March 27, 2023

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Prohibition Against Conflicts of Interest in Certain Securitizations (File No. S7-01-23, RIN 3235-AL04); 88 Fed. Reg. 9,678 (Feb. 14, 2023)

Dear Ms. Countryman:

Better Markets[1] appreciates the opportunity to comment on the above-captioned Proposed Rule ("Proposal" or "Release")[2] of the Securities and Exchange Commission ("Commission"), which would implement prohibitions against conflicts of interest in certain securitizations as required by Section 621 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").

As we approach the fifteenth anniversary of the Financial Crisis of 2008, it is important to remember some of the most egregious behavior that led to the crisis. This includes Wall Street investment banks assembling securitizations comprised of low-grade mortgages, selling them to unsuspecting investors, and then betting against or enabling others to bet against those investments in the derivatives markets. Not only did this especially outrageous conduct victimize the investors who lost hundreds of millions of dollars purchasing these nearly worthless securities, but even more importantly, it contributed to the build-up of systemic risk within out financial system that helped trigger and fuel the worst financial crisis in nearly a century.

After more than a decade since the last time the Commission proposed a rule to implement Section 621 and nearly thirteen years after the Dodd-Frank Act was passed into law, the Commission has reissued its Proposal to prohibit conflicts of interest in securitizations. The Proposal has strengthened several aspects of the rule since it was first issued in 2011 ("2011 proposed rule"), including by incorporating several recommendations Better Markets made in its

1 Better Markets is a non-profit, non-partisan, and independent organization founded in the wake of the 2008 financial crisis to promote the public interest in the financial markets, support the financial reform of Wall Street, and make our financial system work for all Americans again. Better Markets works with allies—including many in finance—to promote pro-market, pro-business, and pro-growth policies that help build a stronger, safer financial system that protects and promotes Americans' jobs, savings, retirements, and more.

2 Prohibition Against Conflicts of Interest in Certain Securitizations, 88 Fed. Reg. 9,678 (Feb. 14, 2023).

comment letter filed in 2012 ("2012 Comment Letter"). For example, the Proposal includes important anti-evasion language as well as documentation requirements for demonstrating compliance with the exemptions for risk-mitigation hedging activities and bona fide market-making activities. The Proposal also refused to dilute the effectiveness of several provisions from the 2011 proposed rule, despite industry arguments for special carveouts and exemptions. Overall, the Proposal would faithfully carry out the Commission's congressionally mandated duty to implement rules to prohibit conflicts of interest in securitization such as we saw in the lead up to the Financial Crisis of 2008. It is time for the Commission to finally adopt this rule.

BACKGROUND

Asset-backed securities ("ABS"), and in particular credit default swaps ("CDS") and collateralized debt obligations ("CDOs"), played a prominent role in the events that led up to the Financial Crisis of 2008. The poorly regulated and poorly policed ABS market, operating in tandem with the unregulated derivatives market, helped to turn a housing crisis into a global financial crisis and the worst economic downturn since the Great Depression. Not only did ABS such as CDS and CDOs help to facilitate fraud and manipulation in the housing markets, they also became a breeding ground for significant fraud in ABS transactions, notwithstanding the mythology that market participants were capable of regulating and policing themselves.

Securitization can be an extraordinarily valuable mechanism for providing credit and liquidity in all major sectors of the economy, ranging from real estate, to the automobile industry, to consumer and commercial credit in general, provided they are designed, structured, and offered in competitive, fair, and well-regulated markets. But securitizations will not function properly in uncompetitive, unfair, and underregulated markets, where market participants can be sold a bill of goods by ABS sponsors and affiliates with impunity. ABS are especially prone to abuse due to their complexities, and as we saw play out in the run up to the Financial Crisis of 2008, conflicts of interest in securitizations can have devastating impacts on even sophisticated, institutional investors.

Goldman Sachs – ABACUS

Perhaps the most infamous example of conflicts of interest in the CDS market in the runup to the crisis involved Goldman Sachs and a set of synthetic CDOs collectively known as "ABACUS." Goldman Sachs structured and marketed the ABACUS CDOs, telling investors that the residential mortgage-backed securities in them had been independently selected by a collateral manager.[3] In fact, Goldman had created the ABACUS CDO at the request of another client, hedge fund manager John Paulson, who wanted to short the housing market. Accordingly, he wanted Goldman to design and create the ABACUS CDOs so that when they would go down in value; he could then purchase a CDS from Goldman ostensibly protecting against their failure and receive a rich payoff once they dropped in value. In fact, he wanted Goldman to create the ABACUS CDOs so he could bet on them to fail.[4] Moreover, Paulson was heavily involved in the portfolio selection process for the ABACUS CDOs, and so was able to populate them with securities he thought

[3] Compl. at 1-2, *SEC v. Goldman Sachs & Co.*, No. 10-cv-3229 (S.D.N.Y 2010).
[4] Compl. at 2, *SEC v. Goldman Sachs & Co.*, No. 10-cv-3229 (S.D.N.Y 2010).

would fail, thus ensuring the profitability of his short position (the collateral agent that was ultimately responsible for selecting the securities was under the impression that Paulson was long the CDO).[5]

Naturally, Goldman did not tell the clients to whom it marketed the ABACUS CDOs that it had created them at the behest of another client who wanted them to fail, nor did it disclose that it had allowed that client to be involved in selecting the securities that would go into the CDO to ensure its failure.[6] The CDO transaction closed in April 2007, at the threshold of one of the most dramatic declines in the history of the U.S. housing market. Unsurprisingly, the portfolio, much of which had been hand-selected by Paulson specifically to lose value, did in fact lose value—in less than a year 99% of the portfolio had been downgraded.[7] As a result, three investors in the ABACUS CDO lost about $1 billion, while Paulson's hedge fund profited by a similar amount.[8] Goldman settled with the SEC for a then-record $550 million and had been subject to civil litigation suits, as a result of its fraud.[9]

J.P. Morgan Securities – CDO Squared

The ABACUS CDO deal was hardly the only example of conflicts of interest that existed in ABSs in the lead up to the crisis. In an ABS offering similar to the ABACUS CDO deal with the hedge fund run by John Paulson, J.P. Morgan Securities sold synthetic CDOs to institutional investors that the hedge fund Magnetar Capital had a hand in assembling and then betting against. In early 2007, J.P. Morgan Securities structured and marketed its $1.1 billion CDO squared product to give investors leveraged exposure to the U.S. housing market at a time when the housing market was showing serious signs of distress.[10] In marketing this CDO squared product to investors, J.P. Morgan Securities falsely represented that the investment portfolio was selected by a specific registered investment adviser with experience in the CDO market.[11] However, much like Goldman's relationship with John Paulson, J.P. Morgan Securities allowed the hedge fund Magnetar Capital to play a significant role in the selection of the assets in the investment portfolio, which Magnetar proceeded to bet against.[12]

J.P. Morgan Securities would proceed to sell approximately $150 million of the mezzanine tranches of the CDO to a group of 15 institutional investors—representing the riskiest assets in the

---

5 Compl. at 2, *SEC v. Goldman Sachs & Co.*, No. 10-cv-3229 (S.D.N.Y 2010).

6 Compl. at 2, *SEC v. Goldman Sachs & Co.*, No. 10-cv-3229 (S.D.N.Y 2010).

7 Jennifer O'Hare, *Synthetic CDOs, Conflicts of Interest, and Securities Fraud*, 48 U. RICH. L. REV. 667, 685 (2014).

8 STAFF OF S. COMM. ON PERMANENT SUBCOMMITTEE ON INVESTIGATIONS, 111TH CONG., WALL STREET AND THE FINANCIAL CRISIS: ANATOMY OF A FINANCIAL CRISIS 12 (COMM. PRINT 2011).

9 *See* SEC Press Release, *Goldman Sachs to Pay Record $550 Million to Settle SEC Charges Related to Subprime CDO* (July 15, 2010), https://www.sec.gov/litigation/litreleases/2010/lr21592.htm. *Goldman Sachs Grp., Inc. v. Arkansas Tchr. Ret. Sys*., 141 S. Ct. 1951 (2021); *see also* Brief of Better Markets, Inc. as Amicus Curiae in Support of Respondents, *Goldman Sachs Grp., Inc. v. Arkansas Tchr. Ret. Sys*., 141 S. Ct. 1951 (2021), https://www.supremecourt.gov/DocketPDF/20/20-222/170888/20210304100303497_20-222%20Amicus%20Brief%20of%20Better%20Markets%20Inc.pdf.

10 Compl. at 1, *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011).

11 Compl. at 2, *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011).

12 Compl. at 2, *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011).

product—without disclosing the role played by the hedge fund Magnetar Capital in selecting the assets for the portfolio and the bet it had made against them.[13] Less than one year later, the CDO had declared default.[14] The SEC later brought an enforcement action against J.P. Morgan Securities that resulted in a settlement and a fine of $153.6 million.[15]

Citigroup – Class V Funding III

While not the most widely known example of conflicts of interest in securitization deals and often overlooked, perhaps the most egregious example of direct conflicts of interest in the CDS market involved the sale of CDOs by Citigroup, particularly its sale of "Class V Funding III." In early 2007, Citigroup structured and marketed its $1 billion CDO squared product which was linked to the U.S. residential housing market.[16] Despite Citigroup's marketing materials stating that a third-party registered investment adviser was used in the asset selection process, Citigroup failed to disclose to investors it played a meaningful role in the asset selection process for $500 million of the assets in the portfolio.[17] Citigroup also failed to disclose that they themselves took a short position against the assets it helped to select in the CDO it sold to investors—betting against the investment product it marketed and sold to those investors.[18]

Citigroup would proceed to sell approximately $343 million of Class V III equity and mezzanine securities to fourteen institutional investors.[19] By November 2007, the CDO squared product had declared default and investors lost several hundred million dollars.[20] Meanwhile, Citigroup reaped at least $160 million.[21] The SEC later brought an enforcement action against Citigroup, resulting in a settlement and a fine of $285 million.[22]

Government Response

The examples of the conflicts of interest in securitizations during the Financial Crisis of 2008 and outright fraud committed by ABS sponsors spurred Congress to take action. In response, Congress enacted comprehensive reforms of our financial markets in the Dodd-Frank Act. That foundational law included several provisions designed to impose new requirements on ABSs, including Section 621. That section prohibits sponsors and other market participants involved in the issuance of ABS, for a year-long period, from engaging in any transaction that would result in any material conflicts of interest with respect to any investor in such transactions, subject to certain conditions and exceptions.[23] The statutory exceptions include risk-mitigating hedging activity,

---

[13] Compl. at 3, *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011).
[14] Compl. at 3, *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011).
[15] *SEC v. J.P. Morgan Securities*, No. 11-cv-4206 (S.D.N.Y. 2011) Litigation Release No. 22008 (June 21, 2011), 2010 WL 6796637 (J.P. Morgan Securities also voluntarily remitted $56,761,214 million to investors of a similar CDO transaction known as Tahoma CDO I).
[16] Compl. at 1, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[17] Compl. at 2, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[18] Compl. at 2, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[19] Compl. at 2-3, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[20] Compl. at 3, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[21] Compl. at 4, *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011).
[22] *SEC v. Citigroup Global Markets*, No. 11-cv-7387 (S.D.N.Y. 2011) Release No. 34-79997 (Oct. 19, 2011).
[23] Section 621 of the Dodd-Frank Act.

trading in connection with liquidity commitments, and bona fide market-making activity.[24] Section 621 also required the Commission to promulgate rules implementing the statutory prohibition against conflicts of interest in securitization transactions.

In response, the Commission issued a Notice of Proposed Rulemaking in 2011 to promulgate rules that would implement the Act's prohibition on conflicts of interests in securitization transactions, including the statutorily required exemptions.[25] However, the proposal was never finalized, delaying for over a decade the regulatory reforms that were so clearly necessary following some of the most egregious behavior that financial institutions engaged in the lead up to the Financial Crisis of 2008. Now, the Commission has issued its re-proposed rule to finally prohibit sponsors of assets-backed securities essentially from betting against the asset-backed securities they create. The Proposal will thus remove or at least limit any incentives that ABS sponsors may have to structure their investments in ways that conflict with the interests of investors.

OVERVIEW OF THE PROPOSAL

The Proposal would implement prohibitions against conflicts of interest in certain securitizations as required by Section 621 of the Dodd-Frank Act. Specifically, proposed Rule 192 would prohibit a securitization participant from engaging in any transaction that would result in a material conflict of interest between the securitization participant and an investor in the relevant ABS for a period of one year. Consistent with Section 621 of the Dodd-Frank Act, the proposed Rule 192 would provide certain exceptions for (1) risk-mitigating hedging activities; (2) bona fide market-making activities; and (3) liquidity commitments.

COMMENTS

More than a dozen years have passed since Congress enacted the Dodd-Frank Act and mandated substantive reforms to the rules governing ABS transactions, including those required under Section 621. The Proposal displays an appreciation and careful consideration of the comments submitted by the public, including Better Markets, on the 2011 proposed rule. The rule is well-designed and there is no reason for further delay. It is well past time to finalize the rules to implement Section 621 and explicitly prohibit material conflicts of interest in certain securitizations, as a complement to the general anti-fraud provisions at the Commission's disposal. The Commission must move forward with the Proposal and carry out its congressionally mandated duty.

I. The Commission has strengthened the reproposed rule in many respects.

The Proposal represents a much-improved reproposed rule compared to the initial 2011 proposed rule. The Proposal adopts a functions-based approach to defining various securitization participants, clarifies the definition of "sponsor" to include collateral managers, includes anti-

24 Section 621 of the Dodd-Frank Act.

25 *See* Prohibition Against Conflicts of Interest in Certain Securitizations, 76 Fed. Reg. 60,320 (Sept. 28, 2011).

circumvention and anti-evasion language, and implements a documentation framework for exceptions to the rule. Overall, the Commission has strengthened various provisions in the current Proposal in relation to the 2011 proposed rule. As discussed below, the Commission should further strengthen the safeguards against potential abuse of the exemptions by requiring Board of Directors and senior management certifications in their compliance programs for risk-mitigating hedging activities and bona fide market-making activities.

First, the Proposal adopts a functions-based approach to the definitions of the terms "underwriter," "placement agent," and "initial purchaser" in an effort to prevent evasion of the prohibition on conflicts of interest in securitizations.[26] As we argued in our 2012 Comment Letter, this is extremely important to ensure that form does not triumph over substance and labels of convenience do not provide loopholes for market participants to exploit. History has taught us that sophisticated market participants with powerful economic incentives are swift to adapt and exploit loopholes in regulated activities. Any person performing functions that are similar to the functions that the enumerated market participants perform, whatever their label, must be held to similar standards. This has been a welcome and common theme in Commission rulemakings in recent years—treating like-for-like. The adoption of function-based definitions is necessary to prevent evasion of the Proposal through label sharing, shifting job duties and responsibilities, and the creation of novel and esoteric categories of securitization participants.

Second, the Proposal clarifies that the definition of "sponsor" is not limited to the definition found in Regulation AB.[27] This is an important distinction because the definition of "sponsor" in Regulation AB would likely not cover key persons in an ABS transaction that should be covered by the conflicts of interest prohibition, such as collateral managers. While industry advocated for a definition of "sponsor" identical to the one found in Regulation AB precisely for the purpose of exempting collateral managers,[28] the Proposal rightly takes a broader view of the term "sponsor" to capture "any person that directs or causes the direction of the structure, design, or assembly of an ABS or the composition of the pool of assets underlying the ABS or has the contractual right to do so."[29]

As we stated in our 2012 Comment Letter, collateral managers should absolutely be covered under the definition of "sponsor" because they play a significant role in selecting, managing, or serving the assets that make up the ABS. Any market participant that has influence in how the ABS is structured, composed, or managed, both prior to and after creation of the ABS,

---

26 Release at 9,684.
27 Release at 9,685.
28 Release at 28 n. 63 ("See SIFMA Letter at 11 (suggesting that the term 'sponsor' be defined as 'a person who organizes and initiates an ABS transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer.'); see also ASF Letter at 22-23 n.36 (supporting the Regulation AB definition of sponsor and stating that '[w]e do not believe the definition of 'sponsor' should cover servicers, custodians or collateral managers, since those who merely service or manage the assets underlying an ABS, by definition, do not play a role in structuring an ABS and are not, therefore, in a position to design the ABS to default or fail'); comment letter from American Bar Association (Feb. 13, 2012) ("ABA Letter") at 4 (supporting the Regulation AB definition of the term 'sponsor')").
29 Release at 9,685.

should be subject to the prohibition on conflicts of interests as Congress intended.[30] Otherwise, the Proposal would include a significant loophole that could be exploited by market participants in the future.

Third, the Proposal substantially lessens the ability of market participants to evade the rule's prohibition on material conflicts of interest with the inclusion of general anti-circumvention language. Proposed Rule 192(d) states "[i]f a securitization participant engages in a transaction that circumvents the prohibition in paragraph (a)(1) of this section, the transaction will be deemed to violate paragraph (a)(1) of this section."[31] This anti-circumvention language is an important and positive addition and it should remain broad to give the Commission ample authority to enforce efforts by market participants to evade the prohibition on material conflicts of interest in the future.

Fourth, the Proposal clarifies that the exception to Rule 192 for liquidity commitments is limited to "purchases and sales."[32] Originally, the 2011 proposed rule suggested that a wide range of activities could fall under the liquidity commitments exception to Rule 192, including short-term loans to ensure adequate cash flows are maintained by investors.[33] However, as we stated in our 2012 Comment Letter, this broad interpretation goes well beyond the plain language of the statute, which limits the exception to "purchases and sales of asset-backed securities."[34] The Proposal recognizes that such "overly broad" exceptions could lead to abusive conduct and therefore limits the exception to "purchases and sales" which is consistent with the statute.[35]

Finally, the Proposal's compliance programs for risk-mitigating hedging activities and bona fide market-making activities strengthen the ability of the Commission to police the use of exceptions to the rule. Specifically, proposed Rule 192(b)(1)(ii)(C) and proposed Rule 192(b)(3)(ii)(E) require securitization participants to establish, implement, maintain, and enforce a reasonably designed internal compliance program to ensure compliance with requirements associated with the use of the risk-mitigating hedging activities exception and the bona fide market-making activities exception.[36] While the exception for the liquidity commitment exception is easier to enforce because at issue will always be the purchase or sale of the underlying ABS, it will be more difficult for the Commission to distinguish permitted risk-mitigating hedging activities and bona fide market-making activities from prohibited activities. That's because those hedging and market-making activities would likely involve the purchase and sale of securities other than the underlying ABS, potentially resulting in direct or indirect conflicts of interest. The Proposal will include requirements to ensure that securitization participants have policies and procedures in place to govern their reliance on the exceptions in Rule 192. They will specifically

---

30 *See* Sens. Merkley and Levin Comment Letter, Prohibition Against Conflicts of Interest in Certain Securitizations, 77 Fed. Reg. 230 (Jan. 3, 2012).
31 Release at 9,727.
32 Release at 9,704.
33 Prohibition Against Conflicts of Interest in Certain Securitizations, 76 Fed. Reg. 60,320, 60,335 (Sept. 28, 2011).
34 Section 621 of the Dodd-Frank Act.
35 Release at 9,704.
36 Release at 9,726-9,727.

require risk-mitigating hedging activities and bona fide market-making activities to be identified, documented, and monitored.

These enhancements in the Proposal are in line with Better Markets' 2012 Comment Letter, in which we argued that the risk-mitigating hedging activities and bona fide market-making activities exceptions to Rule 192 should be subject to written policies and procedures and documentation requirements. [37] As we stated in 2012, these requirements will help to ensure that the exceptions are narrowly applied, abuses are minimal, and that the Commission is better equipped to monitor and enforce Rule 192.

However, the compliance programs could be further strengthened by including accountability mechanisms to ensure the programs are being properly implemented and managed within the company. First, any and all participants utilizing an exception should be required to identify the exception being invoked for each ABS, and management should be required to certify that the activity is for the sole purpose of one of the exceptions—bona fide hedging or market-making—and not for the purpose of generating speculative profits. Second, the Board of Directors and the senior management of the securitization participant should certify the written policies and procedures prior to adoption and on an ongoing basis. These two accountability mechanisms will further strengthen the compliance programs and ensure the Board and senior management are aware of, and responsible for, the proper use of these exceptions.

II. <u>The Commission rightfully resisted calls from industry to dilute the effectiveness of the Proposal.</u>

As with many new laws and subsequent regulations, industry often spends millions of dollars in lobbying efforts to water down proposed rules with often hyperventilated predictions of harm that rarely come to fruition. The Commission's 2011 proposed rule received dozens of comment letters from industry stakeholders seeking to alter the substance of the proposal for their own economic benefit. The Commission's latest Proposal represents an effective proposed rule that would thoughtfully and ably carry out its congressional mandate in Section 621 of the Dodd-Frank Act. The Commission clearly considered many different arguments in response to comment letters received on its 2011 proposed rule, but rightfully resisted calls from industry to dilute the effectiveness of the Proposal. The Commission should continue to push back on arguments from industry that seek unwarranted exceptions and carveouts that are not consistent with Congress's intent.

First, the Proposal appropriately pushed back against industry arguments that disclosure would adequately mitigate or manage material conflicts of interest in securitizations.[38] A disclosure-based framework is not only incapable of curing the conflicts of interest present in securitization but also inconsistent with the text of Section 621 of the Dodd-Frank Act. The text of Section 621 specifically states that securitization participants "shall not…engage in any transaction that would involve or result in any material conflict of interest with respect to any

[37] Better Markets 2012 Comment Letter at 11, 14.
[38] *See* Release at 9,696.

investor in a transaction arising out of such activity."[39] Notably absent from the above text and subsequent exceptions is any mention of an exception based on some specified level of disclosure. The Commission appropriately rejected arguments in favor of a disclosure-based approach and must continue to reject such arguments moving forward.

Second, the Proposal appropriately rejected industry comments seeking an exception for subsidiaries or affiliates of securitization participants based on their use of information barriers. In an effort to enable subsidiaries and affiliates to bet against the ABS of securitization participants, several industry commenters sought an exemption from Rule 192 if they implemented an information barrier regime.[40] However, this approach would be bad policy and also inconsistent with text of Section 621 of the Dodd-Frank Act. Information barrier regimes have historically been unreliable and difficult for regulators to monitor and enforce.[41] Additionally, this approach would again directly contradict the letter and intent of Section 621 of the Dodd-Frank, which specifically lists the entities subject to the prohibition to include "[a]n underwriter, placement agent, initial purchaser, or sponsor, or *any affiliate or subsidiary* of any such entity."[42]

One cause for concern on this subject is the discussion in the Release focused on the possible use of information barriers. Despite the clear statutory language clearly naming affiliates and subsidiaries as subject to the prohibition on material conflicts of interests in securitizations, the Proposal devotes an inordinate amount of attention to discussing how an information barrier regime *could* work. Specifically, the Proposal discusses five conditions governing an affiliate or subsidiary of a securitization participant that might constitute a workable information barrier regime.[43] The Proposal also states "we seek comment on whether information barriers could be designed to effectively mitigate prohibited conflicts of interest and provide adequate protection in this context, whether the use of such barriers would effectively implement Section 27B, and whether internal information barriers are vulnerable to breach." Implementing any form of information barrier regime would be a mistake that would create a significant loophole in the rule and must be rejected.

In short, the Commission must continue to reject the idea that information barriers are an adequate device that could justify exempting affiliates or subsidiaries of securitization participants from the prohibitions on conflicts of interest in securitizations, especially when Congress has specifically stated that they *are* subject to the prohibition.

Third, the Proposal appropriately declines to exclude certain ABS products from the prohibition on conflicts of interests in securitizations. Despite various commenters seeking carveouts and special exemptions for select ABS products, the Proposal recognizes that the

---

39 Section 621 of the Dodd-Frank Act.

40 *See* Release at 9,690 n.92, n.93.

41 *See* Christopher M. Gorman, Note, *Are Chinese Walls the Best Solution to the Problems of Insider Trading and Conflicts of Interest in Broker-Dealers?* IX FORDHAM J. CORP. & FIN. L. 475 (2004) ("Chinese Walls, whether used conceptually to prevent insider trading or structurally to prevent conflicts of interest, are inefficient, largely ineffective, and have more shortcomings than advantages").

42 Section 621 of the Dodd-Frank Act.

43 Release at 9,690-9,691.

language of Section 621 of the Dodd-Frank Act and the intent of Congress in banning such conflicts of interest in connection with any "asset-backed security" is broad and clear. For example, at least one commenter sought an exclusion for non-synthetic ABS from the prohibition;[44] another commenter sought an exclusion for ABS products where investors are involved in the asset allocation;[45] and several commenters sought exclusions for certain synthetic balance sheet collateralized loan obligations.[46] The Commission should continue to decline special industry carveouts and exemptions from the statutorily mandated prohibition on conflicts of interest in ABS.

Fourth and finally, the Proposal appropriately rejects industry arguments that the prohibition on conflicts of interest should be limited to ABS transactions intentionally designed to fail.[47] As we argued in our 2012 Comment Letter, Section 621 of the Dodd-Frank Act contains no reference to an intent requirement and nothing in the phrasing of the language does anything to support a conclusion that Congress intended such a narrowing of the prohibition. In fact, the statutory language compels the opposite conclusion. Section 621 specifically prohibits transactions that would "involve *or result*" in any material conflict of interest.[48] The inclusion of the term "result" is inconsistent with any intent requirement. If the result of the transaction is a material conflict of interest, the text of Section 621 clearly states that it is prohibited. Additionally, the Proposal correctly points out that an intent requirement would greatly increase the difficulty in enforcing the rule.[49] For those reasons, it would be a mistake for the Commission to include an intent requirement in the Rule and it should reject any argument made by commenters to that effect.

CONCLUSION

We hope these comments are helpful as the Commission finalizes the Proposal.

Sincerely,

Stephen W. Hall
Legal Director and Securities Specialist

Scott Farnin

---

44 Release at 9,681.
45 Release at 9,681.
46 Release at 9,682.
47 *See* Release at 9,697, n.125.
48 Section 621(a) of the Dodd-Frank Act (emphasis added).
49 Release at 9,697 ("the need to prove intent could make enforcement of the rule more difficulty, thereby potentially weakening investor protection").

Legal Counsel

Better Markets, Inc.
1825 K Street, NW
Suite 1080
Washington, DC 20006
(202) 618-6464

shall@bettermarkets.org
sfarnin@bettermarkets.org

http://www.bettermarkets.org