Congress of the United States
Washington, DC 20515

December 10, 2013

Chairman Ben Bernanke
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, D.C. 20551

Chairman Martin J. Gruenberg
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429-9990

Chairwoman Mary Jo White
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Comptroller of the Currency Thomas J. Curry
Office of the Comptroller of the Currency
Constitution Center
400 7th St SW, Suite 3E-218
Washington D.C. 20219

Dear Chairman Bernanke, Chairwoman White, Chairman Gruenberg, and Comptroller Curry:

We are writing to you regarding your recently issued proposed rule on the risk retention requirements of Section 941 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-206) ("Dodd-Frank"). We believe the proposed rule fails to appropriately take into account the unique aspects of the open-market collateralized loan obligations (CLOs), which are vital sources of capital for the mid-sized businesses.

The authors of the Dodd-Frank Act designed Section 941 to address the breakdown of the "originate to distribute" market for mortgages. While we can debate the efficacy of such a provision, the implementation of Section 941 has taken a "one-size-fits-all" approach to regulating securitization markets for diverse asset classes that did not cause nor contribute to the financial crisis. This overly broad approach will have an unnecessarily deleterious impact on several markets, including open-market Collateralized Loan Obligations (CLOs).

CLOs are an extremely important source of financing for non-investment grade U.S. companies, including many emerging growth companies, which cannot cost-effectively access the corporate bond market. Instead, these companies rely on loans for the funds to expand their operations or invest in new technologies. CLOs are the leading lenders in this space, providing approximately $300 billion in business financing. Given their sizable role in extending credit to growing U.S. businesses, we believe CLOs have several unique characteristics which should be taken into consideration prior to issuing a final rule to implement Section 941 of the Dodd-Frank Act.

For instance, CLOs do not use the "originate to distribute" securitization model used in other asset-backed securities markets. Rather, CLOs, are typically organized by investment managers and operate more like mutual funds. The CLO manager uses the proceeds received from note-holders to acquire corporate loans, at their discretion, on the open market, and then actively manages this loan portfolio on behalf of investors. Since most of the manager's remuneration is contingent on the CLO's positive performance, the CLO manager's interests are already aligned with the CLO investors.

We believe the re-proposed rule fails to consider these unique characteristics of the CLO market, and in doing so, the re-proposal will unnecessarily drive up transaction costs. As a result, many smaller managers would be forced out of the market, limiting the options available for U.S. companies seeking access to credit; a point acknowledged in the August 2013 release which notes, "that the standard form of risk retention in the original proposal could, if applied to open market CLO managers, result in fewer CLO issuances and less competition in the sector."

The re-proposal attempts to address this clear problem by providing an alternative form of risk retention whereby the bank that lead-arranges the loan syndication is responsible for holding a five percent retained interest instead. While we appreciate your attempt to solve the problem that you concede exists, this alternative appears unworkable. For instance, this retained interest may not be hedged or sold until repayment, default, or bankruptcy, and would limit the bank's ability to actively manage its risk portfolio. Requiring banks to hold these loans without the ability to hedge or sell would result in unsafe and unsound banking practices that are strikingly at odds with overarching principles of prudential bank supervision.

An analysis prepared by Dechert LLP concluded, "few, if any, lead arrangers will accept the invitation being extended by the Agencies," and "given that only the largest, best capitalized managers would be able to fund the required 'risk retention,' we expect a new wave of consolidation and other partnership arrangements to occur among managers, thus leading to fewer managers, less competition and less selection for investors."[1]

The application of risk retention to CLOs would eliminate the incentive to manage CLOs, or under the proposed alternative structure, for banks to syndicate loans for CLOs. A recent survey of CLO managers indicated that if this provision goes into effect, the CLO market could contract by 75 percent, or over $200 billion.[2] It is not apparent what benefit this rule would produce in exchange. Nor is it clear what alternative sources of credit would fill this void. Financial reform should not raise the costs for market participants that did not cause or contribute to the financial crisis.

Our concerns about the viability of imposing risk retention on managers are not theoretical – after the European Union adopted CLO risk retention requirements similar to those in the proposed rule, CLO formation in Europe has been moribund. There were no CLOs formed at all in 2012, and only a handful this year.

We believe, as written, the application of a five percent risk retention to CLOs would eliminate the incentive to arrange or manage a CLO, unnecessarily consolidate the industry, and raise borrowing costs for American businesses. If the responses to the above-cited survey are correct, the corporate credit markets could contract by more than $200 billion. It is not apparent what alternative sources of credit would fill this void. It is unclear what benefit, if any, this rule would provide to the American financial system. Given the potential impact of this rule and the impediments it may create for prudential supervisors, we believe it would be appropriate for you to exercise your exemptive authority under Section 941(e) of the Dodd-Frank Act with respect to this discrete asset class. At the very least, you should endeavor to fashion a risk retention rule that will not impose such costs on the commercial credit markets and our economy as a whole.

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[1] Dechert LLP, *Risk Retention Reproposal's Impact on CLOs: Loan Arrangers Get Invited to the Party that No One Wants to Attend*, August, 2013, http://sites.edechert.com/10/1704/august-2013/2013-08-30-risk-retention-reproposal-s-impact-on-clos--loan-arrangers-get-invited-to-the-party-that-no-one-wants-to-attend.asp.

[2] The Loan Syndications and Trading Association, *Manager Survey*, July 2013, http://www.lsta.org/WorkArea/DownloadAsset.aspx?id=16883.

Sincerely,

Andy Barr
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Scott Garrett
Member of Congress

Steve Stivers
Member of Congress

Stephen Fincher
Member of Congress

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