PUBLIC STATEMENT

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Statement Regarding Joint Rule Reproposal Concerning Credit Risk Retention

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Securities and Exchange Commission

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The Securities and Exchange Commission ("SEC" or "Commission") today approved a joint rule reproposal to implement Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank").[1] I am not able to support the release in the form approved because the reproposal does not contain necessary economic analyses and does not adequately consider alternatives to credit risk retention requirements or the interplay between those requirements and other regulatory reforms.

Before discussing these shortcomings, I want to recognize all the hard work the SEC's staff in the Division of Corporation Finance and the Division of Economic and Risk Analysis ("DERA") put into developing the joint rule reproposal. I also want to thank them for briefing me on the rulemaking and answering my questions.

While I am not able to vote in favor of the reproposal, I am encouraged that some improvements were made to the original proposal in response to public comments. For example, the reproposal removes the problematic premium capture cash reserve account approach. And, with respect to some classes of asset-backed securities ("ABS"), the reproposal revises various risk retention obligations and allows alternative incentive alignment practices.

As a general principle, I believe that regulatory agencies should make greater use of reproposals. Reproposals offer regulators the opportunity to improve the efficiency and effectiveness of their rulemaking processes and provide the public the regulatory transparency and accountability they deserve. Such a measure of discipline is critically important in connection with Dodd-Frank, which requires regulators to promulgate hundreds of new, complex, and interrelated rules that affect every American by impacting capital formation, job creation, and economic growth. I am pleased that the agencies approving today's release saw fit to repropose the rule to take into account public comment. However, because of my concerns about two serious deficiencies in this particular reproposal, I cannot support it and I respectfully dissent.

The Agencies Issuing The Reproposal Did Not Perform Necessary Economic Analyses

The reproposal correctly describes the SEC's statutory obligations to conduct regulatory economic analysis. Section 23(a)(2) of the Securities Exchange Act of 1934 ("Exchange Act") requires the SEC, when promulgating rules under the Exchange Act such as this reproposal, to consider the impact on competition that a rule would have, and prohibits the SEC from adopting any rule that would impose a burden on competition not necessary in furtherance of the Act.[2] In addition, Section 3(f) of the Exchange Act requires the SEC, when engaging in rulemaking where it is required to consider or determine whether an action is necessary or appropriate in the public interest, also to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.[3]

This rulemaking is being conducted under the authority provided by Section 15G of the Exchange Act. Section 15G(b) of the Exchange Act, as added by Section 941(b) of Dodd-Frank, generally requires the SEC and the Office of the Comptroller of the Currency, the Federal Reserve Board of Governors ("Board"), the Federal Deposit Insurance Corporation, and, in the case of any securitization of any residential mortgage asset, together with the Secretary of Housing and Urban Development and the Federal Housing Finance Agency (collectively, referred to as the "federal banking and housing agencies," and together with the SEC as the "Rulemaking Agencies"), to

jointly prescribe regulations under that Section. I interpret this to mean that any regulator acting to implement Section 941 of Dodd-Frank on a joint basis must act in accordance with the rulemaking process mandated for the SEC under the Exchange Act.

The reproposal includes a section entitled "Commission Economic Analysis" that contains a robust analysis by SEC economists of the costs and benefits of the reproposed rule. I believe this analysis largely fulfills the SEC's regulatory economic analysis obligation under the Exchange Act.[4] However, because Congress required the federal banking and housing agencies to jointly promulgate regulations with the SEC under Section 15G of the Exchange Act, I believe those agencies also have an obligation to conduct an economic analysis, equal to the SEC's obligations, under the Exchange Act. The reproposal does not contain an economic analysis from any of the federal banking and housing agencies.[5] This omission is particularly glaring given the large number of discretionary choices made by the agencies in the reproposal.

In addition, Dodd-Frank includes its own requirement to consider the macroeconomic effects of credit risk retention requirements. Pursuant to Section 946, the Chairman of the Financial Stability Oversight Council ("FSOC") conducted a study of the macroeconomic effects of the risk retention under Subtitle D of Title IX (Sections 941 through 946) of Dodd-Frank and issued a report of its findings to Congress ("FSOC Report").[6] The FSOC Report concludes that the macroeconomic implications of credit risk retention requirements are complex and cautions that "[I]f overly restrictive, risk retention could constrain the formation of credit, which could adversely impact economic growth. The challenge is to design a risk retention framework that maximizes benefits while minimizing its costs."[7] Notably, the reproposal does not contain any analysis of the macroeconomic implications identified in the FSOC Report.

The failure by the Rulemaking Agencies to articulate necessary economic analyses to support the reproposal is a significant omission and fundamental flaw that cannot be overlooked.

The Reproposal Does Not Adequately Consider Alternatives to Credit Risk Retention Requirements

Congress gave the Rulemaking Agencies broad exemptive authority in Section 941 of Dodd-Frank, which permits full or partial exemptions from credit risk retention requirements.[8] The reproposal, however, fails to utilize sufficiently this exemptive authority to accommodate alternatives to risk retention that could achieve the goals of Section 941 at a lower cost. The reproposal also does not take adequate account of the analysis and recommendations in the FSOC Report and in a separate study prepared by the Board under Dodd-Frank.

Pursuant to Section 941(c) of Dodd-Frank the Board conducted a study that includes an analysis of the impact of credit risk retention requirements on each individual class of asset-backed security ("Board Report").[9] The Board Report specifically recommends that the Rulemaking Agencies consider the credit risk retention requirements in the context of all other Dodd-Frank rulemakings.[10] The Board Report further notes that "rulemakings under distinct sections of the [Dodd-Frank] Act might more efficiently address the same objectives as credit risk retention requirements."[11] Similarly, the FSOC Report specifically recommends that the Rulemaking Agencies consider that, "While risk retention offers many potential benefits, it is one of many reforms. It cannot address all problems in the securitization chain, and will work in conjunction with other reforms. Moreover, risk retention may be more suitable in some circumstances than others, depending on the specific nature of the underlying financial assets."[12] The FSOC Report concludes, "Therefore, risk retention must be considered in conjunction with other reforms in the Dodd-Frank Act as well as other reforms occurring both domestically and internationally."[13] Despite the statements in the Board and FSOC Reports, the Rulemaking Agencies do not adequately consider potentially more effective and/or less burdensome alternatives to credit risk retention requirements in the reproposal.

In my view, the reproposal should have included disclosure requirements that, contingent on the availability of information regarding secondary market transactions,[14] could facilitate better, more informed decisions by both regulators and investors. Mandatory disclosure also would have the potential to directly reduce informational asymmetries and moral hazard problems. The Rulemaking Agencies could have, for example, proposed and sought comment on enhanced disclosures of loan level characteristics along with mandatory disclosures of the amount, type, and

duration of the credit risk that the originators and securitizers voluntarily retained in each ABS.

The reproposal also should have given further consideration to subordinated performance fees that have components dependent on the performance of the overall pool or on junior tranches. Such fees could potentially mitigate concerns about misaligned incentives between originators, securitizers, and investors. The reproposal points out that some commenters noted that securitizers of collateralized loan obligations often retain a small portion of the residual interest and that commenters asserted that securitizers retain risk through subordinated management and performance fees. The release requests comment on questions related to subordinated performance fees. Importantly, however, the reproposal does not allow for such fees to satisfy credit risk retention requirements in any asset class. To fully address the comments, the Rulemaking Agencies could have proposed disclosures about the structure of such fees.

The reproposal also does not address the effects of recent SEC rules implementing two provisions of Dodd-Frank that are intended to improve various aspects of the securitization markets. On January 20, 2011, the Commission adopted rules regarding the use of representations and warranties in the ABS market to implement Section 943 of Dodd-Frank.[15] These rules require issuers of ABS to disclose the history of the requests they received and repurchases made by them related to their outstanding ABS. On the same day, the Commission also adopted rules to implement Section 945 of Dodd-Frank by requiring the issuers of ABS to conduct a review of the assets underlying those securities and make certain disclosures about those reviews.[16] Requirements to comply with these ABS rules came into effect on February 14, 2012, which means that more than one year of data and information about the implementation and effects of these rules is available. Yet, it does not appear that the Rulemaking Agencies made meaningful use of this information in connection with the reproposal.

I appreciate the efforts made by the Commission's staff in reproposing the risk retention rule, but I am unable to support this joint rulemaking. I am extremely disappointed that the reproposal does not include necessary economic analyses and fails to adequately consider alternatives to the credit risk retention requirements or the interplay between those requirements and other regulatory reforms.

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[1] This release reproposes certain aspects of the initial joint rule proposal published in the Federal Register on April 29, 2011. 15 U.S.C. 78o-11. That proposal was approved before I joined the Commission.

[2] 15 U.S.C. 78w(a).

[3] 15 U.S.C. 78c(f).

[4] In addition to the analysis described in the Commission Economic Analysis section of the release, the SEC's DERA economists conducted a rigorous empirical study that examines the impact of loan characteristics on serious delinquency rates for qualified residential mortgages and qualified mortgages. The study is expected to be submitted to the SEC's public comment file, which is available at http://www.sec.gov/comments/s7-14-11/s71411.shtml.

[5] I believe an independent economic analysis by each agency would not necessarily have been required in connection with the joint rulemaking. Instead, the other agencies could have satisfied their obligation to conduct an economic analysis by adopting explicitly the Commission's economic analysis, to the extent they concurred in the SEC's analysis.

[6] Timothy F. Geithner, Chairman of the Financial Stability Oversight Council, Macroeconomic Effects of Risk Retention Requirements, January 2011, *available at* http://www.treasury.gov/initiatives/wsr/Documents/Section 946 Risk Retention Study (FINAL).pdf.

[7] *Id.* at 4.

[8] *See* Exchange Act Sections 15G(c)(1)(G) and 15G(e).

[9] Board of Governors of the Federal Reserve System, Report to the Congress on Risk Retention, October 2010, *available at*

http://federalreserve.gov/boarddocs/rptcongress/securitization/riskretention.pdf.

[10] *Id.* at 4.

[11] *Id.* at 84.

[12] FSOC Report at 18.

[13] *Id.* at 30.

[14] Information on the Financial Industry Regulatory Authority's Trade Reporting and Compliance Engine, which facilitates the mandatory reporting of over-the-counter secondary market transactions in corporate debt, agency debt, and mortgage and asset backed securities, is available at http://www.finra.org/Industry/Compliance/MarketTransparency/TRACE/.

[15] Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (SEC Rel. No. 33-9175, 34-63741).

[16] Issuer Review of Assets in Offerings of Asset-Backed Securities (SEC Rel. No. 33-9176, 34-63742).

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