Testimony of Richard L. Trumka

President

AFL-CIO

House Financial Services Committee

Hearing on Systemic Regulation, Prudential Matters,

Resolution Authority and Securitization

October 29, 2009

Good morning Chairman Frank and Ranking Member Bachus. My name is Richard Trumka, and I am the President of the AFL-CIO. The AFL-CIO is a federation of 57 unions representing 11.5 million members. Our members were not invited to Wall Street's party but we have paid for it with devastated pension funds, lost jobs, and public bailouts of private sector losses. Our goal is a financial system that is transparent, accountable and stable—that is the servant of the real economy rather than its master.

The AFL-CIO is a member of the Americans for Financial Reform coalition. We share the Coalition's four core goals:

1) Create a consumer financial protection agency

2) Reregulate the shadow financial markets—derivatives, hedge funds and private equity

3) Create a strong fully public systemic risk regulator

4) Address the housing crisis.

We strongly commend the Committee for your work on the Consumer Protection Agency.

However, we are deeply concerned that the Committee's work thus far on the fundamental issues of regulating shadow financial markets and institutions will allow the

very practices that led to the financial crisis to continue. The loopholes in the derivatives bill and the failure to require any public disclosures by hedge funds and private equity funds fundamentally will leave the shadow markets in the shadows. We urge the Committee to work with the leadership to strengthen these bills before they come to the House floor.

With respect to systemic risk regulation, the Americans for Financial Reform and the AFL-CIO strongly support the concepts in the Treasury Department White Paper that a systemic risk regulator must have the power to set capital requirements for all financial institutions that are large enough or connected enough to affect the stability of the financial system. We also strongly support the Treasury's proposal to give the systemic risk regulator the power to place such an institution in a resolution process run by the FDIC.

However, these powers must be given to a fully public body, and one that is able to benefit from the information and perspective of the routine regulators of the financial system. We believe a new agency, with a board made up of a mixture of the heads of the routine regulators and direct Presidential appointees would be the best structure. However, if the Federal Reserve were made a fully public body, it would be an acceptable alternative.

But we cannot support the discussion draft made public earlier this week because it gives dramatic new powers to the Federal Reserve without reforming its governance so that the banks themselves are removed from the governance of the Federal Reserve System. Even more alarmingly, the discussion draft would appear to give power to the Federal Reserve to preempt a wide range of rules regulating the capital markets—power which could be used to gut investor and consumer protections. If this Committee wishes to give more power to the Federal Reserve, it must make clear this power is only to strengthen safety and soundness regulation and it must simultaneously reform the Federal Reserve's governance. Reform cannot be put off until another day.

The Federal Reserve currently is the regulator for bank holding companies. In that capacity, it was responsible throughout the period of the bubble for regulating the parent companies of the nation's largest banks. While regulatory authority rests in the Board of Governors of the Federal Reserve in Washington, routine responsibility for regulatory oversight has been delegated by the Board of Governors to the regional Federal Reserve Banks. The Federal Reserve System's regulatory expertise resides in these regional banks.

The problem is that these regional Federal Reserve Banks are actually controlled by their member banks—the very banks whose holding companies the Fed regulates. The member banks control the selection of the majority of the regional bank boards, and the boards pick the regional bank presidents, who are effectively the CEO's of the regulatory staff.

These arrangements may explain why the Federal Reserve has never given any account of how it allowed bank holding companies like Citigroup and Bank of America to arrive at a point where they required tens of billions of dollars of direct equity infusions from the public purse to avoid bankruptcy.

Giving the Federal Reserve with its current governance control over which financial institutions are bailed out in a crisis is effectively giving the banks the ability to raid the Treasury for their own benefit.

We are also deeply troubled by provisions in the discussion draft that would allow the Federal Reserve to use taxpayer funds to rescue failing banks, and then bill other non-failing banks for the costs. The incentive structure created by this system seems likely to increase systemic risk.

We believe it would be more appropriate to require financial institutions to pay into an insurance fund on an ongoing basis. Financial institutions should be subject to

progressively higher fee assessments, and stricter capital requirements, as they get larger. This would be a way of actually discouraging "too big to fail."

In addition, language in the draft that appears to limit taxpayer bailouts of bank stockholders actually does no such thing, rather it simply ensures that when stockholders are rescued with public funds, bondholders and other creditors are rescued with them.

With regard to the provisions related to asset-backed securities, we are pleased that the legislation would require loan originators and securitizers to retain a portion of the risk in the securitizations they originate and pool. We are concerned, however, that the draft continues to allow the SEC to suspend or terminate disclosure requirements. The authority given to the SEC to require disclosures does not appear to be substantially different from those that exist under current law.

Finally, and not least, the discussion draft appears to envision a process for identifying and regulating systemically significant institutions, and for resolving failing institutions, that is secretive and optional—in other words, the Federal Reserve could choose to take no steps to strengthen the safety and soundness regulation of systemically significant institutions. In these respects, the discussion draft appears to take the most problematic and unpopular aspects of the TARP and makes them the model for permanent legislation.

Instead of repeating and deepening the mistakes associated with the bank bailout, Congress should be looking to create transparent, fully publicly accountable mechanisms for regulating systemic risk and for acting to protect our economy in any future financial crises.

On behalf of the AFL-CIO, I thank you for the opportunity to testify today, and look forward to your questions.