Chairman Angelides, Vice Chairman Thomas and Members of the Commission:

We appreciate the invitation to appear before you and to contribute to the Commission’s work to understand the causes of the financial crisis.

Goldman Sachs and our Business Model

Goldman Sachs is a financial holding company whose principal businesses are investment banking, market making and investment management. We provide services to a diverse and significant client base, which is largely institutional and includes corporations, financial institutions, governments and high net-worth individuals.

Our activities are divided into three general areas:

Our investment banking business provides strategic corporate services, matching the resources of the firm to specific client needs. This frequently means combining advisory, financing and co-investment capabilities. We help clients access equity and debt capital markets in order to grow their businesses, restructure their balance sheets to improve or to solidify their financial strength and to manage their assets and liabilities. We also assess and facilitate strategic options for M&A, divestitures and corporate defense activities. Through our merchant banking activities, we create and manage investment funds consisting of both our own and our clients’ money in order to invest in growing businesses.

Our market making or securities sales and trading business facilitates customer transactions for corporations, financial institutions, governments and individuals through market making and trading of fixed income, equities, currencies, commodities and derivatives products. As a market maker, we provide the necessary liquidity to help ensure that buyers and sellers can complete their transactions and markets can function efficiently. In dislocated markets, we are often required to commit capital to hold client positions over a longer term while a transaction is completed.

Our asset management and securities services businesses help public and private pension funds, corporations, non-profit organizations and high net-worth individuals plan, manage and invest their financial assets for the long-term. We also provide these entities as well as mutual funds and hedge funds with prime brokerage, securities lending and financing services.

You have asked about our business model, major sources of income (or losses) and any changes made.

Before the crisis and since, we have remained focused on providing advice, allocating capital, making markets, managing money and investing with and for our clients. We have all witnessed the consequences of having too narrow a business model. At the same time, we have resisted becoming a financial supermarket – concerned that being too big or dispersed would detract from our focus and expertise.
We have been particularly focused on fee income businesses, such as advisory, commissions and asset management fees, and since our IPO more than ten years ago, we have generated half of our income from them. We continue to see the benefits of a diversified revenue stream across a global franchise centered around integrating advice, execution, financing and co-investing with best-in-class risk management to a broad range of largely institutional clients.

**Lending Activities**

You have asked about specific types of lending activities that may have caused financial problems. While we certainly experienced our share of challenges during the financial crisis, Goldman Sachs was profitable in 2008.

To briefly review, we believe this housing-led downturn has had at least four distinct parts. The first was clearly the U.S. residential mortgage crisis. We experienced limited losses here because of our reluctance to enter the retail mortgage origination business and our proactive management of risk exposures, which I will discuss shortly.

The next leg was related to the broader credit markets. We had a significant amount of leveraged loans given our strong M&A business. But, we identified that exposure early and aggressively reduced it, though not without losses.

The third phase was the pressure on global equity markets and other assets. Since co-investment is important to our strategy and we mark all of these assets at fair value, we are naturally exposed to significant market swings in equity and other asset classes. But we recognized the losses in real time and never allowed the size of those investments to in any way adversely affect our capital or liquidity.

The current phase is the consumer credit cycle. Goldman Sachs has no material exposures to credit cards, auto loans, home equity loans, or consumer loans.

The broader economic weakness has impacted demand for commercial real estate. This market is undergoing stress as the ability to securitize commercial real estate mortgages remains constricted and vacancy rates remain high. While we have experienced losses in our portfolio of assets in this sector, we have reduced our exposure significantly over the past two years.

As the Commission appears to indicate through its lending-related questions, almost all of the losses that financial institutions sustained over the course of the financial crisis thus far have revolved around bad lending practices, particularly in real estate. According to Goldman Sachs Research, the vast majority of the losses can be traced to bad credit decisions in general, and most of those can be traced back to bad real estate loans. While positions in securities like CDOs and in derivatives, such as CDS, led to losses, these instruments embedded and leveraged what were essentially credit risks emanating from lending decisions, not trading decisions.
Trading Risks

The Commission’s focus on lending is noteworthy in light of the fact that some commentators have made statements about the nature and level of trading risk, including proprietary risk, that financial institutions undertake. There has been concern that institutions may be returning to the practices that contributed to the financial crisis. The fact is that for Goldman Sachs, the vast majority of risk we take and the revenues we generate are dominated by trades that advance a client need or objective. Our market making businesses require assuming risk and significant amounts of capital and are deeply imbedded in our risk management processes.

During the financial crisis, this has been especially true as we have helped our corporate and investing clients manage their exposure to interest rate risk, swings in commodity prices and movements in currencies. More broadly, as institutional investors reduced their various risk exposures, they turned to firms like Goldman Sachs, which play the role of intermediary. This ability to help our clients effectively manage their risk, especially in distressed or challenged markets, requires the active and significant commitment of capital.

Risk Management

Policies and Practices

You asked us to discuss our risk management policies and practices as well as our risk exposures.

Our approach to risk management is rooted in accountability, escalation and communication. A large part of this discipline is reflected in the marking process, which assigns current values to financial assets and liabilities. We believe that rigorous fair value accounting for financial instruments is fundamental to prudent management because it facilitates a clear view of risk. It allows us to manage market risk limits, monitor exposure to credit risk and manage our liquidity requirements.

For Goldman Sachs, the daily marking of positions to their fair value was a key contributor to our decision to reduce risk relatively early in markets and in positions that were deteriorating. This process can be difficult, and sometimes painful, but we believe it is a discipline that should define financial institutions. We fair value our positions, not only because we are required to, but because we wouldn’t know how to assess or manage risk if market prices were not reflected on our books.

As I look back prior to the beginning and throughout the course of the crisis, we never knew at any moment if asset prices would deteriorate further, or had declined too much and would snap back. Having to fair value our assets on a daily basis and see the results of that marking in our P&L forced us to cut risk regardless of market or individual views, estimates or expectations.

After the fact, it is easy to be convinced that the signs were visible and compelling. In hindsight, events not only look predictable, but look like they were obvious or known. But none of us know what is going to happen. Risk management begins by admitting this fundamental reality and planning with that mindset as the dominant one running through all of our processes.
We also put great value in our firm-wide committees like the Risk Committee, which monitors financial risk; the Commitments Committee, which looks at our underwriting and distribution activities; the Capital Committee, which focuses on credit extension; and the Business Practices Committee, which reviews operational and reputational risks. These committees create a system of checks and balances that encourage communication between people in both control and business positions and, when necessary, the speedy escalation of a potential issue. Over half the members of our firm-wide committees have worked in two or more divisions at the firm. And, their average tenure at the firm is 17 years.

More broadly, we place great importance on communication between revenue and control areas. This translates into a constant flow of risk reports, and the end result is a better understanding of the risks we are taking.

At the same time, risk and control functions are completely independent from the businesses. Independent verification of prices is frequent and thorough. And, risk managers have at least equal stature with their counterparts in producing divisions. If there is a question about a mark or a disagreement about a risk limit, the risk manager’s view prevails.

Closely related to communication and escalation is accountability. People have to feel responsible for the decisions they make, and for the decisions their subordinates make. If we suffer a credit loss, the relevant business is not absolved of the consequences simply because the risk was approved by the credit department. All flow into one another: Communication encourages escalation and escalation reinforces accountability.

Our Board of Directors regularly reviews and approves the risk profile of the firm, including the firm’s leverage, liquidity risk and other matters. We regularly discuss macro- and business-specific developments with our Board, as well as the potential impact of these factors on the firm’s financial situation. In addition, we periodically review with the Board specific risk analysis, such as stress tests and scenario analysis. In addition to the formal, regular postings (which come from a combination of the CEO, CFO, Chief Risk Officer and Treasurer) the Board interacts on a regular basis with a number of other executives, from both the control and business sides.

**Risk Exposures**

Throughout 2007, we were committed to reducing certain of our risk exposures even though we sold at prices that many in the market, including at times ourselves, thought were irrational, or temporary. But our actions were dictated by daily changes that we were seeing in our P&L through fair value accounting.

In the fourth quarter of 2007, our exposure to leveraged loans, commercial and residential real estate loans, home equity loans and commercial wholesale loans was more than two times our tangible common equity compared with a much higher level across the industry. We then substantially reduced our exposure to these asset classes. For example, since the end of 2007, we have reduced our exposures to leveraged loans, residential real estate and commercial real estate by almost 80 percent to $17 billion or 0.3 times tangible common equity.
Funding and Liquidity

Given our roots as a privately held partnership, we have always focused on maintaining a conservative financial profile. We view liquidity as the single most important consideration for a financial institution, which is why we have lived by a funding motto “more for longer.”

We steadily increased our Global Core Excess pool of liquidity for several years, and it now represents about 20% of our balance sheet, and it is in cash equivalents. We have consistently maintained a significant amount of term in our funding book. The average life of our long-term debt is more than seven years, while our secured funding books’ duration exceeds 100 days.

Keeping this pool of liquidity is expensive. It also inflates our balance sheet and our gross leverage metric. But, it is the best insurance policy we can buy for our shareholders.

Changes Undertaken

While we believe that the extraordinary events and macro economic uncertainty of the past year have validated key attributes of our strategy, culture and processes, they have also prompted change within our firm.

We embraced new realities around regulation and leverage because of our commitment to the long-term stability of our franchise and the overall markets.

The Federal Reserve is now our primary regulator. As a Financial Holding Company, we are subject to the Fed’s capital and leverage tests. Over the last 18 months, our balance sheet has fallen by a quarter, while our capital has increased by over a half. Our Basel I Tier 1 Capital Ratio has increased to 14.5%, through earnings generation and a number of capital offerings. Our tangible common equity grew by 55.5% during the same period to $53.5 billion. In just over a year, we nearly doubled our liquidity balance to over $170 billion.

Our gross leverage ratio is half of what it was going into the crisis – and that metric doesn’t adjust for the cash on our balance sheet. The amount of Level Three, or illiquid assets, is down by almost 50 percent and now represents less than 6 percent of our total assets. In addition, the quality of our capital is very high, with 80 percent in common equity. By any standard, our capital and leverage ratios are the strongest among major financial institutions globally.

Compensation

Lastly, the Commission has asked us to address our compensation policies and practices. Since we became a public company, we have had a clear and consistent compensation policy. We pay our people based on three factors (1) the performance of the firm; (2) the performance of the business unit; and (3) the performance of the individual.

We believe this approach has incentivized our people to act in a way that supports the firm as a whole and to not be parochial or narrow-minded about their specific division or business unit. More broadly, it has produced a strong relationship between compensation and performance.
Since going public in 1999, Goldman Sachs has exhibited a near perfect correlation between changes in net revenues and compensation. From 2000 to 2007, Goldman Sachs has produced a compounded annual growth rate of over 20 percent in earnings per share and 16 percent in book value per share. Adjusted for increased head count over the period, aggregate compensation expense has increased less than 10 percent per year.

Since our IPO, which includes an exceptionally difficult 2008, Goldman Sachs generated an average return on equity of approximately 20 percent for our shareholders.

While the firm produced a profit of $2.3 billion in 2008, our revenues were down considerably. Compensation across the firm, dictated by our policies and practices, reflected that. End of year discretionary compensation was down on average 65 percent. Our most senior people – the firm’s approximately 400 partners -- were down 77 percent on average.

I would also note that Goldman Sachs has never had golden parachutes, employment contracts, special pension arrangements or severance arrangements for its executive officers.

Although we believe our policies and practices have proven to be effective in setting compensation, we have been outspoken about the need to better tie compensation to performance. More importantly, we have outlined specific compensation principles, which are included with this testimony, and have adopted a series of enhancements to our compensation practices consistent with those principles.

In short, we believe:

- The percentage of compensation awarded in equity should increase significantly as an employee’s total compensation increases.

- For senior people, most of the compensation should be in deferred equity. And, senior executive officers should be required to retain the bulk of the equity they receive until they retire. In addition, equity delivery schedules should continue to apply after the individual has left the firm.

- An individual’s performance should be evaluated over time so as to avoid excessive risk taking and allow for a “clawback” effect. To ensure this, all equity awards should be subject to future delivery and/or deferred exercise.

- No one should get compensated with reference only to his or her own P&L. Compensation should encourage real teamwork and discourage selfish behavior, including excessive risk taking, which hurts the longer term interests of the firm and its shareholders.

- To avoid misaligning compensation and performance, multi-year guaranteed employment contracts should be banned entirely. The use of these contracts, unfortunately, is a common practice in our industry. We should all recognize that they are bad for the long-term interests of our industry and the financial system.

On December 10th, 2009, we announced that the firm’s entire 30-person management committee, which comprises all global divisional and regional leadership, will receive 100
percent of their discretionary compensation in the form of Shares at Risk, which cannot be sold for five years.

In addition, we announced that the five-year holding period on Shares at Risk includes an enhanced recapture provision that will permit the firm to recapture the shares in cases where the employee engaged in materially improper risk analysis or failed sufficiently to raise concerns about risks. Enhancing our recapture provision is intended to ensure that our employees are accountable for the future impact of their decisions, to reinforce the importance of risk controls to the firm and to make clear that our compensation practices do not reward taking excessive risk.

Finally, in recent months, we have consulted with many of our largest shareholders on the issue of compensation, specifically philosophy and structure. We found an overwhelming consensus that our model was effective and an important element in producing our strong record of shareholder returns. To further strengthen our dialogue with our shareholders, we announced that they will have an advisory vote ("Say on Pay") on the firm’s compensation principles and the compensation of its named executive officers at the firm’s Annual Meeting of Shareholders in 2010.

We do think it is important to recognize that while incentive structures should be improved across our industry, this is not a panacea for poor risk management. And, the Commission, along with policymakers, regulators and the industry, are appropriately focused on learning from the mistakes made in risk management and elsewhere.

**Contributing Causes to the Financial Crisis**

Without trying to shed one bit of our industry’s accountability, we would also further our collective interests by recognizing other contributing causes to the severity of the crisis.

Factors from both Main Street and Wall Street contributed to today’s circumstances. Neither part of our economy acted completely independently of the other. So, any examination of how we got to this point must begin with an understanding of some of the global economic and financial dynamics of the last two decades.

Certainly, what started in a localized part of the U.S. mortgage market spread to virtually every corner of the global financial markets. But the genesis of the problem wasn’t in sub-prime alone. Instead, the roots of the damage to our financial system are broad and deep. They coalesced over many years to create a sustained period of cheap credit and excess liquidity. The resulting under-pricing of risk led to massive leverage across wide swaths of the economy – from households to the corporate sector to the public sector.

I see at least three broad underlying factors:

- First, there has been enormous growth in the amount of foreign capital, much of it held in large pools, and a very significant shift in the balance of payments of many emerging markets;
- Second, and linked to this, nearly ten years of low long-term interest rates; and
- Third, the official policy of promoting, supporting and subsidizing homeownership in the United States.
Between 1992-2007, the U.S. current account deficit increased by more than 1,300 percent. During the same period, China’s current account surplus increased by over 5,700 percent, as did roughly the surplus for the oil exporting nations.

After previous financial crises, emerging economies began to self-insure against a repeat of those events by building up their foreign currency reserves. Their primary objective was to reduce their dependence on dollar-denominated domestic debt.

Of course, the other, perhaps more significant factor in the growth in current account surpluses had been the record run-up in oil prices since 2000. Increases in global savings run almost parallel with the increase in petrodollar flows.


The flood of foreign capital into safe and liquid assets, particularly U.S. Treasuries, helped push relatively low long-term interest rates down even further. And they stayed low, even after the Federal Reserve began raising short-term rates in 2004.

This was accompanied by a significant reduction in inflation. Between the period 1985 and 1995 versus the next 12 years, inflation in advanced economies fell by more than one-half.

Enormous excess liquidity, strong global economic growth and low real-interest rates created a desire to find new investment opportunities. Many of the best were thought to be in the housing market. The reasons are three-fold.

First, governments, particularly the U.S., explicitly supported homeownership through a variety of government programs and initiatives, recognizing the social benefits from more people owning homes. Second, mortgage assets were considered relatively impervious to sharp downturns. And lastly, the creation of more flexible and varied mortgage products attracted even more capital in search of higher returns.

These factors, to varying degrees, contributed to a housing bubble – not just in the U.S. but in many other countries as well. While real home prices increased nearly 50 percent in the U.S. between 1998 and 2006, they increased more than 130 percent in Ireland, 120 percent in the U.K. and Spain and over 100 percent in France.

Not surprisingly, in the U.S., mortgage origination as a percentage of total mortgage debt outstanding rose from an average of 6.3 percent between 1985 and 2000 to 10 percent between 2001 and 2006. Sub-prime debt, in particular, grew from just over 2 percent in 2002 to 14 percent in 2008. In a sustained environment of cheap capital, lending standards for residential mortgages simply deteriorated.
Lessons Learned

As we have thought about our industry’s understanding of the previous years’ risks, it is important to reflect on some of the lessons learned.

At the top of my list are the rationalizations that were made to justify that the downward pricing of risk was justified. While we recognized that credit standards were loosening, we rationalized the reasons with arguments such as: the emerging markets were more powerful, the risk mitigants were better, there was more than enough liquidity in the system.

We rationalized because a firm’s interest in preserving and growing its market share, as a competitor, is sometimes blinding – especially when exuberance is at its peak.

A systemic lack of skepticism was equally true with respect to credit ratings. Too many financial institutions and investors simply outsourced their risk management. Rather than undertake their own analysis, they relied on the rating agencies to do the essential work of risk analysis for them. This was true at the inception and over the period of the investment, during which time they did not heed other indicators of financial deterioration.

This over-dependence on credit ratings coincided with the dilution of the coveted triple A rating. In January 2008, there were 12 triple A-rated companies in the world. At the same time, there were 64,000 structured finance instruments, like CDO tranches, rated triple A.

Another failure of risk management concerned the fact that risk models, particularly those predicated on historical data, were too often allowed to substitute for judgment. Early on in the crisis, we heard the phrase, “multiple standard deviation events” more than a few times. If events which were calculated to occur likely once in twenty years in fact occurred much more regularly, it doesn’t take a mathematician to figure out that risk management assumptions did not reflect the distribution of actual outcomes. Our industry must do more to enhance and improve scenario analysis and stress testing.

Second, size matters. For example, whether you owned $5 billion or $50 billion of (supposedly) no-risk super-senior debt in a CDO, the likelihood of loss rates would appear to be the same. But the consequences of a miscalculation were obviously much bigger if you had a $50 billion exposure.

Third, risk monitoring and activities often failed to capture the risk inherent in off-balance sheet activities, such as Structured Investment Vehicles (SIVs). It seems clear now that managers of companies with large off-balance sheet exposure didn’t appreciate the full magnitude of the economic risks they were exposed to; equally worrying, their counterparties were unaware of the full extent of these vehicles and, therefore, could not accurately assess the risk of doing business. Post Enron, that is quite amazing.

Lastly, a large institution’s assets should be valued at their fair market value – the price at which willing buyers and sellers transact – not at the (frequently irrelevant) historic value. Some argue that fair value accounting exacerbated the credit crisis. We see it differently. If more institutions had been required to recognize their exposures promptly and value them appropriately, they would have been likely to curtail the worst risks. Instead, positions were not monitored, so changes in value were often ignored until losses at some firms grew to a point when solvency became an issue.
Of course, fair value accounting may not make sense for every institution, particularly those that focus on lending and engage in little or no capital markets activities. We believe the broader aspiration, however, is a guiding one: markets, and ultimately investors, are better served with information that more closely reflects the judgment of the market.

**Regulatory Reform**

The Administration, legislators and regulators are considering important regulatory actions to be taken and our firm pledges to continue to be a constructive participant in that process. In that vein, I believe it is useful, in light of the lessons we take away from this crisis, to consider important principles for our industry, for policymakers and for regulators as we move towards reform.

Risk and control functions need to be completely independent from the business units. And clarity as to whom risk and control managers report is crucial to maintaining that independence. As I mentioned earlier, risk managers need to have at least equal stature with their counterparts in revenue producing divisions.

Capital and credit benchmarks should be subject to more “dynamic regulation.” Regulators should consider the regulatory inputs and outputs needed to ensure a regime that is nimble and strong enough to identify and appropriately constrain market excesses, particularly in a sustained period of economic growth. Just as the Federal Reserve adjusts interest rates upward to curb economic frenzy, various benchmarks and ratios could be appropriately calibrated.

To increase overall transparency and help ensure that book value really means book value, regulators should require that all assets across a systemically important financial institution be similarly valued. Fair value accounting gives investors more clarity with respect to balance sheet risk. How can one justify that the same instruments or risks are priced differently because they reside in different parts of the balance sheet within the same institution?

More specifically, all of the exposures of a financial institution should be reflected through its P&L. If existing and contingent liabilities, credit commitments and other exposures are not transparent, how can risk managers and regulators see all the risks to which an institution is exposed?

In this vein, valuation and capital standards across risky assets, regardless of the form or legal entity in which they are held, must be consistent. Capital standards proved to be adequate for institutions that had all of their risks well-classified and openly held. Unfortunately, a lot of risk had been repackaged (i.e., securitized) and transferred to special purpose vehicles that had lower reporting and capital standards.

Calculations by our economists suggest that closing the gaps just on mortgages held in SIVs and securitizations would have raised capital in the system by over $75 billion, which would have reduced the amount of capital U.S. banks have needed to raise since the start of the crisis by 25 percent. In other words, system-wide capital levels were too low and risks were allowed to grow too large without sufficient warning. If risks had been visible all along, the problems may have been more contained or the panic could have ended much sooner.
Weaknesses or failures in loss recognition created concerns about what would emerge next. One of the larger stresses placed on Goldman Sachs and other firms during the height of the crisis was the possibility that we were hiding risk in the same way other institutions, which were severely hampered or later failed, had hidden their risks. Getting the market to recognize that our balance sheet was well-marked and that our reported capital levels were accurate was one of our significant challenges.

Without question, direct government support helped stabilize the financial system. We believe that the government action was critical and we benefited from it. The system clearly needs to be structured so that private capital, rather than government capital, is used to stabilize troubled firms promptly before a crisis metastasizes.

The two mechanisms that seem to hold the most promise for addressing this goal and addressing “too big to fail” are ongoing stress tests, which are made public, and contingent capital, possibly triggered by failing a stress test, for the conversion of capital. The stress test implemented by the Federal Reserve in 2009 did an effective job of creating a new, higher level of consistency across institutions in terms of disclosure and the valuation of risks. The use of well-structured contingent capital could force any significant shortfalls in capital to be immediately addressed by reducing risk, raising capital or both, without government assistance.

These two elements could also be the core of a strong but flexible resolution authority -- the process to oversee and, if necessary, execute an orderly liquidation of a failing firm -- which we strongly support. Improving the ability of regulators and the market to assess institutions’ real-time health and making recapitalization automatic if capital levels fall below a public threshold would minimize systemic risk and force shareholders and bondholders to bear the burden of the firm’s mistakes, not taxpayers or the economy.

Certainly, enhanced capital requirements, in general, will reduce systemic risk. But we should not overlook liquidity. An institution can have a very low leverage ratio, but that tells you nothing about its liquidity.

If a significant portion of an institution’s assets are impaired and illiquid, and its funding is reliant on short-term borrowing, low leverage will not be much comfort. Problems within financial institutions nearly always become life-threatening as liquidity begins to dry up. That is why regulators should lay out standards that emphasize prudence and the need for longer-term maturities depending on the assets being funded. Institutions should also be required to carry a significant amount of cash at all times, insuring against extreme events. Because of the interconnected nature of finance, one institution’s liquidity crisis can swiftly be transmitted around the system. In determining a robust level of liquidity, regulators should insist on recurring stress tests which we referenced above.

Beyond resolution authority and increased capital and liquidity requirements, policymakers are considering additional reforms.

With respect to OTC derivatives, Goldman Sachs supports the broad move to central clearinghouses and exchange trading of standardized derivatives. A central clearinghouse with strong operational and financial integrity will reduce bi-lateral credit risk, increase liquidity and enhance the level of transparency through enforced margin requirements and verified and recorded trades. This will do more to enhance price discovery and reduce systemic risk than perhaps any specific rule or regulation.
We believe that all liquid OTC derivatives should be centrally cleared. And, where trading volumes are high enough and price discovery mechanisms can be established, regulators should strongly encourage exchange trading. In less liquid markets, prompt reporting of aggregated pricing and clearing is necessary to improve transparency.

More generally, it is incumbent upon financial institutions to recognize that we have a responsibility to the financial system which demands that we should not favor non-standard products when a client’s objective and the market’s interests can be met through a standardized product traded on an exchange.

When customized derivatives are used they should entail more rigorous capital requirements. The pros and cons of buying and selling derivatives on or off an exchange should be immediate and clear to all market participants.

The Administration and many in Congress also are focused on the creation of a Consumer Financial Protection Agency. Because we are an institutional firm that largely focuses on corporations, governments, and large public and private investing organizations, we do not have retail businesses. While we have not expressed a position on the consumer agency and are not engaging policymakers or anyone else on the associated issues, we agree that a more specific focus on consumer protection, whether in the context of a new agency or otherwise, is warranted.

On a related point, we do support the extension of a fiduciary standard to broker/dealer registered representatives who provide advice to retail investors. The fiduciary standard puts the interests of the client first. The advice-giving functions of brokers who work with investors have become similar to that of investment advisers. But, investors may not understand that the person they are getting advice from may be regulated under different rules and regulations. Retail investors should be able expect the same duty of care when they are receiving investment advice.

**Conclusion**

After the shocks of recent months and the associated economic pain, there is a natural and appropriate desire for wholesale reform. We should resist a response, however, that is solely designed around protecting us from the 100-year storm. Taking risk completely out of the system will be at the cost of economic growth. We know from economic history that innovation – and the new industries and new jobs that result from it -- require risk taking.

Similarly, if we abandon, as opposed to regulate, market mechanisms created decades ago, such as derivatives, we may end up constraining access to capital and the efficient hedging and distribution of risk, when we do come through this crisis.

More specifically, the Commission rightly has focused on lending standards and decisions as a primary cause of the financial crisis. While there are a number of contributing causes to the crisis, bad lending associated with the perceived infallibility of the housing market should be a central area of examination and reform. There is more than enough blame to go around, but we would do the process of meaningful reform a disservice if we allowed factors or areas that have had far less of a direct impact on the events of the last two years to detract from a focus on the underlying reasons.
Most of the past century was defined by markets and instruments that fund innovation, reward entrepreneurial risk taking and act as an important catalyst for economic growth. History has shown that a vibrant, dynamic financial system is at the heart of a vibrant, dynamic economy.

We have to safeguard the value of risk capital, which is at the heart of market capitalism, while enhancing investor confidence through meaningful transparency, sound risk management, effective oversight and strong governance. If we fail to achieve this balance, we not only constrain our ability to finance ourselves out of the downturn, we weaken the elements of our financial system that, over the long-term, have contributed significantly to systemic growth and investment.

Thank you.