable "needs" requirement.

Eligible institutions include higher educational institutions and vocational schools that comply with specific federal regulations. In order to qualify, a student must have been carrying, or planning to carry, at least one-half the normal full-time work load for the course of study the student was pursuing at the applicable eligible institution.

The Risk Retention Requirement Should Not Apply to Securitization Transactions Collateralized by Qualifying Private Student Loans

Section 941(b) of the Dodd-Frank Act provides the Agencies with broad authority to exempt certain asset classes from the risk retention requirement, so long as such exemption helps to ensure high quality underwriting standards and encourages appropriate risk management practices. Although many of the events of 2007-2008 were the result of circumstances in the mortgage loan market, the Proposed Rule recognizes the appropriateness of certain exemptions from the risk retention requirement for securitization transactions in which the underlying securitized assets are qualifying residential mortgage loans, commercial loans, commercial real-estate loans or automobile loans. The Agencies have requested comment as to whether additional qualifying asset classes should be established.

[9] *Id.*
[10] *Id.*, at 24137.

Brazos believes that because collections on Private Student Loans have been consistent and have not been the subject of volatility due to other factors which have affected the capital markets, the Agencies should provide a risk retention exemption for securitization transactions backed by Private Student Loans that meet specified underwriting and other criteria ("Qualifying Private Student Loans"). Brazos further believes that an exemption for Qualifying Private Student Loans would facilitate lending to qualified borrowers at lower interest rates and on more favorable terms than what might otherwise be commercially available, thus making higher education more affordable. Such an exemption would serve the underlying purpose motivating the risk retention requirement by requiring that securitized Private Student Loans be underwritten to high standards and in accordance with sound risk management practices.

Among the criteria that should be included in the definition of Qualifying Private Student Loan are: (1) type of school, (2) whether the loan is co-signed by a parent, (3) FICO scores of applicant and co-signer and (4) other data that shows historical payment performance. The criteria for the Qualifying Private Student Loan exemption should also include the same type of risk management and monitoring requirements as those specified in the qualifying asset exemptions included in the Proposed Rule.

Conclusion

The Dodd-Frank Act authorizes the Agencies to provide "a total or partial exemption of any securitization, as may be appropriate in the public interest and for the protection of investors." There is no policy reason to impose a risk retention requirement on Brazos and other nonprofit student loan companies. If Brazos and other nonprofit student loan companies are required to retain risk as set forth in the Proposed Rule, their ability to fulfill their charitable purpose will be impaired. In addition to exempting nonprofit student loan companies, the Agencies should also exempt securitization transactions backed by FFELP Loans and Qualifying Private Student Loans.

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We very much appreciate the opportunity to provide the foregoing comments on the Proposed Rule. We are available at your convenience to discuss our comments. Should you have any questions or desire any clarification concerning the matters addressed in this letter, please do not hesitate to contact the undersigned at (254) 753-0913 or murray.watson@brazos.us.com.

Very truly yours,

BRAZOS HIGHER EDUCATION AUTHORITY, INC.

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