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The Honorable Timothy F. Geithner
Secretary of the Treasury
U.S. Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Dear Mr. Secretary:

I am writing on behalf of the American Bankers Association to express the views of the banking industry on the principal issues under consideration for improving the regulatory structure of the financial services industry. The ABA's members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ over 2.2 million men and women.

The ABA strongly supports the creation of a systemic regulator that looks across the economy and identifies potential systemic issues, issues that could relate to certain institutions, products, or practices. However, in this area, as well as others discussed below, practical and political realities also need to be considered. There are limits on how much regulatory change can be undertaken and implemented, particularly in the middle of a crisis, and there are limits on the ability of Congress to pass overly broad legislation. Thus it makes sense, whenever possible, to build on current regulatory mechanisms and therefore, with respect to a systemic regulator, to use the Federal Reserve as that regulator or as the lead regulator.

ABA's preference would be to create a council of regulators to be the systemic regulator and to have the council chaired by the Federal Reserve Chairman. This council should not be a committee of regulators, but rather a stand-alone agency with a small staff specifically charged with identifying systemic issues and recommending solutions. The council should not, ABA believes, regulate institutions itself, but should have access to information from other regulators, as well as back-up authority to obtain additional information, as needed, directly from institutions and to require regulatory action relating to systemic issues.

The ABA also supports regulation of those institutions and financial products that are capable of doing significant harm to the economy, consumers, and businesses, but which are currently not subject to effective regulation. Such gaps in regulation – including hedge funds, credit default swaps and other derivatives, and mortgage brokers – should be addressed in new legislation. Another area where there are gaps relates to payment services outside of the banking system. The Federal Reserve

should have the authority to set performance and operational standards for all significant providers of payments system services.

The ABA strongly supports the creation of a mechanism to address failures of systemically important institutions. The lack of such a mechanism to address problems with Lehman Brothers and AIG clearly contributed to the current financial crisis. Such a mechanism, with clear resolution policies stated in advance, should also limit the consequences of some institutions being perceived as too-big-to-fail.

However, the ABA does oppose proposals to make the FDIC the systemic resolution authority. While the FDIC has experience and a well-deserved reputation with respect to resolving bank failures, future failures of systemically important institutions could involve a broad range of institutions – securities firms, insurance companies, or even hedge funds. The FDIC is seen by the public as the insurer of bank deposits. Consumer confidence in this insurance system for bank deposits has prevented bank runs for many decades. This consumer confidence in the FDIC should not be undermined by having the FDIC directly involved in the failures of all types of institutions, an involvement that would clearly confuse consumers. Furthermore, banks, which pay all costs of the FDIC, should not pick up the tab to run an infrastructure created to deal with future non-bank resolutions. The FDIC's expertise can be tapped as necessary by the creation of a separate resolution authority, defined clearly in advance, but not activated until needed. This authority could use FDIC staff and capabilities, as appropriate.

According to press reports, the Administration may be considering the creation of a separate consumer financial products protection agency. The ABA is strongly opposed to the creation of such an agency for a number of reasons. First, many believe that the existing financial regulatory structure is overly complex. It would be amazing, therefore, if the Administration's first proposal in this area contains the creation of yet another large agency with overlapping authority with other agencies. Such a new agency would need to be large enough to deal with all financial products to be effective and fair. It would also need to be able to cover products of federally regulated, state regulated, foreign regulated and currently unregulated entities. Since in our evolving economy new products that compete with old ones are constantly being invented, without such broad jurisdiction products outside the authority of the new agency would compete with, and often crowd out, regulated products.

For example, the product line that caused the most damage to our economy and to individuals in recent history was those mortgages that were unfair and unaffordable. It is worth noting what Chairman Barney Frank said about these mortgages:

> Reasonable regulation of mortgages by the bank and credit union regulators allowed the market to function in an efficient and constructive way, while mortgages made and sold in the

> unregulated sector led to the crisis. At every step in the process, from loan origination through the use of exotic unsuitable mortgages to the sale of securities backed by those mortgages, the largely unregulated uninsured firms have created problems, while the regulated and FDIC-insured banks and savings institutions have not.[1]

Thus a consumer financial product protection agency would have to focus on all mortgage originators and investors. This same breadth of jurisdiction would be necessary for all savings, investment, lending, transaction and other financial products. Legislation including the creation of an agency with such wide authority would engender broad opposition and efforts for carve outs. Already there are efforts underway to carve out products such as mutual funds.

Finally, ABA does not believe it is rational to separate consumer policy from enforcement, operational issues and safety and soundness issues, as would be the case under the proposal. For example, issues relating to check hold periods involve consumer issues, but they also involve significant fraud and payments system operational issues that need to be balanced. Wherever there are perceived weaknesses in the protection of consumers by regulated depository institutions – banks and credit unions – they should be specifically addressed, but not by the creation of yet another regulatory agency.

Also, according to press reports, the Administration may be considering the creation of a single prudential regulatory agency for banks, in effect merging the OCC, OTS, and the bank regulatory functions of the FDIC and the Federal Reserve Board. The ABA is adamantly opposed to this concept because we believe it would, as a practical matter, be the end of a true dual banking system. Such a federal regulatory agency would undoubtedly have a strong bias toward federally regulated institutions. Therefore, state regulated banks would be at a disadvantage. The dual banking system has served our country well, particularly in terms of innovation of products and regulatory mechanisms. Furthermore, there has been no indication that the dual banking system contributed to the financial crisis; indeed, the diversity of our banking system has provided strength in overcoming the crisis. Finally, the model for this approach would appear to be the Financial Services Authority of the United Kingdom. As Chairman Barney Frank pointed out on CNBC this morning, this model did not work well in preventing the current crisis in that country.

In closing, let me briefly touch on several other issues relevant to the regulatory restructuring debate. First, the ABA has testified on several occasions that the systemic regulator cannot function effectively without some role in the oversight of accounting policy. In April, the G-20 took a similar position. We urge the

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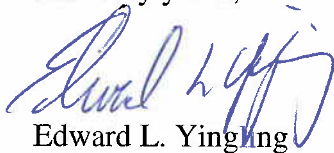
[1] B. Frank, "Lessons of the Subprime Crisis," Boston Globe (Sept. 14, 2007)

Administration to support addressing this issue as part of creating a systemic regulator. Second, the ABA strongly supports the continuation of the OTS in its current form under Treasury. Third, the ABA strongly supports our historic system of charter options and would oppose the elimination of any of the current charters. Fourth, the ABA urges the creation of an optional federal charter for insurance firms.

Reform of our regulatory structure for financial institutions is a critical issue to bankers across the country. There appears to be a growing consensus in support of creating a systemic regulator, filling gaps in the regulatory structure relating to less regulated entities, and developing a system to address troubled institutions that are systemically risky. These issues alone are extremely complex and difficult. Other issues are both highly controversial and very complicated. In particular, the creation of a new consumer financial product regulator is likely, based on our discussions with other associations in the financial services sector, to be broadly and deeply opposed. In addition, creating a single federal prudential regulator would also raise strong opposition because of its negative impact on the dual banking system. These controversial issues, if included in restructuring legislation, are likely to undermine chances for enacting reform.

Thank you for considering the views of the ABA on regulatory reform.

Sincerely yours,



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