



Americans for Financial Reform
1629 K St NW, 10th Floor, Washington, DC, 20006
202.466.1885

September 2, 2011

Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Re: Consultative Document – Effective Resolution of Systemically Important Financial Institutions

Dear Sir or Madam:

American for Financial Reform (“AFR”) appreciates this opportunity to comment on the Consultative Document regarding Effective Resolution of Systemically Important Financial Institutions (SIFIs). AFR is a coalition of more than 250 American organizations who have come together to advocate for reform of financial sector regulation. Members of the AFR include consumer, civil rights, investor, retiree, labor, religious and business groups along with prominent economists and other experts.

We welcome the Financial Stability Board’s (FSB) support for comprehensive measures “to improve the capacity of authorities to resolve systemically important financial institutions without systemic disruption and without exposing the taxpayer to the risk of loss.” As a representative of citizens’ organizations that were dismayed by the exceptional transfer of private losses to the public balance sheet during the 2008-09 financial crisis, we are deeply aware of the negative effect of bailouts. We fully support the view conveyed early in the paper that the public support of major financial institutions during the crisis increased moral hazard in a very significant way. Effective resolution mechanisms are a key to preventing future bailouts, lessening the expectation of public support, and thus reinstating market discipline on SIFIs.

There are many specific positive elements in this document, including the strong support for cross-border sharing of information and the support for resolution plans. However, AFR is concerned that the document does not sufficiently emphasize the importance of coordinated regulatory action to reduce the complexity of large international financial institutions. Instead, the document for the most part appears to accept such complexity as a “fact of life” and attempts to plan regulatory mechanisms for addressing it in the event of a resolution. But as the document itself admits at several points, the current level of complexity of international financial institutions makes this task extremely challenging at best. The document should place a greater emphasis on the need for regulators to work together to reduce the size and complexity of

international financial institutions, rather than simply attempting to accommodate the current level of complexity within an international resolution framework.

AFR's comments at this time are generally limited to this issue. However, we also advance some recommendations for the improvement of resolution plans.

Recommendations Must Place a Greater Emphasis on Reducing The Complexity of International Financial Institutions

The consultative document admits at several points that the current level of complexity of international financial institutions renders an effective international resolution regime extremely difficult and perhaps impossible. For example, on page 10 of the document the Board states:

“The complexity and integrated nature of many firms’ group structures and operations, with multiple legal entities spanning national borders and business lines, make rapid and orderly resolutions of these institutions under current regimes virtually impossible.”

Given this frank admission of the enormous problems created for financial regulation by the complexity of financial firms, it is striking that supervisory action to actually reduce this complexity seems to be such a low priority in this document. Almost the entire document is devoted to schemes for handling and managing complexity across international borders. But the only mention of actually SIFI reorganization to reduce complexity is a brief and general recommendation in part 3.3 of Annex 6 that SIFIs should “identify areas in their existing organizational structure where there is unnecessary complexity....and take measures to reduce those complexities.” While we agree that financial firms should do this, we doubt that they actually will.

This omission is all the more striking given the evidence that the complexity of international SIFIs is driven less by genuine economic efficiencies than by regulatory and tax arbitrage, attempts to render shareholder monitoring more difficult, and simple accretion of institutional complexity driven by frequent financial mergers.¹ These factors have driven the complexity of financial institutions far beyond that of other large corporations. As the scholar Richard Herring has pointed out²:

“The sixteen large, complex international financial institutions identified by the IMF and the Bank of England have 2.5 times more majority-owned subsidiaries than the 16 largest multinational manufacturing firms..... The most complex SIFI has 2,435 majority-owned subsidiaries, 50% of them chartered abroad”

¹ Herring, Richard and Jacapo Carmassi, “The Corporate Structure of International Financial Conglomerates”, in *The Oxford Handbook of Banking*, Oxford: Oxford University Press, 2010.

² Herring, Richard, “Wind-Down Plans As An Alternative To Bailouts: The Cross Border Challenges”, in *Ending Bailouts As We Know Them*, edited by Kenneth Scott et. al. Stanford, CA: Hoover Institution Press, 2009.

In light of the events of 2008, it is time for a change in supervisory culture and more aggressive regulatory action to actually reduce institutional complexity and size. As Lord Turner of Britain's Financial Services has stated³:

“In the past, authorities around the world have tended to be tolerant of the proliferation of complex legal structures designed to maximize regulatory and tax arbitrage. Now we may have to demand clarity of legal structure”

Furthermore, such reductions in complexity are likely to create benefits for top management oversight of financial risks taken by SIFIs. The same complexities that make monitoring and resolution planning difficult for regulators can make effective risk management difficult for central management of SIFIs.

There are many avenues open to supervisors to reduce organizational complexity. Perhaps the most important is that when regulators are not satisfied that the SIFI is able to lay out a clear process for resolution that avoids systemic risk, they should require that the SIFI divest subsidiaries or reorganize its structure until an orderly resolution is possible. AFR urges that this step be explicitly added to Annex 4 of the document, as a part of the process of resolvability assessment.

Concerns about complexity should be incorporated into the approval process for bank mergers. Supervisors should question the reasons for multiplication of subsidiaries and intra-organizational complexity as they see such multiplication occurring, and should inform management of any concerns and the possibility that resolution planning concerns could lead to the need for divestment.

In cases where regulators encourage separate subsidiaries for reasons of reducing risk (e.g. “firewalls” between risky activities and the rest of the bank), they should ensure that such firewalls will actually protect the institution from risk. In the United States prior to the financial crisis the effectiveness of New Deal reforms that effectively protected “utility” banking institutions from speculative risks was gradually eroded and in the end almost completely eliminated. But much of the organizational complexity that resulted from this structure remained. AFR supports separation between risky speculative activities and core banking services – but not when such separation is merely cosmetic and simply serves to increase organizational complexity. (Note also however, that in cases where “ring-fencing” of risky activities is truly effective in walling off speculative risks from core systemically significant activities, AFR would oppose the Board's implied statement on page 63 of the document that such ring-fencing should be discouraged simply because of concerns about recovery of assets in case of a bankruptcy).

In sum, the document contains many valuable recommendations regarding resolution planning and resolvability that would encourage regulators to exchange information, encourage SIFIs to improve management information systems and take steps to improve the continuity of operations, etc. These

³Giles, Chris, Patrick Jenkins, and George Parker, “[Living Wills to Be Forced on Banks.](#)” *Financial Times*, September 15, 2009.

are all useful steps. But they are unlikely to be truly effective in the absence of a more thorough commitment to actually reducing the complexity of international financial institutions.

14. Does Annex 5: Recovery and Resolution Plans cover all critical elements of a recovery and resolution plan? What additional elements should be included?

AFR has previously made recommendation to U.S. national authorities concerning resolution plans.⁴ These recommendations include the requirement that each SIFI develop a continuous virtual database of total counterparty credit and loan exposures that can be immediately disaggregated by counterparty or borrower and legal entity, and also includes information on the collateral for each exposure.

There are several reasons for this requirement. First, this credit information is the crucial data to determine the types of financial contagion that could occur in the event of material distress at a major SIFI. It is likely that this information will be a crucial input for regulators to determine the implications of a bankruptcy or indeed a Title II resolution procedure. Second, it would be prudent to ensure that the top management of a SIFI to understands the full range of credit exposures across their entire institution. Finally, this requirement would serve as an incentive for SIFIs to reduce their internal complexity.

Thank you for the opportunity to comment on this consultative document. If you have any further questions, please contact Marcus Stanley, AFR's Policy Director, at marcus@ourfinancialsecurity.org or (202) 466-3672.

Sincerely,

Americans for Financial Reform

⁴ Americans for Financial Reform, [Comment on Proposed Rule Regarding Resolution Plans and Credit Exposure Reports \(RIN 7100-AD73\)](#), June 10, 2011.

Following are the partners of Americans for Financial Reform.

All the organizations support the overall principles of AFR and are working for an accountable, fair and secure financial system. Not all of these organizations work on all of the issues covered by the coalition or have signed on to every statement.

- A New Way Forward
- AARP
- AFL-CIO
- AFSCME
- Alliance For Justice
- Americans for Democratic Action, Inc
- American Income Life Insurance
- Americans United for Change
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- Center for Media and Democracy
- Center for Responsible Lending
- Center for Justice and Democracy
- Center of Concern
- Change to Win
- Clean Yield Asset Management
- Coastal Enterprises Inc.
- Color of Change
- Common Cause
- Communications Workers of America
- Community Development Transportation Lending Services
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO Mobile
- CTW Investment Group
- Demos
- Economic Policy Institute
- Essential Action
- Greenlining Institute
- Good Business International
- HNMA Funding Company

- Home Actions
- Housing Counseling Services
- Information Press
- Institute for Global Communications
- Institute for Policy Studies: Global Economy Project
- International Brotherhood of Teamsters
- Institute of Women's Policy Research
- Krull & Company
- Laborers' International Union of North America
- Lake Research Partners
- Lawyers' Committee for Civil Rights Under Law
- Move On
- NASCAT
- National Association of Consumer Advocates
- National Association of Neighborhoods
- National Community Reinvestment Coalition
- National Consumer Law Center (on behalf of its low-income clients)
- National Consumers League
- National Council of La Raza
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National People's Action
- National Council of Women's Organizations
- Next Step
- OMB Watch
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO
- Progress Now Action
- Progressive States Network
- Poverty and Race Research Action Council
- Public Citizen
- Sargent Shriver Center on Poverty Law
- SEIU
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Fuel Savers Club
- The Leadership Conference on Civil and Human Rights
- The Seminal
- TICAS
- U.S. Public Interest Research Group
- UNITE HERE
- United Food and Commercial Workers

- United States Student Association
- USAction
- Veris Wealth Partners
- Western States Center
- We the People Now
- Woodstock Institute
- World Privacy Forum
- UNET
- Union Plus
- Unitarian Universalist for a Just Economic Community

Partial list of State and Local Signers

- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans For Responsible Lending
- Association for Neighborhood and Housing Development NY
- Audubon Partnership for Economic Development LDC, New York NY
- BAC Funding Consortium Inc., Miami FL
- Beech Capital Venture Corporation, Philadelphia PA
- California PIRG
- California Reinvestment Coalition
- Century Housing Corporation, Culver City CA
- CHANGER NY
- Chautauqua Home Rehabilitation and Improvement Corporation (NY)
- Chicago Community Loan Fund, Chicago IL
- Chicago Community Ventures, Chicago IL
- Chicago Consumer Coalition
- Citizen Potawatomi CDC, Shawnee OK
- Colorado PIRG
- Coalition on Homeless Housing in Ohio
- Community Capital Fund, Bridgeport CT
- Community Capital of Maryland, Baltimore MD
- Community Development Financial Institution of the Tohono O'odham Nation, Sells AZ
- Community Redevelopment Loan and Investment Fund, Atlanta GA
- Community Reinvestment Association of North Carolina
- Community Resource Group, Fayetteville A
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (NYC)
- Cooperative Fund of New England, Wilmington NC
- Corporacion de Desarrollo Economico de Ceiba, Ceiba PR

- Delta Foundation, Inc., Greenville MS
- Economic Opportunity Fund (EOF), Philadelphia PA
- Empire Justice Center NY
- Empowering and Strengthening Ohio's People (ESOP), Cleveland OH
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing
- Fitness and Praise Youth Development, Inc., Baton Rouge LA
- Florida Consumer Action Network
- Florida PIRG
- Funding Partners for Housing Solutions, Ft. Collins CO
- Georgia PIRG
- Grow Iowa Foundation, Greenfield IA
- Homewise, Inc., Santa Fe NM
- Idaho Nevada CDFI, Pocatello ID
- Idaho Chapter, National Association of Social Workers
- Illinois PIRG
- Impact Capital, Seattle WA
- Indiana PIRG
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc., Mayville NY
- La Casa Federal Credit Union, Newark NJ
- Low Income Investment Fund, San Francisco CA
- Long Island Housing Services NY
- MaineStream Finance, Bangor ME
- Maryland PIRG
- Massachusetts Consumers' Coalition
- MASSPIRG
- Massachusetts Fair Housing Center
- Michigan PIRG
- Midland Community Development Corporation, Midland TX
- Midwest Minnesota Community Development Corporation, Detroit Lakes MN
- Mile High Community Loan Fund, Denver CO
- Missouri PIRG
- Mortgage Recovery Service Center of L.A.
- Montana Community Development Corporation, Missoula MT
- Montana PIRG
- Neighborhood Economic Development Advocacy Project
- New Hampshire PIRG
- New Jersey Community Capital, Trenton NJ
- New Jersey Citizen Action
- New Jersey PIRG
- New Mexico PIRG
- New York PIRG
- New York City Aids Housing Network
- NOAH Community Development Fund, Inc., Boston MA
- Nonprofit Finance Fund, New York NY

- Nonprofits Assistance Fund, Minneapolis M
- North Carolina PIRG
- Northside Community Development Fund, Pittsburgh PA
- Ohio Capital Corporation for Housing, Columbus OH
- Ohio PIRG
- OligarchyUSA
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance, Charlottesville VA
- Michigan PIRG
- Rocky Mountain Peace and Justice Center, CO
- Rhode Island PIRG
- Rural Community Assistance Corporation, West Sacramento CA
- Rural Organizing Project OR
- San Francisco Municipal Transportation Authority
- Seattle Economic Development Fund
- Community Capital Development
- TexPIRG
- The Fair Housing Council of Central New York
- The Loan Fund, Albuquerque NM
- Third Reconstruction Institute NC
- Vermont PIRG
- Village Capital Corporation, Cleveland OH
- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty - Florida
- WashPIRG
- Westchester Residential Opportunities Inc.
- Wigamig Owners Loan Fund, Inc., Lac du Flambeau WI
- WISPIRG

Small Businesses

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Environmental Planning
- Hayden & Craig, PLLC
- Mid City Animal Hospital, Pheonix AZ
- The Holographic Repatterning Institute at Austin
- UNET

