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Via Electronic Mail

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Re: Response to Standard & Poor’s Request for Comment:
Methodology for Rating Interest-Only Certificates

Ladies and Gentlemen:

The Commercial Mortgage Securities Association (CMSA) submits this letter in response to Standard & Poor’s Request for Comment on the proposed Methodology for Rating Interest-Only Certificates dated June 1, 2009. CMSA is the global trade organization for commercial real estate finance. In the United States alone, the amount of securities issued via the Commercial Mortgage Backed Securities (CMBS) market is approximately \$1 trillion while non-U.S. issuance is approximately US\$315 billion, which includes markets within Canada, Japan, pan-European and United Kingdom. The organization’s primary mission is to promote the ongoing strength, liquidity and viability of commercial real estate capital market finance worldwide. Based in New York, with a government relations office in Washington, DC as well as a strong presence in Canada, Europe and Japan, CMSA is the voice of the entire industry, with a diverse global membership of over 400 member firms represented by more than 5,000 individuals who actively engage in commercial real estate capital market finance activities. These members embody the full spectrum of the CMBS market, including senior executives at the largest banks and investment banks, insurance companies, investors such as money managers and specialty finance companies, servicers, other service providers to the industry, as well as the rating agencies, including Standard & Poor’s, DBRS, Fitch Ratings, Moody’s and Realpoint.¹ CMSA and its members are the leaders in setting standards and maintaining a favorable investing environment, and we submit these comments in an effort to further advance these dual objectives.

¹ This letter does not reflect the views of CMSA’s credit rating agency members.

In the request for comment, S&P proposes to change its methodology for rating interest-only certificates (IO's) across the spectrum of CMBS, residential mortgage-backed securities and other asset-backed securities. Inasmuch as the proposed changes move in the direction of evaluating credit risk associated with IOs, CMSA believes the proposed changes are a positive development. However, the proposal to link IO ratings to the lowest rating associated with the notional balance of the collateral would overstate the credit risk inherent in the IO security. Our members recommend that S&P consider an approach that looks to the weighted average of the ratings associated with the notional balance of the collateral that an IO references. Just as a pool of mortgage loans is itself not merely as creditworthy as the least creditworthy borrower under one of the mortgage loans in the pool, so too an IO should not be considered only as good as the lowest rated portion of its notional balance of referenced collateral. The weighted-average ratings approach provides greater consistency of IO ratings with credit ratings of other fixed- income securities.

The proposed Methodology expresses concern that “holders of IO securities may receive less interest and therefore a lower-than-expected investment return...” as a result of collateral-level defaults. The triple-A ratings received by CMBS IO securities in all their forms – WAC IO, PAC IO, companion IO – do not reflect the rating agencies’ views on the underlying credit quality of the security, but explicitly on its position in the cash-flow waterfall. IO securities do not have a principal balance but only a notional balance on which interest payments are based. Thus, the valuation of a CMBS IO tends to be extremely subjective, as it is based on individual investors’ projections of loan-level defaults and losses, and the timing of those losses on a given pool. Investors value IO securities by determining how loan-level defaults and losses affect the size of the IO’s notional balance over time and thus the interest cash-flow stream they will receive. Therefore, it would be difficult for S&P to adjust its ratings purely based upon lower-than-expected investment returns since investors’ initial expectations of returns (and inherent collateral default assumptions) are not readily available.

As CMSA has expressed now in several responses to requests for comment from S&P on various topics, our members believe strongly that securities ratings should be comparable across all types of credits. As the request for comment notes, S&P’s ratings for IOs to date have related to the IO’s senior position in the cash-flow waterfall and thus the contractual promise to pay interest to IO investors, but have not addressed the credit risk that realized losses due to collateral-level defaults will reduce the IO’s notional amount. In this sense, the methodology behind – if not the very meaning of – an S&P rating on an IO has historically been fundamentally different than that associated with an S&P rating on any other type of security. CMSA therefore believes the basic concept behind the request for comment, namely that IO ratings should reflect such credit risk, is a sound and positive step in the right direction.

Where CMSA believes the proposal falters, however, is in linking the rating of an IO according to the lowest rating associated with the notional balance of the collateral an IO references. IO securities can be viewed as a portfolio of cash flow strips, each of which benefit from the levels of credit enhancement established at the initial rating of the underlying transaction. As such, we believe the ratings of IO securities should reflect the

composition of the credit quality of the underlying securities from which the notional balance is based.

Accordingly, CMSA respectfully submits that an approach that considers the weighted average of the ratings associated with the components of an IO's notional balance would result in a rating that more accurately reflects the credit risk associated with that IO.

A weighted average approach presumably will involve an analysis similar to that undertaken for the related transaction as a whole, making the IO rating more comparable in meaning to the ratings assigned to other securities in the transaction and in all similar transactions. Such a rating also will more accurately reflect the totality of credit risk associated with the IO, because it requires consideration of the credit risk associated with the components that make up the IO's notional balance, rather than simply assuming the worst. As such, the rating will be a "credit" rating in substance as well as in name, and thus more comparable to credit ratings assigned to securities based on other types of financial assets and corporate credits. A weighted average approach thus better achieves the objectives of the request for comment and the larger goal of ratings consistency. Finally, CMSA's members believe that the non-credit risks – such as asset prepayments and termination risks – that are associated with IOs do not have meaningful corollaries in other types of securities, and thus agree with S&P that such risks should continue not to be considered when rating IOs.

CMSA appreciates the opportunity to comment on this proposal and would be happy to engage in further dialogue with S&P regarding its proposed methodology for rating IOs. Please do not hesitate to contact us with any questions or comments.

Sincerely,

A handwritten signature in blue ink, appearing to read "Dottie Cunningham". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Dottie Cunningham
Chief Executive Officer