


 The logo for JSF the Journal of Structured Finance. 'JSF' is in large, bold, orange letters. To its right, 'the Journal of' is in a smaller, red, sans-serif font. Below that, 'STRUCTURED FINANCE' is written in large, bold, red, all-caps letters.

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Welcome to the Fall 2022 issue of *The Journal of Structured Finance*. This issue is guest edited by Ann Rutledge, the of CreditSpectrum Corp. She has curated a selection of four theory- and policy-themed articles that form the heart of this issue.

Issuance activity remains somewhat slower than in 2021. Agency MBS issuance has slowed considerably, while other areas are staying closer to last year's pace of activity.

Rising interest rates, falling stock prices, and the prospect of additional rate hikes by the Federal Reserve are putting a damper on things. To quote Bruce Springsteen, "The times are tough now, just getting tougher. This old world is rough, it's just getting rougher." (Springsteen 1984). Even if that sentiment does not (yet) describe the whole economy, it certainly captures the state of the fixed-income landscape. But this offers opportunity: the opportunity for the broad structured finance industry to prove its worth by delivering positive effects for Main Street.

Many private-label securitizations did not fare well in the aftermath of the 2007 mortgage meltdown. Private-label MBS performed terribly and CDOs performed even worse (Adelson 2021, 2022). The industry produced a flood of risky loans that created problems for both consumers and institutional investors. The industry received a black eye and suffered reputational damage. Ultimately, though, none of that matters if the industry can prove its true worth by producing substantial net benefits to Main Street.

The benefits of securitizing conforming residential mortgage loans through the agency MBS are widely recognized: America's mortgage market is national in scope. Regional differences in mortgage rates and regional funding shortages have been eliminated. Likewise, the nation's homeownership rate is around 66%, giving roughly two-thirds of Americans a concrete economic stake in their communities. Together with public education and the rule of law, that stake serves as one of the great pillars of American democracy.

Non-agency securitization can meet the challenge of the times by promoting credit availability to households and businesses on reasonable and responsible terms. Helping households and businesses weather the tough times while helping them to avoid becoming overextended should be the goal. In other words, asset quality must be a consideration along with production volume. History has delivered this lesson. Now the industry has a chance to demonstrate that the lesson has been absorbed.

Thinking about embracing the notion of a larger mission for non-agency securitization might echo past paradigm shifts that have produced key advances. For example, from the time of Archimedes until the development of infinite series techniques, the method of estimating pi ( $\pi$ ) was based on calculating the perimeter of regular polygons that fit within and around a circle. The more sides to the polygons, the more accurate the estimate. In 1596 Ludolph van Ceulen estimated  $\pi$  to 20 digits using a polygon with  $60 \times 2^{39}$  sides.



But the development of infinite series methods (alongside the invention of calculus) changed that. It was a critical change. For example, each term of the following series adds about 15 digits:<sup>1</sup>

$$\frac{1}{\pi} = \sum_{n=0}^{\infty} (-1)^n \times \frac{(6n)!}{(3n)!n!^3} \times \frac{163096908 + 6541681608n}{(262537412640768000)^{\left(n+\frac{1}{2}\right)}}$$

Embracing Main Street value creation as an industry goal requires collective action. It won't be easy. However, it would be a new and powerful tool—like infinite series and calculus—for moving the structured finance industry toward a stronger and more secure future.



Recent conflicting court decisions at the intermediate appellate level in New York could reach New York's highest court, the New York Court of Appeals. The issue is whether contractual language stating that a "trustee agrees to... exercise the rights referred to above for the benefit of all present and future certificateholders" creates a contractual duty in the trustee. More specifically, the issue is whether that language creates a duty for an MBS trustee to "exercise rights" under a deal's contracts to compel other parties to repurchase loans that breach representations and warranties. On August 30, 2022, the court in *IKB Intl. v Wells Fargo Bank* held that the language does create a duty.<sup>2</sup> Three weeks earlier, the court in *Western & Southern Life Ins. Co. v. US Bank* held that it does not.<sup>3</sup> The decisions came from two different panels of the New York Supreme Court, Appellate Division, First Department. Two earlier cases from other courts agree with the view that the language does not create a duty.<sup>4</sup> Other earlier cases take the view that that the language is merely "belts and suspenders," and that the duty to enforce repurchases arises from a duty to reject non-conforming

<sup>1</sup>Two more interesting series for calculating  $\pi$ :

$$\frac{1}{\pi} = \frac{2\sqrt{2}}{9801} \sum_{n=0}^{\infty} \frac{(4n)!(1103 + 26390n)}{(n!)^4 396^{4n}}$$

and

$$\frac{1}{\pi} = 12 \sum_{n=0}^{\infty} \frac{(-1)^n (6n)!(13591409 + 545140134n)}{(3n)!(n!)^3 640320^{3n+\frac{3}{2}}}$$

<sup>2</sup>*IKB Intl., S.A. v Wells Fargo Bank, N.A.*, \_\_\_ N.Y.S.3d \_\_\_, 208 A.D.3d 423, 2022 WL 3720417 (N.Y.A.D. 1 Dept.), 2022 N.Y. Slip Op. 05058 (N.Y. App. Div. 1st Dept., Aug. 30, 2022), <https://govt.westlaw.com/nyofficial/Document/I9ffa4d30287111ed9ef9cdc900f507ae>.

<sup>3</sup>*Western & S. Life Ins. Co. v US Bank N.A.*, 209 A.D.3d 6, 173 N.Y.S.3d 543, 2022 N.Y. Slip Op. 04886 (N.Y. App. Div. 1st Dept., Aug. 9, 2022), <https://govt.westlaw.com/nyofficial/Document/I86a3353017f611ed8f35bde9c93eba8c>.

<sup>4</sup>*Commerzbank v. US Bank*, 475 F. Supp. 3d 233 (S.D.N.Y. 2020); *Western & S. Life Ins. Co. v. Bank of N.Y. Mellon*, 2019-Ohio-388, 129 N.E.3d 1085 (Ohio Ct. App. 2019).



loan files, which is simply an element of the trustee's agreement to "hold the mortgage files for the benefit of certificateholders."<sup>5</sup> Others hold the opposite.<sup>6</sup>

These cases are important because they go directly to the issue of whether investors are getting what they bargain for when they invest in securitizations. The federal securities laws provide scant protections for securitization investors because of their short time limits for bringing claims. This amplifies the importance of contractual rights and remedies. Unless investors are told otherwise in disclosure materials, they will naturally expect a securitization to include the enforcement of repurchases of defective assets (i.e., assets that breach representations and warranties or that have incomplete or defective documentation). Otherwise they cannot have confidence that they will receive the deal that they've been sold.



Following the selection of articles curated by guest editor Ann Rutledge are two reports by me on recent industry events. The first covers the *11th Annual Investors' Conference on CLOs and Leveraged Loans*, which was held on May 23–24, 2022. The second covers the *1st Annual Middle Market CLOs and Direct Lending Conference*, which was held on June 15, 2022. Both events provided a wealth of interesting content for attendees.

The next section is selected highlights from *GlobalCapital* for the third quarter of 2022. The selection was compiled and curated by GC deputy securitization editor, Tom Lemmon. Five stories are featured, covering the following subjects:

- Recent activity in the European ABS market
- ESG consideration in the US ABS market
- Conflicting signals about the performance outlook for securitized assets
- Comparison of recent activity in US and European ABS markets
- The ability of the US securitization market to embrace ESG principles without the need for government oversight

Next comes a selection of industry news items from the Structured Finance Association, also from Q3 2022. The selection includes a dozen news snippets covering timely and important developments in the structured finance market.



<sup>5</sup>These cases address loans with defective documentation rather than loans that breach (other) representations and warranties. *Finkelstein v U.S. Bank, N.A.*, 75 Misc.3d 1202(A), 166 N.Y.S.3d 510 (Table), 2022 WL 1311461 (N.Y.Sup.), 2022 N.Y. Slip Op. 50338(U) (N.Y. Sup. Ct. May 22, 2022), <https://govt.westlaw.com/nyofficial/Document/lc03f0f80cb1611ec89cab276b2ee3ded>; *Zittman v. Bank of New York Mellon*, 2022 NYSlipOp 31527(U) (N.Y. Sup. Ct. May 10, 2022), [www.nycourts.gov/reporter/pdfs/2022/2022\\_31527.pdf](http://www.nycourts.gov/reporter/pdfs/2022/2022_31527.pdf); *Zittman v. Bank of New York Mellon*, 2022 NYSlipOp 31529(U) (N.Y. Sup. Ct. May 10, 2022), [www.nycourts.gov/reporter/pdfs/2022/2022\\_31529.pdf](http://www.nycourts.gov/reporter/pdfs/2022/2022_31529.pdf).

<sup>6</sup>*Park Royal I LLC v HSBC Bank USA, N.A.*, 2022 NYSlipOp 31715(U) (N.Y. Sup. Ct. May 25, 2022), [www.nycourts.gov/reporter/pdfs/2022/2022\\_31715.pdf](http://www.nycourts.gov/reporter/pdfs/2022/2022_31715.pdf).



As always, we welcome your submissions. Please encourage those you know who have good papers or who have made good presentations on structured finance- or project finance-related subjects to submit them to us.

Submission guidelines can be found at <https://jsf.pm-research.com/authors>. If you have comments or suggestions, you can e-mail them directly to me at [m.adelson@pm-research.com](mailto:m.adelson@pm-research.com).

**Mark Adelson**

Editor

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