Risky business

Battles won, lost and somewhere in between …..

Systemic risk regulation
Under current law, there is no single body designated to look at the "big picture," and head off financial crises like the crash of 2008 and major non-bank players in the financial market operated in the shadows without any government oversight

- **We won**:
  - Systemic risk monitoring: A new, council of regulators will both monitor system-wide risk and advise the Federal Reserve Board – the current primary systemic risk regulator.
  - Oversight and limits: For the first time, there will be higher capital, leverage and liquidity standards on the biggest, riskiest financial firms, as well as bank-like oversight for large "shadow bank" financial companies like AIG and the mortgage financers that were at the center of the crisis.

- **We lost**: There remains an unnecessary loophole, inserted in the Senate at the last minute that unnecessarily allows any financial firm that is just 16 percent commercial to escape oversight from the systemic risk council, no matter the threat the firm could pose to the economy.

"The Volcker Rule"
The so-called "Volcker Rule" ensures that banks do not make risky "proprietary" bets for their own accounts with taxpayer-backed deposit funds and limits investment in private funds. Proprietary trading and private fund speculation is not only risky; it puts banks in conflict with their clients and diverts bank capital away from lending to America's small businesses and families.

- **We won**:
  - The Volcker rule was not in the House bill at all. In the Senate-passed version, regulators had wide authority to define proprietary trading. The conference report tightens the definition, narrows exemptions and makes the rule a law, not able to be undone by future regulators.
  - It also includes language banning Goldman-style conflicts-of-interest wherein Wall Street firms package risky securities for customers and then bet that they will fail.
- **We lost**:
  - Long before the conference, efforts to limit the size of banks, as in the Brown-Kaufman amendment, or fully separate Wall Street speculation from Main Street banks with a new Glass-Steagall, were defeated.

- **We compromised:** Sen. Scott Brown was able to win a classic special-interest carve-out that allows banks to trade using private-equity and hedge funds, though they will be limited to investing no more than 3 percent of bank capital and own no more than 3 percent of the fund. But we won key safeguards protecting taxpayers from the danger of Sen. Brown's carve-out: banks will have to hold in capital reserves every dollar that they invest in hedge funds and private equity funds. Additionally, banks cannot bail out their funds.

Taking on Bank Risk:
After decades of deregulation, America's financial industry has grown riskier through overreliance on debt (or "leverage") and dangerous levels of interconnection through derivatives contracts, repurchase ("repo") agreements and other complex products that turned Wall Street into a house of cards.

- **We won**: The final bill ensures that firms don't become too exposed to any single financial counterparty or to their own affiliates. Also, banks will have to hold capital in reserve that reflects all the off-balance sheet debt they could potentially be responsible for in the event of a crisis.
- **We compromised**: The final bill includes delayed implementation of rules to improve the quality of capital that banks have to hold and ensure that leverage and capital standards are higher in the future than they are today.
- **We lost**: The House would have required systemically-risky financial companies to hold at least $1 in capital for every $15 in debt. The conference turned that reasonable leverage ratio into a discretionary standard the Fed could impose only if the systemic risk council finds that the firm poses a grave threat to the economy.

Providing an Alternative to Bailouts with Resolution Authority:
Never again should a few large, risky companies be able to hold the American taxpayer hostage for bailouts when its bets go bad.

- **We won:**
  - The bill expands the FDIC "resolution authority" – the authority to dismantle failing banks – so that the government can safely shut down not just depository banks, but shadow banks like AIG or the conglomerates that own banks (like Citigroup). This will be critical to containing the next financial company failure and providing an alternative to bailouts.
  - To pay for costs associated with the entire bill, the conference originally included a risk-based assessment on large hedge funds and Wall Street banks, to be used in the event of liquidation or, after 25 years, to pay down the national debt. In other words – those that caused the mess will pay to clean it up. Republicans protested, the conference report was reopened, and fee was changed so costs associated with the bill would now be paid for by

a combination of TARP funds and an increase in premiums big banks now pay the FDIC

- **We lost**: The House bill included a $150 fund paid for by the big banks that would protect taxpayers from the cost of shutting down a large, failed financial firm. Opponents of reform grabbed onto the liquidation fund as a talking point – claiming, nonsensically, that this industry-paid fund for shutting down firms was a “bailout fund”.
- **We compromised**: The fund was replaced by a line of credit from Treasury to be repaid by Wall Street in the future.

The Federal Reserve

Federal Reserve Governance Reform:
Today, the powerful Federal Reserve is functionally controlled by its regulated banks, with banks choosing 2 out of every 3 regional Fed Bank directors.

- **We won**: The bill partially ends this conflict of interest by eliminating the ability of the bank representative directors to vote for the regional bank Presidents.
- **We lost**: The conference eliminated the most powerful provisions: barring member banks from voting for directors or bank officers serving as directors (“the Jamie Dimon rule”) and making the powerful NY Fed Bank President presidentially-elected.

Federal Reserve Transparency / Audit:

- **We won**:
  - The bill includes a one-time audit of all Federal Reserve 13(3) emergency lending during the ‘07-‘08 financial crisis, and ongoing GAO audit authority for future 13(3) and Fed discount window lending, as well as its open market transactions.
  - The bill also ends the Fed’s open-ended bailout authority by limiting 13(3) lending to system-wide support for healthy companies, not propping up individual troubled firms, and requiring that taxpayers be paid back.
    - **We lost**: However, the conference eliminated the House’s more comprehensive audit of the Federal Reserve.