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Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Re-Opening of Comment Period for Asset Backed Securities Release (RIN 3235-AK37)

Americans for Financial Reform ("AFR") appreciates this opportunity to respond to the Security and Exchange Commission's ("SEC", or "Commission") Request for Comment on Asset Backed Securities Release (the "Request for Comment"), and the accompanying Memorandum From the Division of Corporation Finance Regarding Disclosure of Asset-Level Data (the "Staff Memorandum"). AFR is a coalition of more than 200 national, state, and local groups who have come together to advocate for reform of the financial industry. Members of AFR include consumer, civil rights, investor, retiree, community, labor, faith based, and business groups.

Section 942 of the Dodd-Frank Act, which contains the new disclosure rules being implemented here, was adopted in response to major abuses in the market for asset-backed securities (ABS) prior to the financial crisis.[1] This market, which produced the 'toxic assets' at the center of the crisis, was marked by extensive problems including fraud and deception of investors. Investors did not understand the weakness of the loans underlying ABS, which in many cases were poorly underwritten or not underwritten at all. Ratings agencies, the supposed monitor of ABS quality, turned out to be an unreliable substitute for rigorous investor due diligence. These agencies faced major conflicts of interest and were highly motivated to preserve the revenue stream from ABS issuers. Issues in the ABS market not only led to massive investor losses, but contributed significantly to the global financial crisis and trillions of dollars in collateral economic damage.

The disclosure requirements in Section 942 are an important advance in transparency for the ABS market. Improved transparency for this market is vital for investor protection and indeed for broader financial stability.

[1] The term 'asset backed securities' in this comment refers to the full range of securities covered under the definition in Section 3(a)(77) of the 1934 Exchange Act, as added by Section 941 of the Dodd-Frank Act, which is the statutory definition applying to these disclosure rules. This definition of asset backed securities includes all securities and re-securitizations backed by self-liquidating loans, including mortgage backed securities, collateralized debt obligations, re-securitizations of collateralized debt obligations, collateralized bond obligations, etc.

For example, this discussion of stress testing bank positions makes clear the crucial importance of granular, loan-level information in understanding the risks of securitizations and the current issues with the availability of such data[2]:

> "Using a consistent method to stress test across asset classes implies the ability to reliably convert forecasts on a potentially large set of macroeconomic factors into performance projections on each of the bank's positions. In the world of structured finance, this ideally means crafting projections at the underlying loan-level. The United States is one country, but each of its fifty states has unique laws and economic environments, which means granular data at the loan-level is critical….Loan-level data can be frustratingly scarce, especially for certain structured finance asset classes like ABS, which contributes to a dearth of granular structured finance asset models."

AFR thus supports strong and rapid action by the SEC to provide investors and third-party consultants performing analytic services for investors with asset-level disclosures adequate to determine the risk of ABS, as well as related assets like re-securitizations and synthetic securitizations that rely on cash flows from asset backed securities. We would note that other jurisdictions, such as the European Union and the United Kingdom, are already providing such asset-level information to investors.[3]

One reason for the delay in the provision of this data in the U.S. has been privacy concerns regarding public disclosure of possibly sensitive information, as related to the method of data access in the original 2010 proposal on asset-level disclosures. In that proposal, the disclosures were to be made on the public EDGAR database. Privacy concerns were addressed by redacting information that would uniquely identify individual debtors (e.g. social security numbers, names, and street addresses) and replacing exact data values with broad ranges in many cases. However, concerns were still raised regarding the combining of this newly public data with other public data sources to re-identify individual borrowers. In addition, the use of data ranges and the restriction of geographic data to the very broad Metropolitan Statistical Area (MSA) level would have substantially compromised the transparency value of the data for investors.

In the Staff Memorandum, the Commission has now proposed an alternative disclosure method that is based on the use of protected web sites for potentially sensitive information, rather than fully public disclosure on EDGAR. AFR broadly supports the protected web site approach, which has two major advantages over the public disclosure of all data on EDGAR:

1) Protected web sites with screened access can limit access to those parties who are investors or provide analytic services to investors, and who agree to accept legal liability for any privacy violations.

[2] Jacobs, Andrew and Stephen Clarke, "The Challenges of Stress Testing U.S. Structured Finance", Moody's Analytics Risk Perspectives: North American Edition, Volume II, December, 2013.
[3] See, for example, the European Data Warehouse, information on which is available at http://www.eurodw.eu/ .

2) Data available on such protected web sites can be more detailed and granular than data provided on fully public sites, and will therefore be more useful for transparency purposes.

It is true that in theory even a protected web site approach could be subverted by actors who were willing to commit fraud by both lying concerning their intended use of the data, and somehow evading their legal liability for privacy violations. If such entities also had the technical sophistication and resources to re-identify data through matching asset-level disclosures to other databases, they could potentially gain access to at least some individual-level data. However, we believe that criminal actors who were both willing to commit fraud and who had a high level of technical sophistication and resources would find it much more rewarding to attack other types of protected data containing information more directly conducive to identity theft, such as social security numbers and dates of birth, neither of which would be available on this data. They could also find it more advantageous to purchase commercially available data, such as loan-level and individual credit report data available from LPS-McDash, Core Logic, or Equifax, rather than taking the legal risks associated with accessing less extensive data on these disclosure web sites. While the Commission must give due weight to legitimate privacy concerns raised by critics of the earlier proposal, the clear and vital statutory mandate in Section 942 should not be sacrificed to a goal of absolute protection from even hypothetical and unlikely privacy threats.

However, AFR also has several criticisms of the Staff Memorandum recommendation.

We do not believe that it is correct or appropriate to give individual issuers the responsibility for maintaining protected web sites storing sensitive information. First, if issuers are given the ability to limit access to asset level data, they may use this ability to inappropriately discriminate between investors or providers of analysis services. Investors with more market power may be given preferential access to the data. Second, we do not believe that all individual issuers will have the technical capacity to implement appropriate privacy controls on protected web sites, nor do we believe that the Commission will have the supervisory resources to police privacy controls at each individual issuer. Finally, if the design of the data is left to individual issuers it is likely to be inconsistent in its technical standards or format, making it more difficult to use.

As an alternative to individual issuer web sites, we would suggest an aggregated 'data warehouse' which would be a single source for sensitive asset level disclosure information. Such a single data warehouse could be supported under several models.

1) A single data warehouse managed by a Federal agency. The data warehouse could be maintained and managed by the Commission itself, by the Federal Reserve (as in the Bank of England model), or by the Office of Financial Research.

2) A non-profit data warehouse that is mutually owned and managed by private sector entities, either issuers, investors, or a third party contractor, under Commission regulatory

oversight. Such a warehouse could be financed on a non-profit basis through small fees on issuers or investors. This is the model of the European Data Warehouse.

It will be much easier to implement and oversee appropriate privacy controls at such a single data warehouse. It will also be easier to police universal and non-discriminatory access for all appropriate users, and incentives to exclude users will be far less than they might be for an individual issuer. Finally, a single data warehouse will also make it easier to ensure consistent data formats so that investors and analysts can more easily make use of the data.

The Staff Memorandum also appeared to include an inappropriately narrow limitation on the types of entities who could legitimately access this asset-level data. Such entities should include not only investors, but also third party providers of analytic services to investors and the financial markets. The ability of third party providers of analytic services to access loan level data would provide a critical new source of sophisticated analysis of credit risk to investors and the broader market. Such analytic service providers would not face the conflict of interest in the issuer-pays model of credit rating agencies, and would provide competition to credit rating agencies in the crucial area of asset-backed securities, where ratings services have historically been the least reliable.[4] We also believe the Commission should investigate making this data available to academic researchers under strict privacy controls, such as those used by the Internal Revenue Service or the Census Bureau for access to micro data. Of course, all users should be required to provide legally binding assurances that the data will not be used for any purpose or in any way that compromises individual privacy of borrowers.

Beyond the issues raised in the Staff Memorandum, AFR also wishes to comment on questions asked in the July, 2011 request for comment on securitization disclosures. In that proposal the Commission requested input on whether asset-level disclosures should be required for asset-backed securities not typically offered under Reg AB, including synthetic ABS, CDOs, CLOs, and ‘novel asset types or structures’ that may be invented by issuers.[5]

The Commission had appropriately proposed in its 2010 release that issuers of structured finance products sold in reliance on Rule 144A or Rule 506 of Regulation D would have to make available to investors comparable loan-level data. AFR believes that asset-level disclosures should be required for all asset backed securities whose risk exposures ultimately trace back to individual loans. In addition, many of these types of securities, including CDOs and re-securitizations of CDOs, fall under the explicit definition in Section 941 of the Dodd-Frank Act. If the Commission’s proposed approach is viewed as lacking sufficient clarity for these types of securities, the appropriate response is for the Commission to clarify the disclosure obligations that would apply, not exempt them from the disclosure requirement.

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[4] See Cornaggia, Jess and Cornaggia, Kimberly Rodgers and Hund, John, “Credit Ratings across Asset Classes” (February 20, 2013).

[5] See CFR 47970-47971 and Questions 98-101 in http://www.sec.gov/rules/proposed/2011/33-9244fr.pdf

The exclusion of synthetic securities and ‘novel asset types or structures’ from loan-level disclosures could have serious and harmful consequences for the financial system by driving issuers toward increasingly complex and exotic types of securitizations in order to conceal risk from investors. The harm created by exotic securitizations that layer and conceal risk is not merely theoretical. For example, recent research shows that losses in CDOs were far higher than losses in the underlying subprime asset-backed securities that were re-securitized to form the CDOs.[6] Furthermore, the same research finds that synthetic CDO collateral showed significantly higher losses than the already extremely high losses in subprime CDOs generally, with each dollar of additional synthetic collateral associated with fifteen cents in additional write downs above and beyond the average CDO write down.[7]

Much of the ‘innovation’ in the securitization space is associated with adding additional layers of complexity and opacity between the underlying loan exposure and the final payment to investors. These layers of complexity make clear understanding of the risk exposure by the investor much more difficult. Yet despite that complexity, each payment ultimately relies on the performance of a loan in the real economy. The purpose of asset-level disclosures is to permit investors to examine the quality of that underlying loan. The Commission’s actions should serve that purpose and should not create incentives for the creation of additional complexity that could mislead investors. The availability of loan-level data for the underlying securities that are ultimately referenced in re-securitizations, as well as credit default swaps and their associated synthetic securitizations should make it technically straightforward to provide true loan-level disclosures even for complex securities.

Thank you for the opportunity to comment on this Request for Comment. Should you have any questions, please contact Marcus Stanley, AFR’s Policy Director, at 202-466-3672 or marcus@ourfinancialsecurity.org.

[6] Cordell, Larry, Lilin Huang, and Meredith Williams, “Collateral Damage: Sizing and Assessing the Subprime CDO Crisis”, Federal Reserve Bank of Philadelphia, Working Paper 11-30/R, May, 2012.
[7] Op cit. table 13, discussion on p. 17