



Americans for Financial Reform
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202.466.1885

March 12, 2014

Dear Representative,

On behalf of Americans for Financial Reform, we are writing to express our opposition to H.R. 4167, the “Restoring Proven Financing for American Employers Act”.¹ By exempting almost all collateralized loan obligations (CLOs) issued before January, 2014 from Volcker Rule restrictions on bank sponsorship of external funds, this legislation would seriously undermine the risk protections created by the Volcker Rule. Since many of these CLO vehicles are permitted to buy and sell securities in a manner similar to a hedge fund, passage of HR 4167 could make basic Volcker Rule restrictions on proprietary trading difficult to enforce for years to come. With a historically strong market for risky corporate debt and observers warning against possible overheating in the booming CLO market, there is no justification for undermining the Volcker Rule in order to permit a few of the nation’s largest Wall Street banks to continue to hold these instruments.²

The Volcker Rule makes the banking system safer by banning proprietary gambling with customer funds, and sharply restricting bank sponsorship of external funds such as hedge funds that could permit banks to engage in such gambles through external vehicles. These restrictions on bank sponsorship of external funds, including securitizations, were and are directly responsive to the problems revealed in the global financial crisis. Bear Stearns, the first major investment bank to collapse during the financial crisis, failed due to events triggered by the firm’s sponsorship of two credit hedge funds. As the crisis developed, numerous major banks were exposed to major losses due to the implicit guarantees they had offered to external securitization vehicles. These are exactly the same type of securitization vehicles that are used to create the CLOs that this legislation exempts from the ban on sponsorship of external funds.

When writing the regulations for the Volcker Rule, regulators created a generous exemption for ‘plain vanilla’ loan securitizations. This exemption permits banks unlimited sponsorship of external securitization vehicles so long as those vehicles hold only loans and a few closely related types of assets. The exemption is intended to permit banks to continue to support lending through straightforward loan securitizations, while also maintaining the Volcker limitations on bank involvement in the complex re-securitizations, synthetic securitizations, and hedge-fund type vehicles that were most problematic during the financial crisis. In addition, since the

¹ Americans for Financial Reform is a coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups.

² Miller, Steve, “[2013 CLO Issuance Hits \\$81.9 Billion, Most Since 2007](#)”, Forbes Magazine, January 2nd, 2014; Alloway, Tracy and Viviane Rodrigues, “[Boom-Era Credit Deals Raise Fears of Overheating](#)”, Financial Times, October 22, 2013; Natarajan, Srivar and Krista Giovacco, “[Junk Loans Top ’08 Record as Safeguards Stripped](#)”, Bloomberg, December 23, 2013; Cohn, Caroline, “[High Yield Bonds Draw Investors](#)”, Reuters, March 10, 2014.

Volcker Rule specifically exempts loans themselves, banks can continue to originate and sell individual loans and syndicate such loans without any Volcker Rule restrictions.

But this legislation would go far beyond the already generous exemption established by regulators and exempt all CLOs issued prior to January 2014 that were composed ‘primarily’ of loans. This would apparently permit exempted CLOs to hold up to 49 percent non-loan assets, including repackaged securities and complex credit derivatives. It is also important to understand that the managers of these CLO vehicles are generally permitted to buy and sell assets in order to maximize their returns. Thus, exempting CLOs issued prior to January 2014 could permit any bank that held or purchased such an exempted securitization to conduct proprietary trading in securities and derivatives through the securitization vehicle. Passing this bill would create numerous exempted securitization vehicles that could each act as a kind of mini-hedge fund through which banks could continue proprietary trading. This would seriously hamper the capacity to enforce the Volcker Rule for years to come.

This is not a community bank issue. Most bank-owned CLOs are held by a few large Wall Street banks. In fact, almost two thirds of all bank-owned CLOs are held by just two mega-banks – Citigroup and JP Morgan.³ It is unclear why the large Wall Street banks who hold CLOs cannot simply sell them. There is strong current demand for CLOs and it is likely that banks who sold CLOs at this time would book significant profits. There is no good reason to undermine the Volcker rule in order to permit major Wall Street banks to stockpile CLOs that they could easily sell on the open market.

Supporters of HR 4167 argue that it is justified by the need to sustain corporate lending, but it is completely unnecessary for that purpose. First, as discussed above corporate credit markets are booming and regulators are in fact warning that loan issuance in this market may be excessive.⁴ Second, regulators have already exempted securitizations from the Volcker Rule which are restricted to loans alone, including CLOs restricted to corporate loans. Finally, CLOs do not generally hold conventional corporate loans, but instead hold high-yield ‘subprime’ corporate loans designed to fund leveraged buy outs, not fund ordinary investment or hiring.

Finally, HR 4167 would also put in statute a highly technical restriction on the permissible regulatory definition of ‘owning’ a CLO. Specifically, an investment which carried voting rights allowing the investor replace a CLO manager for cause would not count as an equity investment. We would urge Congress to avoid trying to micromanage the definition of ‘ownership’ or equity in this way. The technical change here does not correspond to the ordinary legal definition of the line between debt and equity – for example, purchase of a corporate bond does not carry the right to vote on replacing a company CEO who is found guilty of a minor criminal charge, while purchase of an equity stake generally does carry that right. This change would artificially restrict the circumstances in which regulators can judge that a bank owns a CLO.

³ Better Markets, [“Fact Sheet: The CLO Debate Is Just the Latest Wall Street Attack On The Volcker Rule”](#), February 26, 2014.

⁴ Gage, Caroline Salinas, Craig Torres and Kristen Haunss, [“Attack on Junk-Loans Risks LBO Profits as U.S. Cracks Down”](#), Bloomberg News, November 13, 2013.

We urge you to reject this legislation, which would create dangerous loopholes in Volcker Rule risk protections for no clear public purpose, Thank you for your consideration. For more information please contact AFR's Policy Director, Marcus Stanley at marcus@ourfinancialsecurity.org or 202-466-3672.

Sincerely,

Americans for Financial Reform

Following are the partners of Americans for Financial Reform.

All the organizations support the overall principles of AFR and are working for an accountable, fair and secure financial system. Not all of these organizations work on all of the issues covered by the coalition or have signed on to every statement.

- AARP
- A New Way Forward
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Income Life Insurance
- American Sustainable Business Council
- Americans for Democratic Action, Inc
- Americans United for Change
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- Center for Media and Democracy
- Center for Responsible Lending
- Center for Justice and Democracy
- Center of Concern
- Center for Effective Government
- Change to Win
- Clean Yield Asset Management
- Coastal Enterprises Inc.
- Color of Change
- Common Cause
- Communications Workers of America
- Community Development Transportation Lending Services
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO Mobile
- CTW Investment Group
- Demos
- Economic Policy Institute
- Essential Action
- Green America
- Greenlining Institute
- Good Business International

- HNMA Funding Company
- Home Actions
- Housing Counseling Services
- Home Defender's League
- Information Press
- Institute for Agriculture and Trade Policy
- Institute for Global Communications
- Institute for Policy Studies: Global Economy Project
- International Brotherhood of Teamsters
- Institute of Women's Policy Research
- Krull & Company
- Laborers' International Union of North America
- Lawyers' Committee for Civil Rights Under Law
- Main Street Alliance
- Move On
- NAACP
- NASCAT
- National Association of Consumer Advocates
- National Association of Neighborhoods
- National Community Reinvestment Coalition
- National Consumer Law Center (on behalf of its low-income clients)
- National Consumers League
- National Council of La Raza
- National Council of Women's Organizations
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Resource Center
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Nurses United
- National People's Action
- National Urban League
- Next Step
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO National Network
- Progress Now Action
- Progressive States Network
- Poverty and Race Research Action Council
- Public Citizen
- Sargent Shriver Center on Poverty Law
- SEIU
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Fuel Savers Club

- The Leadership Conference on Civil and Human Rights
- The Seminal
- TICAS
- U.S. Public Interest Research Group
- UNITE HERE
- United Food and Commercial Workers
- United States Student Association
- USAction
- Veris Wealth Partners
- Western States Center
- We the People Now
- Woodstock Institute
- World Privacy Forum
- UNET
- Union Plus
- Unitarian Universalist for a Just Economic Community

List of State and Local Partners

- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans For Responsible Lending
- Association for Neighborhood and Housing Development NY
- Audubon Partnership for Economic Development LDC, New York NY
- BAC Funding Consortium Inc., Miami FL
- Beech Capital Venture Corporation, Philadelphia PA
- California PIRG
- California Reinvestment Coalition
- Century Housing Corporation, Culver City CA
- CHANGER NY
- Chautauqua Home Rehabilitation and Improvement Corporation (NY)
- Chicago Community Loan Fund, Chicago IL
- Chicago Community Ventures, Chicago IL
- Chicago Consumer Coalition
- Citizen Potawatomi CDC, Shawnee OK
- Colorado PIRG
- Coalition on Homeless Housing in Ohio
- Community Capital Fund, Bridgeport CT
- Community Capital of Maryland, Baltimore MD
- Community Development Financial Institution of the Tohono O'odham Nation, Sells AZ
- Community Redevelopment Loan and Investment Fund, Atlanta GA
- Community Reinvestment Association of North Carolina
- Community Resource Group, Fayetteville A
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (NYC)
- Cooperative Fund of New England, Wilmington NC

- Corporacion de Desarrollo Economico de Ceiba, Ceiba PR
- Delta Foundation, Inc., Greenville MS
- Economic Opportunity Fund (EOF), Philadelphia PA
- Empire Justice Center NY
- Empowering and Strengthening Ohio's People (ESOP), Cleveland OH
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing
- Fitness and Praise Youth Development, Inc., Baton Rouge LA
- Florida Consumer Action Network
- Florida PIRG
- Funding Partners for Housing Solutions, Ft. Collins CO
- Georgia PIRG
- Grow Iowa Foundation, Greenfield IA
- Homewise, Inc., Santa Fe NM
- Idaho Nevada CDFI, Pocatello ID
- Idaho Chapter, National Association of Social Workers
- Illinois PIRG
- Impact Capital, Seattle WA
- Indiana PIRG
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc., Mayville NY
- La Casa Federal Credit Union, Newark NJ
- Low Income Investment Fund, San Francisco CA
- Long Island Housing Services NY
- MaineStream Finance, Bangor ME
- Maryland PIRG
- Massachusetts Consumers' Coalition
- MASSPIRG
- Massachusetts Fair Housing Center
- Michigan PIRG
- Midland Community Development Corporation, Midland TX
- Midwest Minnesota Community Development Corporation, Detroit Lakes MN
- Mile High Community Loan Fund, Denver CO
- Missouri PIRG
- Mortgage Recovery Service Center of L.A.
- Montana Community Development Corporation, Missoula MT
- Montana PIRG
- New Economy Project
- New Hampshire PIRG
- New Jersey Community Capital, Trenton NJ
- New Jersey Citizen Action
- New Jersey PIRG
- New Mexico PIRG
- New York PIRG
- New York City Aids Housing Network
- New Yorkers for Responsible Lending

- NOAH Community Development Fund, Inc., Boston MA
- Nonprofit Finance Fund, New York NY
- Nonprofits Assistance Fund, Minneapolis M
- North Carolina PIRG
- Northside Community Development Fund, Pittsburgh PA
- Ohio Capital Corporation for Housing, Columbus OH
- Ohio PIRG
- OligarchyUSA
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance, Charlottesville VA
- Michigan PIRG
- Rocky Mountain Peace and Justice Center, CO
- Rhode Island PIRG
- Rural Community Assistance Corporation, West Sacramento CA
- Rural Organizing Project OR
- San Francisco Municipal Transportation Authority
- Seattle Economic Development Fund
- Community Capital Development
- TexPIRG
- The Fair Housing Council of Central New York
- The Loan Fund, Albuquerque NM
- Third Reconstruction Institute NC
- Vermont PIRG
- Village Capital Corporation, Cleveland OH
- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty - Florida
- WashPIRG
- Westchester Residential Opportunities Inc.
- Wigamig Owners Loan Fund, Inc., Lac du Flambeau WI
- WISPIRG

Small Businesses

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Environmental Planning
- Hayden & Craig, PLLC
- Mid City Animal Hospital, Pheonix AZ
- UNET