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August 31, 2012

Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219
Docket Number OCC-2011-0002
RIN 1557-AD40

Jennifer J. Johnson, Secretary
Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket Number 2011-1411
RIN 7100-AD70

Robert E. Feldman, Executive Secretary
Attention: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
RIN 3064-AD74

Ms. Elizabeth M. Murphy, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
File Number S7-14-11
RIN 3235-AK96

Alfred M. Pollard, General Counsel
Attention: Comments/RIN 2590-AA43
Federal Housing Finance Agency
Fourth Floor
1700 G Street, NW
Washington, DC 20552

Regulations Division
Office of General Counsel
Department of Housing and Urban Development
451 7th Street, SW, Room 10276
Washington, DC 20410-0500
RIN 2501-AD53

RE: Credit Risk Retention

Sirs and Madames:

The logo for Ashurst LLP, featuring the word "ashurst" in a lowercase, orange, sans-serif font.

The undersigned sponsors of tender option bond programs ("TOB Programs"), together with the Investment Company Institute (the "ICI"),¹ which represents both purchasers of tender option bond floating rate certificates and purchasers of tender option bond residual interests, submit this letter to supplement their initial responses² (the "Initial Comment Letters") to the request of the Office of the Comptroller of the Currency, Treasury; the Board of Governors of the Federal Reserve System; the Federal Deposit Insurance Corporation; the U.S. Securities and Exchange Commission (the "SEC"); the Federal Housing Finance Agency; and the Department of Housing and Urban Development (collectively, the "Agencies") for comments on proposed rules (the "Proposals") to implement the credit risk retention requirements of section 15G of the Securities Exchange Act of 1934 (15 U.S.C. §78o-11), as added by section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. We appreciate the opportunity to supplement our initial comments on the Proposals.

We are banking entities and the trade association for registered investment companies ("registered funds"), including money market funds, long-term bond funds and closed-end funds. Together we represent the interests of the overwhelming majority of the participants in the tender option bond market ("TOB Program Participants").³ Notwithstanding the different roles that the TOB Program Participants each play and the benefits to each of participating in this market, we all agree that imposing the proposed risk retention requirements on TOB Programs is not necessary pursuant to the stated intent of the law and, therefore, would not further its purpose.

Specifically, the TOB Program Participants and the ICI firmly believe that TOB Programs should be identified as transactions that "would be properly exempted from the risk retention requirements" that would be imposed on securitization transactions generally under the Proposals. To the extent that the Agencies do not agree, we request that the Agencies adopt a separate form of risk retention requirement that specifically addresses TOB Programs and their structural nuances.

For ease of your review, we have organized our letter by the specific requests for comment to which we are responding. We ask that this letter be read in conjunction with the Initial Comment Letters, which elaborated on many of the key structural features of a TOB Program trust.⁴

1. REQUESTS FOR COMMENT 173(A) AND (B)

1.1 *Requests for comment 173(a) and (b) ask: Are there securitization transactions that would not be covered by the exemptions in the proposed rules that should be exempted from risk retention requirements pursuant to section 15G(e)(3) of the Exchange Act?⁵ If so, what are the features and characteristics of such securitization transactions that would properly exempt them from risk retention requirements pursuant to section 15G(e)(3)?*

(a) For the following reasons set forth in greater detail in the Initial Comment Letters, we believe that all TOB Programs should be exempt from the risk retention requirements.

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange traded funds, and unit investment trusts. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors and advisers. Members of ICI manage total assets of \$13.1 trillion and serve over 90 million shareholders.

² Letter from Ashurst on behalf of Citibank, N.A., Deutsche Bank AG, New York Branch, Societe Generale, New York Branch, and Wells Fargo Bank, N.A. dated August 1, 2011; Letter from The Investment Company Institute dated July 29, 2011.

³ Banking entities provide liquidity, remarketing and/or depositor services to all TOB Programs. We estimate that long-term bond funds and closed-end funds own 30 to 40% of the total value of outstanding TOB Program residual interests, banking entities own 45 to 60%, with other entities owning no more than 5%.

⁴ We have attached at [Appendix A](#) to this letter a more detailed description of TOB Program assets and the TOB Program structure. We have attached at [Appendix B](#) to this letter a graphic description of TOB Program Participants and the TOB Program market.

⁵ Section 15G(c)(1)(G)(iii) exempts from the statutory risk retention requirements asset-backed securities that are issued by states and municipalities. Because the securities that are issued under TOB Programs are issued by a TOB trust (and not by states or municipalities), technically TOB Program securities may not satisfy the requirements for the section 15G(c)(1)(G)(iii) exemption.

- (i) TOB Programs are almost uniformly used to finance municipal securities, not to transfer risk.
 - (ii) The TOB Program structure (A) ensures that the interests of the securitizer are closely aligned with those of the holders of tender option bond floating rate certificates, and (B) provides all participants with transparency regarding the TOB Program assets.
 - (iii) TOB Program assets are high quality and are typically publicly issued, rated debt securities that are subject to the anti-fraud provisions of the federal securities laws.
 - (iv) TOB Programs are vital to both the municipal securities market and the tax-exempt money markets.
- (b) Further, each of the TOB Program Participants is subject to existing regulations that ensure that its participation in TOB Programs does not present an undue risk to itself, other investors, or the financial system.
- (i) Banking entities, which sponsor and provide liquidity facilities for TOB Programs and also hold residual interests, are subject to strict capitalization requirements and limitations on their activities that have been designed to minimize risk to the institutions and the financial system.⁶ When a TOB Program sponsoring bank is the residual interest holder it consolidates the underlying TOB trust assets on its balance sheet for accounting purposes (with a corresponding liability for the liquidity extended with respect to the floating rate certificates); investment in a TOB Program residual interest is not an "off balance sheet" transaction. Banking entities are required to hold capital against the risk-weighted assets of the consolidated TOB trusts.
 - (ii) Money market funds, which purchase the vast majority of TOB Program floating rate certificates, are subject to Investment Company Act rule 2a-7, which has been designed -- and recently strengthened -- to ensure that those funds hold the highest quality assets subject to minimal credit risks.
 - (iii) Registered funds, including long-term bond funds and closed-end funds, which buy residual interests, are subject to strict asset segregation and disclosure requirements that are designed to protect investors with respect to assets such as TOB Program securities.⁷ As with banking entities, registered funds that hold residual interests reflect the underlying municipal securities on their balance sheets.
- (c) Additionally, although TOB Program securities may appear exotic to those not familiar with them, they are well understood by the institutional investors who buy them. Those institutional investors, in turn, perform not only initial due diligence on, but ongoing monitoring of, the individual underlying municipal securities in the TOB trust and the liquidity facility provider to protect their interests as well as the interests of their shareholders.

⁶ Banking entities are subject to limitations on the type and amount of activities in which they can engage. For example, banking entities governed by the Bank Holding Company Act are subject to section 4(c)(8) thereof and section 225.28(b) of Regulation Y, which lists permissible nonbanking activities.

⁷ Registered funds are required to treat residual interests as senior securities unless they segregate unencumbered, liquid assets with a value at least equal to the amount of the floating rate certificates plus accrued interest. See SEC Investment Management Staff Issues of Interest Summary: Funds Using Tender Option Bond Financings (March 29, 2012). Because open end funds are not allowed to issue senior securities and closed end funds have strict asset coverage requirements that apply to senior securities, this position for all practical purposes limits the amount of leverage such funds can maintain through TOB residual interests.

- (d) Accordingly, there is no need to attempt to further align the interests of those who sponsor TOB Programs with those who invest in TOB Program securities by imposing the risk retention requirements of section 15G.
- (e) If the Agencies determine that, despite the reasons provided in the Initial Comment Letters and above, a full exemption for TOB Program transactions is not permitted or appropriate, then the TOB Program Participants and ICI request that, as an alternative, the Agencies develop risk retention requirements specifically designed for TOB Programs, as described in Section 2 below.

2. **REQUEST FOR COMMENT 19(A) AND 19(B)**

- 2.1 *Request for comment 19(a) and 19(b) ask: Are there other forms of risk retention that the Agencies should permit? If so, please provide a detailed description of the form(s), how such form(s) could be implemented, and whether such form(s) would be appropriate for all, or just certain, classes of assets.*
- 2.2 Due to the structure of TOB Programs, which is largely dictated by tax law,⁸ the residual interest in a TOB Program does not meet the risk retention requirements under any of the proposed permissible forms of risk retention.⁹ Accordingly, we believe that, in the event the Agencies determine that some level of risk retention is required for TOB Programs in certain circumstances, the Agencies should create a new risk retention method specifically for TOB Programs. That method should permit a choice among one or more of three options to meet the requirements of section 15G. Each of these alternative methods of risk retention is consistent with the Proposals in that each would ensure that a participant bears at least 5% risk of loss, due to either (i) its exposure to any decline in the market value of the underlying assets, (ii) the amount of its upfront cash investment in the TOB Program trust, and/or (iii) its independent parallel investment in other municipal securities having the same credit risk as the municipal securities in the TOB Program trust.
- 2.3 Option 1: A TOB Program transaction in which the residual interest holder is either (i) the same as, or an affiliate of, the entity that provides a liquidity facility,¹⁰ or (ii) an unaffiliated entity that agrees to reimburse the liquidity facility provider for any losses,¹¹ would have a risk retention requirement of 0%, in recognition of the fact that all of the market risk associated with the underlying assets is already borne by the residual interest holder.
- (a) Unlike most other asset backed securities programs, TOB Programs involve significant market risk to the residual interest holder¹² in addition to the pro rata sharing of credit

⁸ For tax-exempt interest to be passed through to both TOB floating rate certificates and the residual interest, the federal tax laws require that they each share in the benefits and burdens of ownership of the underlying trust assets. As a result, the residual interest cannot be structured as a first loss position.

⁹ A TOB residual interest is not a first loss position, so the horizontal form of risk retention is not met; the residual interest holder does not typically purchase any floating rate certificates, so the vertical risk retention option is not met; TOB Program trust assets are not revolving lines of credit, so the seller's interest risk retention option cannot be met; and a TOB Program does not involve 1,000 separate assets from which to draw a representative sample, so the representative sample option cannot be met. The other risk retention options address distinct types of securitizations that do not include TOB Programs.

¹⁰ In a TOB Program, floating rate certificate holders have the right to tender their interests for any reason for a repurchase price equal to 100% of the face amount of the floating rate certificates, plus accrued interest. The residual interest holder has the right, exercisable at periodic intervals, to cause the sale of the municipal securities and the forced redemption of the floating rate certificates for 100% of par value plus accrued interest and any applicable gain share. The liquidity facility provides funds for payment of both principal and interest on the floating rate certificates whenever a floating rate certificate holder exercises its tender option or the residual interest holder calls the floating rate certificates for mandatory tender.

¹¹ In many TOB Programs, the residual interest holder is obligated to reimburse the liquidity provider for all amounts paid to floating rate certificate holders and not otherwise reimbursed from a remarketing of tendered certificates or, if the certificates are not remarketed, from the proceeds of the sale of the municipal securities.

¹² The liquidity facility provider in a TOB Program is contractually obligated to pay the floating rate certificate holders par plus accrued interest in the event that tendered certificates are not successfully remarketed, regardless of the market value of the

risk between the floating rate certificate holders and the residual interest holder.¹³ This market risk alone could result in losses to the residual interest holder far in excess of the face amount, or initial cash investment, of the residual interest. The market risk aspect of TOB Programs is a result of the combination of the tender option/liquidity feature of the floating rate certificates and an active market in the underlying collateral, both of which distinguish TOB Programs from other types of asset backed securities programs. The residual interest holder bears all of this risk either directly, when the residual interest holder is the same entity as, or an affiliate of, the liquidity provider, or indirectly when the residual interest holder agrees to reimburse the liquidity provider for any losses. In both of these circumstances, this market risk already aligns the interest of the residual interest holder with the interest of the other participants in the TOB transaction that the assets in the TOB trust not lose value.

- (b) We believe that 100% market risk, along with the pro rata credit risk in the event of a tender option termination event, is a more than adequate substitute for a 5% credit risk under any of the currently proposed risk retention methods. It provides greater protection to floating rate certificate holders under a much broader and more dynamic set of market-driven circumstances than a 5% risk of loss only in the event of default or other significant credit event. To our knowledge, no tender option termination event has ever occurred in the history of the TOB market. In contrast, market risk has materialized many times and in some instances quite dramatically. This market risk has resulted in losses for liquidity providers as well as residual holders, but never any losses for holders of TOB floating rate certificates.

2.4 Option 2: The credit risk retention requirement would be satisfied by purchasing and retaining a residual interest having an up-front cash investment value equal to five percent of the initial market value of the municipal securities in the TOB Program.

- (a) A TOB floating rate certificate is a liquid, money market eligible security; therefore, requiring a residual interest holder to purchase TOB floating rate certificates (that is, meeting the vertical risk retention method) would not materially increase the residual interest holder's exposure to the overall risk of the underlying municipal securities.
- (b) As explained in Section 2.3(a) above, the nature of a residual interest in a TOB Program creates market risk for the holder that other forms of asset backed securities interests do not have. That risk creates a complete alignment of interest between the residual interest holder and the floating rate certificate holder regarding the value of the underlying collateral.
- (c) Because (i) the residual interest holder bears all market risk prior to the occurrence of a tender option termination event, and (ii) any credit losses are shared pro rata between the floating rate certificates and the residual interest after the occurrence of a

underlying municipal securities. If the liquidity provider is required to make any such payments, then the underlying municipal securities are sold and the proceeds are used to reimburse the liquidity provider for those payments. If the proceeds of sale are insufficient to repay the liquidity provider for the amount of the payments, then there is a shortfall that is characterized as the "market risk" (i.e., the risk that the value of the assets in the TOB trust is lower than the amount of the liquidity provider's exposure at any time). When the liquidity provider and the residual interest holder are the same entity (or affiliated entities), that entity will always bear all of the market risk associated with owning the underlying municipal securities. Likewise, when an unaffiliated residual interest holder is unconditionally obligated to reimburse the liquidity provider, it also bears all of the market risk of the underlying municipal securities. These two structures are known as "recourse structures."

¹³ In very limited circumstances, known as tender option termination events, the liquidity provider's obligation terminates. The following are the four typical tender option termination events: a default on the underlying municipal securities and credit enhancement, where applicable; a credit rating downgrade below investment grade; the bankruptcy of the issuer and, when applicable, the credit enhancer; and the determination that the municipal securities are taxable. If a tender option termination event occurs, then the residual interest holder and the floating rate certificate holder share in any losses pro rata. Accordingly, in addition to the market risk described above, the residual interest holder bears credit risk on a pro rata basis with the floating rate certificate holders. For tax reasons and because of other legal considerations, the residual interest cannot be first loss position.

tender option termination event, holding the residual interest in a TOB Program is equivalent to holding horizontal risk prior to the occurrence of a tender option termination event and a seller's interest after a tender option termination event. Therefore, the approach suggested in this proposed Option 2 (i.e., a minimum residual interest amount without a first credit loss requirement) is not without precedent; it merely combines the concepts of two of the previously proposed risk retention methods in a way that allows TOB Programs to function without unnecessary and inefficient structural changes.

- (d) For purposes of this proposed Option 2, we would suggest that a residual interest holder's up-front cash investment take into account both (i) the purchase price of the residual interest, and (ii) the value of any liquid collateral that the residual interest holder is required to deposit with the liquidity provider to secure the liquidity provider for any losses.¹⁴ In both instances, the residual interest holder has contributed cash at the outset that is at risk of loss for the life of the TOB trust.

2.5 Option 3: TOB Program transactions would be subject to a credit risk retention amount equal to the excess of 5% of the initial market value of the municipal securities in the TOB Program over the initial market value of municipal securities that the residual interest holder owns directly outside the TOB Program that have the same credit risk (that is, securities issued by the same issuer with the same source of payment and same payment priority), up to and including a full offset (i.e., the risk retention amount inside the TOB trust may be 0%).¹⁵

- (a) In such circumstances, it is clear that the residual interest holder is exposed to the risk of the collateral underlying the TOB Program securities, albeit outside rather than inside the securitization vehicle. This exposure creates the alignment of interest that the credit risk retention rule was designed to achieve. Accordingly, there is absolutely no reason to require the residual interest holder to retain an additional interest in the TOB Program securities themselves.
- (b) As an example, if at inception of the TOB trust an entity owned \$100 million market value of State of Texas General Obligation Bonds, then it could place \$95 million market value of those bonds into a TOB trust and purchase a residual interest in that trust in an amount as little as \$5,000, because the risk retention requirement would be met by holding \$5 million outside of the TOB trust. The residual interest holder would not be allowed to sell or hedge the credit risk of the \$5 million held outside the TOB trust as long as the TOB trust was outstanding.

2.6 All three of these options are necessary to address the various circumstances and structures that exist with respect to TOB Programs. TOB Program Participants are not always similarly situated; therefore, no one option works for all of them. Accordingly, these three options should not be exclusive of each other. For example, an entity with a less than total offset under Option 3 should be able to meet its risk retention requirement through acquiring and maintaining a residual interest as provided in Option 2.

2.7 We urge that any risk retention requirements apply prospectively only; that is, these requirements or any others the Agencies establish should not apply to TOB Program trusts in existence on the effective date of the implementing rules. Otherwise sponsors of TOB

¹⁴ When the residual interest holder is an entity that is not related to the liquidity provider, it is very common for the liquidity provider to require the residual interest holder to post cash or cash equivalent collateral at the time of closing to secure the liquidity provider for any losses, particularly when the residual interest holder has not agreed to a full recourse obligation to reimburse the liquidity provider for any losses and when the leverage ratio is higher than 2:1. The liquidity provider typically holds this collateral, in the form of a fixed "independent amount," as security during the entire life of the TOB trust.

¹⁵ To the extent that municipal securities in the TOB trust mature or are redeemed during the life of the TOB Program, the base amount for purposes of the calculation would be adjusted to reflect the book value of the municipal securities remaining in the trust.

Programs could be forced to choose between engaging in costly restructuring transactions or unwinding TOB Programs at a time or under circumstances that are detrimental to sponsors, liquidity providers, residual interest holders and/or floating rate certificate holders, as well as the municipal markets in general.

2.8 Form of Disclosure and Compliance. We suggest that the Agencies require the securitizer of a TOB Program to provide, or cause to be provided, to potential purchasers of floating rate certificates a reasonable time prior to the sale of those certificates and, upon request, to the SEC and to its appropriate Federal banking entity (if any):

- (a) the amount (expressed as a percentage and a dollar amount) of residual interest and, if applicable, the amount and/or type of other forms of approved risk retention (based on Options 1-3 above) the securitizer will retain (or did retain) at closing as well as the amount (expressed as both a percentage and a dollar amount) and/or type that it is required to retain under the rules;
- (b) a description of the material terms of the residual interest and, if applicable, other forms of retained risk (based on Options 1-3 above); and
- (c) the material assumptions and methodologies it used to determine the aggregate dollar amount of floating rate certificates issued by a TOB trust.

3. **REQUEST FOR COMMENT 12(A) AND 12(B)**

3.1 *Requests for comment 12(a) and 12(b) ask: Would the minimum five percent risk retention requirement, as proposed to be implemented, have a significant adverse effect on liquidity or pricing in the securitization markets for certain types of assets? If so, what adjustments to the proposed rules (e.g., the minimum risk retention amount, the manner in which credit exposure is measured for purposes of applying the risk retention requirement, or the form of risk retention) could be made to the proposed rules to address these concerns in a manner consistent with the purposes of section 15G? Please provide details and supporting data.*

3.2 TOB Programs are beneficial for the municipal securities market for a variety of reasons.

- (a) If the risk retention requirements under the Proposals are imposed on TOB Program securitizers, thereby requiring that they increase their investment in each TOB trust, then in the case of proprietary programs,¹⁶ sponsors may no longer finance their acquisition of municipal securities with TOB Programs, but could simply turn to a different form of financing, which could increase the cost of financing municipal securities, reduce demand for municipal securities, and reduce supply of eligible investments for money market funds.
- (b) Because TOB Programs are the only form of municipal securities structured financing that creates money market fund eligible securities (in the form of floating rate certificates), the indirect market for municipal securities would diminish, perhaps substantially.
- (c) Municipal Markets Advisors, Inc. ("MMA") submitted testimony to the Senate Committee on Finance in May 2011.¹⁷ In that testimony, MMA indicated that the volatility in the municipal market starting in 2007 was due to the integration of leverage into municipal bond buying strategies through TOB Programs. We strongly

¹⁶ In a proprietary program, a banking entity uses a TOB Program to finance its own investment in municipal securities.

¹⁷ MMA's Perspective: Financing of Infrastructure and the Role the Municipal Market Plays, testimony of Matt Posner, Director, MMA (May 17, 2011) ("MMA Testimony"),

disagree with this conclusion.

- (A) The MMA testimony misconstrues the cause of the municipal market volatility. The volatility in late 2007 and 2008 in the municipal markets was due to certain single strategy hedge funds that used TOB Program residual interests to take a leveraged long position in municipal securities financed with the sale of the floating rate certificates on a ten-to-one basis, at the same time they were holding short positions on 30 year LIBOR swaps. The breakdown in the relationship between 30 year municipal bond rates and 30 year LIBOR swaps put these hedge funds out of business, causing the extreme shifts in the municipal securities market. If TOB trusts had not existed, the hedge funds that employed this strategy could have obtained the identical leverage ratio through repurchase agreement financing and other secured borrowing arrangements.
- (B) The MMA testimony does not differentiate among types of TOB Program residual interest holders. We note that during the time that the single strategy hedge funds were unwinding their TOB Program positions, residual interests held by registered funds and banking entities remained largely intact, despite the additional pressure from the hedge fund liquidations.¹⁸ Residual interest holders that are banking entities and registered funds are limited in their ability to use TOB Programs as part of an overall non-diversified, leveraged strategy. As noted earlier, banking entities and registered funds are both subject to significant regulation with respect to the nature of the investments they can hold and the amount of leverage they can assume. Hedge funds, on the other hand, are not. The volatility in the municipal markets was not due to the fact that TOB Programs were not regulated, but rather that hedge funds were not regulated. Existing regulation already addresses the activities of the vast majority of TOB Program Participants,¹⁹ and there is no doubt that TOB Programs provide an overall benefit to the municipal markets.
- (d) TOB Programs provide a sound source of investment supply for investors.
- (i) TOB floating rate securities represent an estimated 15-25% of the assets in tax-exempt money market funds. If a risk retention requirement is imposed on TOB Program securitizers, then there will be a significant reduction in TOB Programs and/or other structural changes that could make it impossible for floating rate certificates to meet the eligibility requirements of Investment Company Act rule 2a-7, resulting in reduced investment opportunities for individual and institutional investors in money market funds.
- (ii) Both municipal money market funds and long-term municipal bond funds provide a more efficient and prudent way for retail investors to invest in

¹⁸ The majority of the TOB Program residual interests held in registered funds were issued before and even during the mass hedge fund liquidation of TOB residual interests. For example, a number of registered funds used TOB residual interests to refinance auction rate preferred securities during this time. See, e.g., BlackRock, Inc. Press Release (June 2, 2008); Nuveen Investments Press Release (June 11, 2008); Van Kampen Municipal Closed-End Funds Press Release (June 13, 2008). We note that these and other refinancing transactions were transparent by virtue of the public notices and registered fund filings that preceded and accompanied them and were intended as replacements for long-term structural funding rather than any transfer of risk.

¹⁹ In fact, each of the undersigned TOB Program Participants and/or their affiliates continued either to provide liquidity, own TOB residual interests, and/or own TOB floating rate certificates before, during and after the municipal market upheaval.

municipal securities than if they were to make those investments directly. The diversification and credit quality analysis provided by the managers of these funds are significant forms of investor protection. Subjecting TOB Programs to unworkable and unnecessary risk retention requirements could threaten the viability of these funds.

4. **CONCLUSION**

- 4.1 For the reasons set forth above, we believe that the Agencies should expressly exempt TOB Programs from the risk retention requirements of section 15G.
- 4.2 In the alternative, we believe that the Agencies should establish a separate risk retention requirement and method for TOB Programs that (i) gives due recognition to both the retention of market risk and any exposure to the same credit risk outside the TOB Program structure, and (ii) does not require unnecessary changes to the TOB Program structure.

The undersigned TOB Program Participants, the ICI and our counsel are more than happy to respond to any questions that you may have and/or to discuss TOB Programs more generally in the context of the changing legal landscape. We could be available to meet with any of the Agencies at your convenience, and/or you may contact us by email or telephone. For your convenience our contact information is attached on Appendix C.

Very truly yours,

ASHURST LLP

By: 

Margaret Sheehan

By: 

Joyce Gorman

SIGNATURES OF PARTICIPATING TOB PROGRAM PARTICIPANTS AND THE ICI FOLLOW

CITIBANK, N.A.

By:




Title:

VICE PRESIDENT

DEUTSCHE BANK AG, NEW YORK BRANCH

By:

A handwritten signature in black ink, appearing to be a stylized name, written over a horizontal line.

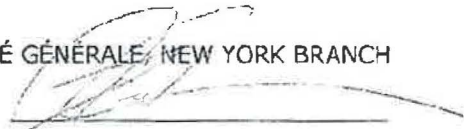
Title:

Director

SOCIÉTÉ GÉNÉRALE NEW YORK BRANCH


By:

Title:


DIRECTOR

WELLS FARGO BANK, N.A.

By:



Title:

ARTHUR EVANS, SVP

ashurst

INVESTMENT COMPANY INSTITUTE

By: Karrie McMillan

Title: General Counsel

DESCRIPTION OF TOB PROGRAM ASSETS AND TOB PROGRAM STRUCTURETOB Program Assets

Typically the assets in a TOB trust consist of a single issue of highly rated, fixed rate, long-term municipal securities of a single municipal issuer.²⁰ In the less common instance in which TOB Trust assets consist of the securities of more than one municipal issuer, the TOB Trust has specific, written deposit criteria governing the eligibility of assets for deposit. In either case, because the municipal securities deposited and/or eligible for deposit are both limited and specified in advance, holders of both classes of TOB Program securities know exactly what assets are (or in the future may be) deposited in the TOB Trust. In addition, if additional deposits are permitted in accordance with the established eligibility criteria, the investors holding TOB floating rate certificates are apprised in advance of any such deposit and may elect not to continue their investment after the deposit, in which case they are entitled to payment of their TOB floating rate certificates at par.

In order to ensure that the TOB floating rate certificates meet the portfolio security eligibility requirements of rule 2a-7, the municipal securities in a TOB trust either are rated AA- or better by an independent credit rating agency or are the subject of a credit enhancement arrangement that results in a rating of at least AA-. An official statement or other detailed disclosure document covers each offering of municipal securities, and the antifraud provisions of the securities laws apply to purchases and sales. In cases where there may not be a detailed underlying disclosure document, the underlying municipal securities are wrapped by credit enhancement and the TOB trust provides the TOB floating rate certificate holders and the TOB residual interest holder with disclosure about the credit enhancement.

Because a secondary market generally exists for municipal securities, they are liquid and are capable of being marked to market. The broker-dealers selling municipal securities are also subject to the antifraud provisions of the federal securities laws as well as the disclosure and sales practice rules of the Financial Industry Regulatory Authority. Municipal securities offer a steady income stream, making them a common component of investors' portfolios.

TOB Floating Rate Certificates

TOB floating rate certificates are variable rate, short-term, high quality, liquid securities whose price is equal to their face amount. TOB floating rate certificates bear interest at a variable interest rate, reset periodically based on prevailing short-term tax-exempt market rates, which generally are lower than the fixed rate payable on the underlying municipal securities. They are typically entitled to 5-10% of any capital gain ("Gain Share") realized upon any sale of the municipal securities from the TOB trust (a requirement driven by tax law). Under most circumstances, the TOB floating rate certificate holders have the right to tender their interests, for any reason or no reason, for a repurchase price equal to 100% of the face amount of the TOB floating rate certificates, plus accrued interest.²¹ The tender option allows those TOB floating rate certificate holders that are money market funds (offering a stable net asset value of \$1 per share pursuant to rule 2a-7) to treat the TOB floating rate certificates as having an extremely short maturity, i.e., the next interest rate reset date.

The purchase of TOB floating rate certificates is limited to "Accredited Investors," as defined in rule 501(a)(1)-(3) of Regulation D under the Securities Act of 1933 and "Qualified Purchasers," as

²⁰ The municipal issuer generally does not work with or coordinate with any TOB Program sponsor when issuing the municipal securities, although a TOB Program sponsor or an affiliate that is a broker-dealer may on occasion participate in the underwriting of the underlying municipal securities, subject to applicable securities laws and other customary legal and rating agency requirements.

²¹ TOB floating rate certificates also are subject to mandatory tender under certain circumstances.

defined in section 2(a)(51)(A) of the Investment Company Act of 1940, who possess such "knowledge and experience in financial and business matters as to be capable of evaluating the merits and risks of an investment in...and are able and prepared to bear the economic risk of investing in" the TOB floating rate certificates. Any investor who purchases TOB floating rate certificates must, prior to investing, provide written attestation of the foregoing. The primary buyers of TOB floating rate certificates are rule 2a-7-regulated, tax-exempt money market funds. For this reason, if there are any future changes to the credit quality requirements of rule 2a-7, TOB Program sponsors will amend TOB Program terms to conform to the new credit requirements so that TOB floating rate certificates are always eligible securities.

The tender option feature of TOB floating rate certificates is made possible through a liquidity facility that provides funds for payment of both principal and interest on the certificates whenever floating rate certificate holder exercises its tender option or a floating rate certificate is called for mandatory tender.²² The liquidity facility may be provided by the TOB Program sponsor, one of its affiliates or another bank or other entity. The liquidity provider's obligation to pay the TOB floating rate certificate holders terminates without notice upon the occurrence of any of the following very limited and remote events known as "TOTES" (an acronym for "Tender Option Termination Events"): a default on the underlying municipal securities and credit enhancement, where applicable; a credit rating downgrade below investment grade; the bankruptcy of the issuer and, when applicable, the credit enhancer; or the determination that the municipal securities are taxable. (Like Gain Share, inclusion of TOTES in TOB Program structures is required for tax reasons.)

In most instances, the liquidity provider is the same entity as, or an affiliate of, the holder of the TOB residual interest. When that is not the case, the liquidity provider typically requires that the holder of the TOB residual interest enter into a reimbursement agreement with the liquidity provider to reimburse the liquidity provider for all amounts paid to TOB floating rate certificate holders and not otherwise reimbursed from a remarketing of tendered floating rate certificates or, if the floating rate certificates are not remarketed, from the proceeds of sale of the municipal securities. Because the liquidity provider bears the market risk of any difference between the par amount of TOB floating rate certificates outstanding and the market value of the municipal securities (whose sale would generate proceeds to reimburse the liquidity provider for any liquidity draws) the liquidity provider typically has the right to direct the termination of the TOB trust prior to the occurrence of a TOTE. If the liquidity provider exercises this termination right, it must pay the floating rate certificate holders in full.

TOB Residual Interest

The TOB trust issues a residual interest that synthetically creates the economic equivalent of a leveraged position in the underlying municipal securities. The price of the residual interest is generally a nominal amount. The TOB residual interest holder receives all interest on the municipal securities not paid to the TOB floating rate certificate holders (net of the TOB trust's expenses) as well as 90-95% of any Gain Share recognized upon any sale of the municipal securities. The TOB residual interest holder has the right, exercisable at periodic intervals, to cause the sale of the municipal securities and the forced redemption of the TOB floating rate certificates for 100% of par value plus accrued interest and the applicable Gain Share. TOB residual interests typically have significant restrictions on transfer. In addition, there is no established secondary market for TOB residual interests.

In many cases, the TOB residual interest holder is the TOB Program sponsor or an affiliate of the TOB Program sponsor. In cases in which the TOB residual interest holder is not the TOB Program sponsor or an affiliate, it is a third party institutional or high net worth investor.

²² The TOB floating rate certificates have a short-term credit rating (based on the short-term rating of the liquidity provider) as well as a long-term credit rating (based on the credit quality of the assets on deposit in the TOB trust, including any credit enhancement). The combination of a high quality credit rating and a short-term rating makes TOB floating rate certificates eligible for purchase by money market funds.

Tax and Accounting Treatment of TOB Program Certificates

TOB Program sponsors design TOB Programs so that the tax-free nature of the income on the underlying municipal securities passes through to the TOB floating rate certificate holders and the TOB residual interest holder. In order to ensure pass-through tax treatment, TOB Programs provide for termination of the liquidity facility upon the occurrence of a TOTE, the pro rata sharing of credit risk as between the floating rate certificate holders and the residual interest holder, and the Gain Share payable to floating rate certificate holders. These features provide the necessary indicia of ownership to allow the income to remain tax-free to the holders of the TOB Program securities.

For accounting purposes, the TOB residual interest holder typically carries the underlying municipal securities as assets and the TOB floating rate certificates as debt, because the residual interest holder is acquiring the municipal securities and financing its acquisition with the proceeds of the floating rate certificates.

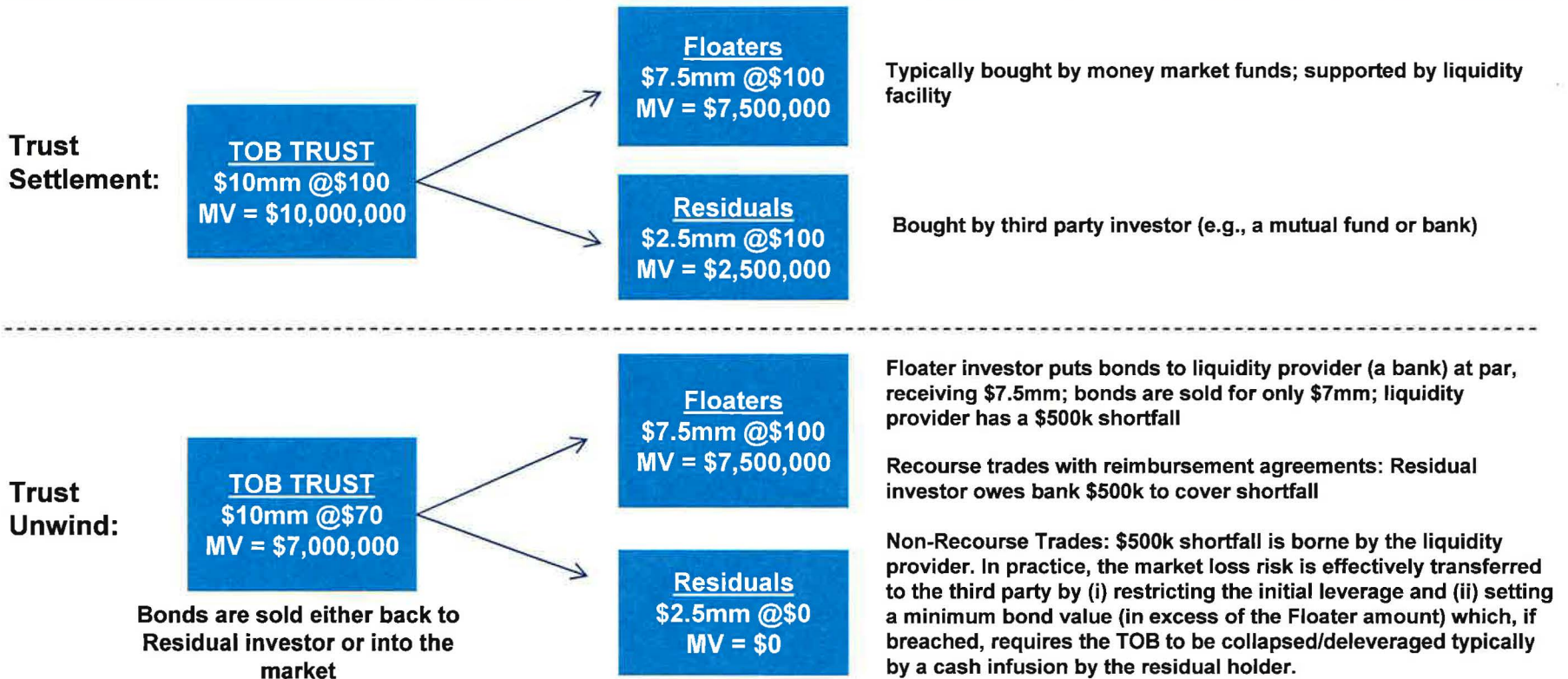
TOB Market Risk Overview

August 2012



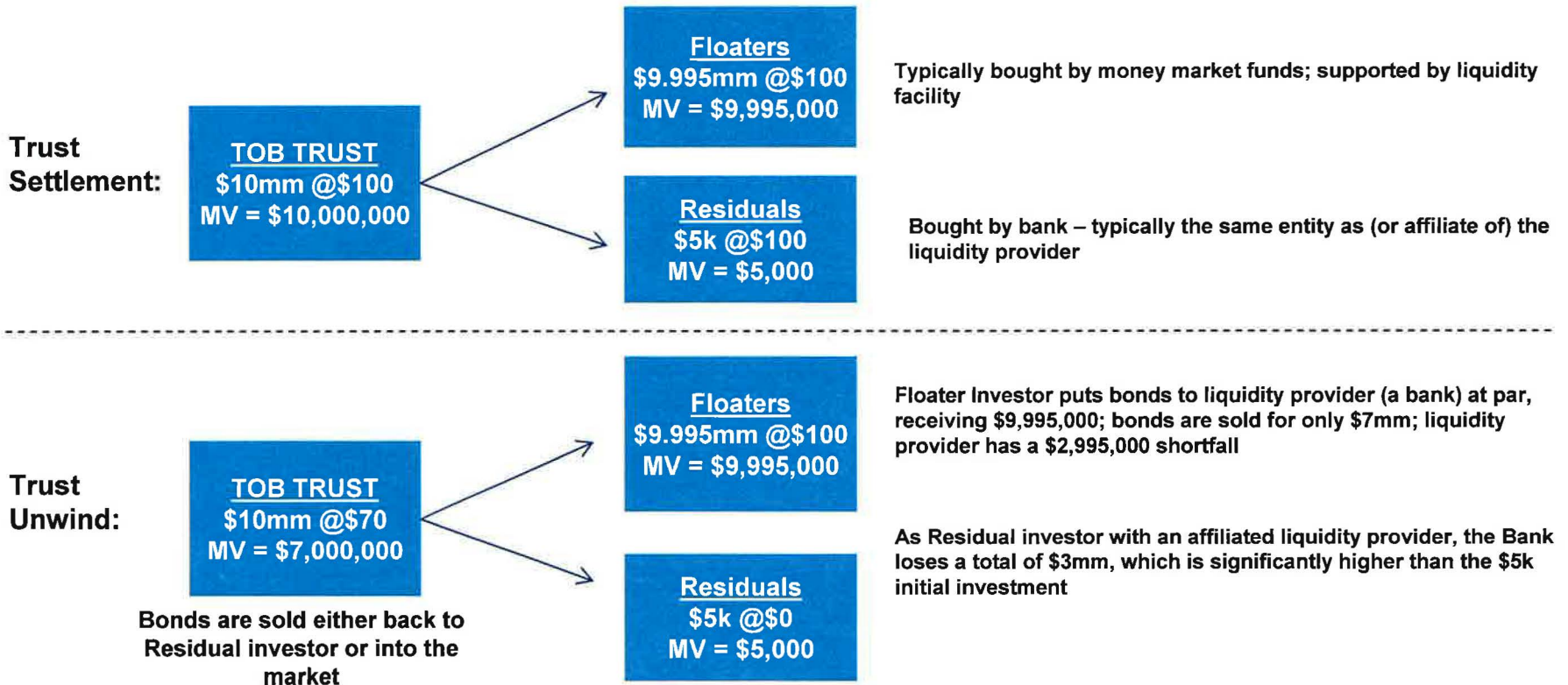
TOB Market Risk – Third Party TOB Trust

- **Trust Settlement:** \$10mm of bonds are deposited into trust at par (\$100 price) with 75% leverage
 - \$7.5mm of floating rate certificates (Floaters) and \$2.5mm of residual interests (Residuals) are issued
 - Floaters have a weekly put feature, backed by a liquidity facility provided by a bank
- **Trust Unwind:** At unwind, assume bonds are worth only \$7mm
 - In any unwind, other than a TOTE, the residual interest bears first loss



TOB Market Risk – Bank-Sponsored TOB Trust

- **Trust Settlement:** \$10mm of bonds are deposited into trust at par (\$100 price)
 - \$9.995mm of Floaters and \$5k of Residuals are issued
 - Floaters have a weekly put feature, backed by a liquidity facility provided by a bank
- **Trust Unwind:** At unwind, assume bonds unwind at \$70 (market value of \$7mm)
 - The bank (as Residual investor) takes full mark-to-market risk on the bonds



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