

Opening Statement of Stephen Hall
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At the SEC Credit Ratings Roundtable, May 14, 2013

Good morning. My name is Stephen Hall and I'm the Securities Specialist at Better Markets, an independent, nonpartisan, non-profit organization that promotes the public interest in the financial markets. We appreciate the invitation to join this important roundtable, and we would like to thank Chairman White, all of the SEC commissioners, and the SEC staff for including us.

In our view, the assignment system known as the Franken amendment is a crucial reform that should be implemented without delay. Here are three reasons why it's so important.

1. First, the other reforms in the Dodd-Frank Act will not do enough to address the conflicts of interest embedded in the issuer-pay model. It's an accepted fact that the grossly inflated ratings assigned to thousands of mortgage-backed securities in the years leading up to the financial crisis helped bring our economy to its knees. As shown in a Better Markets report issued last September, the crisis will ultimately cost our economy at least 13 trillion dollars, along with incalculable human suffering. Clearly, we must eliminate or minimize the conflicts of interest in the issuer-pay model, which contributed so heavily to these devastating consequences.

The Dodd-Frank Act includes many reforms that will help address the problems in the ratings industry. They will enhance disclosure, decrease regulatory reliance on ratings, and increase exposure to liability in private actions. But the conflicts of interest in the issuer-pay model are so strong and so potentially damaging to our financial system that additional measures are necessary.

The assignment system fills this gap by offering a uniquely powerful remedy. Rather than simply attempting to expose or contain conflicts of interest, this approach will fundamentally change the incentives in the ratings for structured products.

2. Second, the assignment system will be effective, without eliminating positive aspects of the credit rating marketplace. It clearly satisfies the core mandate in the Dodd-Frank

Act by preventing the issuer from selecting the NRSRO that determines the initial rating for any structured product. It also provides many other advantages:

- a. It will promote competition, incentivize accurate ratings, restore investor confidence, and ultimately help resuscitate the market for structured finance.
- b. It will be implemented by a new SRO Board that is informed by a variety of perspectives, but ultimately controlled by investor interests.
- c. It will complement, not displace, other reforms under the Dodd-Frank Act.
- d. It will permit issuers to obtain additional ratings for their structured products outside the assignment system.
- e. It will continue to make ratings widely available to the public.
- f. It will be funded by the industry that reaps the principal benefits of the ratings process, not by the government.
- g. And it will be subject to a comprehensive review and evaluation in five years.

Implementation will present challenges of course. The SEC and the CRA Board must carefully draft their rules to ensure that the system works as intended. This means (a) setting strong standards of independence for Board members; (b) overseeing fees and compensation for ratings, not just the assignment process; (c) developing an effective system for evaluating ratings performance; and (d) imposing meaningful sanctions for attempts to evade or violate the rules. All of this can and must be accomplished.

3. Third and finally, the potential costs of the assignment system are minimal compared to the astronomical costs we face if we don't do everything in our power to prevent another financial crisis. Opponents of financial reform invariably exaggerate the costs and the supposedly crippling effects of new regulation. But throughout history, such dire predictions have proven to be unfounded, and they are equally meritless here.

In any case, Congress has settled the debate in favor of the public interest, not industry costs. The Dodd-Frank Act **requires** the SEC to establish an assignment system in the form of the Franken amendment. This requirement is subject to only one exception: a determination by the SEC that an alternative system would **better serve the public interest and the protection of investors**. In other words, any costs, lost revenues, or other detriments to the ratings

industry cannot justify inaction or a change in approach. Rather, the SEC must be guided by what's best for investors and the public interest. That's as it should be.

Thank you again for including Better Markets in this roundtable, and I look forward to discussing these and other issues in greater detail this morning.