Lenders Compliance Group

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Resecuritizing the RMBS Portfolio

The Comptroller of the Currency (OCC) has recently concluded that the resecuritization of certain residential mortgage-backed securities by a bank is permitted through its subsidiary.

In its Interpretive Letter # 1133 (September 2011), the OCC determined that a bank could consummate a certain type of structured transaction in order to enhance the marketability of the underlying interests and its liquidity position and to address regulatory concerns relating to its exposure to non-investment grade securities.

The OCC's consent was based, among other things, on the petitioning bank's representations that it would adhere to prudential requirements and supervisory guidance on safe and sound banking practices and that it would establish and maintain, to the OCC's satisfaction, "an adequate and effective risk measurement and management program."

Re-Packaging Risk

Here is a brief overview of this resecuritization plan:

- A real estate mortgage investment conduit (REMIC) is one type of vehicle used for securitizing mortgage loans, and it is subject to a specialized set of tax rules. [A Re-REMIC (Re-REMIC) transaction involves the resecuritization of the residential mortgage-backed securities (RMBS) issued by the REMIC. Re-REMIC transactions can have structural differences.]
- The Re-REMIC Transaction would involve a bank transferring the RMBS to a limited purpose subsidiary of that bank.
- This limited purpose subsidiary would form several trusts and transfer several RMBS to each trust.
- Each trust would then issue new securities backed by the RMBS (Re-REMIC Securities) to the limited purpose subsidiary.
- Thereafter, through its limited purpose subsidiary, the bank would hold the Re-REMIC Securities to maturity, but would have the ability to sell them if market conditions improve. It is believed that the Re-REMIC Securities, on the whole, would be more marketable and liquid than the original RMBS.
- A "nationally-recognized statistical rating organization" would rate the Re-REMIC Securities based on a credit and cash flow analysis of the underlying loans, rather than based on the RMBS.

Analysis

The OCC determined that the bank could consummate the transaction and hold the Re-REMIC securities resulting from the transaction. According to the OCC's Interpretive Letter, a bank's authority to securitize assets it holds includes the authority to securitize assets that are securities.

The Interpretative Letter states that a bank may securitize the RMBS through a Re-REMIC Transaction and hold the resultant Re-REMIC Securities.

The letter further states that there is no distinction between securitizing internally generated assets and securitizing other permissibly held assets.

The OCC also concluded that a bank may hold the investment-grade Re-REMIC securities as Type V securities. (A Type V security is a security that is rated investment grade; marketable; not a Type IV security; and fully secured by interests in a pool of loans to numerous obligors in which a national bank could invest directly. The aggregate par value of Type V securities held by the bank that are issued by any one issuer may not exceed 2% of a bank's capital and surplus.)

By restructuring its assets in the Re-REMIC transaction, a bank would enhance the marketability of the underlying assets, improving its liquidity position and reducing its amount of non-conforming assets.

The purpose of the Re-REMIC Transaction, then, is to allow for a "better reflection of the true economic value of the nonperforming and nonconforming RMBS as economic conditions

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true economic value of the nonperforming and nonconforming RMBS as economic conditions improve," and to thereby enhance the marketability of the RMBS assets and the bank's liquidity position.

Some Notes

It should be noted that the Re-REMIC Transaction is not entered into for the purpose of obtaining "capital relief," and, accordingly, a bank would still hold capital against the RMBS (rather than the Re-REMIC Securities) for so long as the RMBS remain on the bank's balance sheet.

Also noteworthy is that the petitioning bank expects, based upon previous discussions with nationally recognized debt rating agencies, that "the aggregate book value of the non-investment grade Re-REMIC Securities will be substantially less than the aggregate book value of the investment-grade Re-REMIC Securities at the commencement of the Re-REMIC Transaction."

The OCC said that this transaction was a "modern variation" of the type of asset restructuring long recognized as permissible for national banks.

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Comptroller of the Currency (OCC)

Resecuritization of Certain Residential Mortgage-Backed Securities

Interpretive Letter #1133

September 2011

Labels: Interpretive Letter 1133, OCC, Office of the Comptroller of the Currency, Re-REMIC, Re-Securitization, Real Estate Mortgage Investment Conduit, REMIC, Residential Mortgage-Backed Securities, RMBS

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