Congress of the United States
Washington, DC 20515
July 31, 2014

CLO: #Y - 76
CCS: 14-5969
RECVD: 8/18/14

The Honorable Janet L. Yellen
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave, NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Director
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 200429

The Honorable Mary Jo White
Chair
The Securities and Exchange Commission
100 F Street, NE, Room 10700
Washington, DC 20549

The Honorable Thomas J. Curry
Comptroller of the Currency
Administrator of National Banks
250 E Street, SE
Washington, DC 20219

Dear Sirs and Madams:

We are writing in regards to your joint rulemaking designed to implement the risk retention requirements of Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. While the joint order setting forth further proposed rules issued on August 28, 2013, is an earnest effort to improve upon the initial proposal of rules issued in March 2011, the provisions regarding open market collateralized loan obligations (CLOs), and in particular the potential adverse effect on credit availability, continue to concern us.

CLOs are a vital source of corporate finance in the United States. They provide more than $300 billion of loans to American companies — almost one-quarter of all outstanding funded corporate loans. Understanding the significant role CLOs play, we want to ensure that the risk retention requirements are properly tailored to the unique structure of open market CLOs. Open market CLOs do not engage in "originate to distribute" securitizations, so simply applying the standard risk retention rules designed for such securitizations to open market CLOs does not necessarily make sense. As you acknowledge in your re-proposal, "the standard form of risk retention in the original proposal could, if applied to open market CLO managers, result in fewer open market CLO issuances and less competition in the sector." Specifically, we are concerned that the approach outlined in the August re-proposal that requires CLO managers to retain 5% of the CLO's fair value could impede the issuance of new CLOs. With very limited balance sheets, very few CLO managers could retain a 5% share of a CLO.

One approach to risk retention that we believe merits consideration is a proposal to create "qualified" open market CLOs ("QCLOs") that would have to meet a series of strict criteria designed to protect investors, ensure that a CLO's portfolio is conservatively invested, and align the interests of the CLO manager and the investors in the CLO. We believe this approach could provide a workable solution for most managers of open market CLOs and ensure the continued flow of credit to companies across the country. We hope you will seriously evaluate this proposal as you work towards the final rules implementing Section 941.

The QCLO approach requires managers of open market CLOs to retain 5% of the equity of a QCLO rather than 5% of fair value. This level of retention would still be a significant commitment for thinly capitalized CLO managers, and would still likely force some managers out of the market. However, this approach would permit most CLO managers to continue to participate in this important market, avoiding a dramatic reduction in CLO financing and resulting harms to the public interest that could otherwise result from the agencies' proposed rules.

Importantly, this modified risk retention requirement would apply only to CLOs that meet certain criteria across six categories. First, the portfolio would have to consist almost entirely of U.S. dollar denominated senior secured commercial loans and could contain no re-securitizations or derivatives other than basic interest rate or FX hedges. The portfolio would also have to be diversified such that no more than 3.5% of a CLO's assets could relate to any single borrower, and no more than 15% of its assets could relate to any single industry — thereby reducing the chance that a few individual defaults could cause significant losses for a CLO investor. The borrowing companies would have to be overwhelmingly based in the United States. The CLO's equity would have to equal at least 8% of the value of its assets, which would provide a substantial cushion for CLO debt investors.

Significantly, the QCLO proposal would advance the core policy goals of the risk retention requirement by ensuring an alignment of interests between the CLO manager and the investors. Specifically, the CLO manager's interests would have to be aligned with those of the CLO's investors through the subordination of the majority of the manager's fees — in addition to the manager satisfying the risk retention requirement — and the CLO documents would have to provide that the manager could be removed by the CLO investors. The QCLO designation would be available only if the CLO manager is an SEC-registered investment adviser and, as such, has a fiduciary duty to the CLO investors. Finally, investors in a qualifying CLO would be provided with extensive information, including a monthly report that would, among other things, specifically identify all CLO assets and benchmark the CLO's compliance with its various performance covenants.

We urge you to consider the QCLO proposal as an alternative approach to credit risk retention. We believe this proposal could achieve the important goals of Section 941 while enabling the continuation of the vibrant CLO market that is so important to economic growth.

Sincerely,

JIM HIMES
Member of Congress

ANDY BARR
Member of Congress

GWEN MOORE
Member of Congress

SCOTT GARRETT
Member of Congress

GARY PETERS
Member of Congress

PATRICK MCHENRY
Member of Congress

JOHN CARNEY
Member of Congress

PETER KING
Member of Congress

TERRI SEWELL
Member of Congress

BILL POSEY
Member of Congress

BILL FOSTER
Member of Congress

BLAINE LUETKEMEYER
Member of Congress

JOHN DELANEY
Member of Congress

STEVE STIVERS
Member of Congress

PATRICK MURPHY
Member of Congress

STEPHEN FINCHER
Member of Congress

GREGORY W. MEEKS
Member of Congress