AMERICANS FOR FINANCIAL REFORM
ACCOUNTABILITY ★ FAIRNESS ★ SECURITY

Americans for Financial Reform
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July 29, 2014

Dear Representative,

On behalf of Americans for Financial Reform (AFR), we are writing to express our opposition to HR 5018, "The Federal Reserve Accountability and Transparency Act".[1] Among other responsibilities, the Federal Reserve is the single most significant regulator of U.S. financial institutions, including the large Wall Street banks that played a central role in the 2008 financial crisis. This legislation would dramatically reduce the ability of the Federal Reserve to effectively regulate these institutions. Section 4 of the legislation would require the agency to give detailed advance information to major financial institutions concerning the methods that will be used for 'stress testing' their safety and soundness. Section 7 of the legislation would impose dozens of complex and potentially contradictory cost-benefit requirements that must be satisfied prior to any Federal Reserve rulemaking. Any one of these cost-benefit requirements could be used as the basis for a lawsuit by Wall Street interests seeking to avoid regulatory oversight. These provisions are completely at odds with the ability of the Federal Reserve to perform its regulatory functions.

AFR has consistently supported reform of the Federal Reserve. This includes support for legislation on Federal Reserve transparency advanced by former Representative Ron Paul and Senator Sanders, and support for legislation on ending conflicts of interest in Federal Reserve governance advanced by Representative De Fazio and Senator Sanders.[2] Most recently, we have strongly opposed the lack of appropriate accountability and limitations in the Federal Reserve's proposed emergency lending powers, echoing criticisms that have also been made by Chairman Hensarling of the Financial Services Committee.[3] However, the major impact of this legislation would not be to reform the Federal Reserve, but to empower our largest banks to block Federal Reserve regulatory oversight of Wall Street. Below, we detail specific issues with the bill.

Section 4 – Requirements For Stress Tests

Section 165 of the Dodd-Frank Act requires the Federal Reserve, as the consolidated supervisor of the major bank holding companies that dominate Wall Street, to subject these financial

[1] Americans for Financial Reform is a coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups.

[2] See e.g. Americans for Financial Reform, "AFR Supports Federal Reserve Transparency Amendment", May 4, 2010; Americans for Financial Reform, "AFR Letter To Senator Sanders Re Federal Reserve Independence Act", June 1, 2012.

[3] Americans for Financial Reform, "Comment Letter Re Extensions of Credit By Federal Reserve Banks; Docket No. R-1476 RIN 7100-AE08", March 10, 2014. See also U.S. House of Representatives, Committee on Financial Services, "Comment on Extensions of Credit By Federal Reserve Banks", January 13, 2014.

institutions to annual supervisory ‘stress tests’. These tests are intended to serve as an objective and independent check on the financial soundness of the financial institution and the private resources it has available to absorb potential future losses due to its loans and other investments. The stress testing requirement is designed to protect taxpayers and avoid a situation like the one experienced in 2007 and 2008, where despite clear signs of financial stress the major banks distributed some $80 billion in dividends to shareholders. Later in 2008, taxpayers had to make up this lost capital through capital injections under the TARP program.[4]

Stress tests have become crucial to the emerging post-crisis system of financial supervision. Federal Reserve Governor Tarullo recently called them a ‘cornerstone’ of the regulatory response to the financial crisis.[5] Yet the changes made in Section 4 of this bill would greatly weaken the ability of the Federal Reserve to perform effective supervisory stress testing. The legislation would require public notice and comment rulemaking in advance of any stress test that detailed the exact models, methodologies, and assumptions to be used in the stress test. Just as one would not require schools to provide tests to their students in advance, it is inappropriate to require the Federal Reserve to provide the details of what is intended to be an independent supervisory assessment to regulated entities in advance.

Such advance notice would allow banks to tailor their exposures to the specific methods to be used by the Federal Reserve to measure their risk. The ability to ‘game the system’ in this manner would reduce the efficacy of stress tests as an objective and external check on bank risks. It would also encourage an unhealthy private sector focus on making decisions that produced benefits under the Federal Reserve’s stress testing models, rather than pursuing independent judgments of risk and benefit. In addition, this change would allow banks to bring lawsuits under the Administrative Procedures Act to block stress test procedures they feel would reveal shortcomings in their risk management.

AFR is critical of some aspects of Federal Reserve stress testing policies, particularly in cases where a reliance on stress testing seems to be a substitute for more fundamental structural reform. More information concerning the stress testing process, possibly including some modeling assumptions, could be useful for the public to better understand the strengths and weaknesses of stress tests as a supervisory method. But the Federal Reserve does already provide significant transparency into the stress test process, both in its post-test announcements of results and through events such as the annual Stress Test Modeling Symposiums sponsored by the Boston Federal Reserve. Furthermore, it is crucial that any additional transparency be created in a manner that does not reduce the value and efficacy of stress tests as an independent supervisory check on bank risks. The changes in this bill certainly do not meet this requirement.

Section 7 – Requirements for Cost Benefit Analysis

Section 7 of the legislation imposes some two dozen new requirements for cost-benefit analysis prior to any Federal Reserve rulemaking, or interpretation of an existing rule or law. Indeed,

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[4] Rosengren, Eric, “Dividend Policy And Capital Retention: A Systemic ‘First Response’ “, Speech delivered at Rethinking Central Banking Conference, Washington, DC, October 10, 2010.
[5] Tarullo, Daniel, “Stress Testing After Five Years”, Speech delivered at the Third Annual Stress Test Modeling Symposium, Boston, Massachusetts, June 25, 2014.

since the section also requires the agency to assess the costs and benefits of all the potentially numerous alternatives to the regulation actually proposed, the additional analyses required by this legislation could easily be far greater. Not only are these new requirements numerous and complex, they are also potentially contradictory. For example, the section requires that any new regulation impose "the least burden…on market participants" and also that it "maximize net benefits". Yet the regulatory approach that maximizes net benefits for society may not be the approach that minimizes costs for market participants.

Because these new requirements are placed in statute, any Wall Street interest seeking to block a Federal Reserve rule could sue in court by contesting the Federal Reserve's findings on any of these numerous cost-benefit requirements. (This is a crucial distinction between these statutory requirements and cost-benefit language in executive orders or recommendations). Due to the inherent uncertainty and difficulty in the quantitative measurement of the impact of financial regulations, including hypothetical alternatives to such regulations, it will always be possible for industry-funded researchers to contest them in some way. For example, an extensive industry-funded study of new global capital rules claimed that they would raise U.S. lending rates by over 4.6 percentage points – between eight and sixteen times higher than the estimates found by multiple independent studies.[6] Even genuinely independent studies can show significant uncertainties in the future impacts of financial regulations.[7]

In this context, it is worth noting that the Federal Reserve employs more PhD economists than any other institution in the world, and already performs extensive economic analysis on the impact of its regulations. For example, the Federal Reserve played a central role in the analysis of the economic impact of new Basel Committee capital standards and global derivatives rules. As part of this analysis, at least four different major impact assessments were published, each of which drew on dozens of different academic and regulatory economic analyses.[8] The effect of the cost-benefit provisions in this legislation would not be to improve economic analysis at the Federal Reserve. Instead, by enabling Wall Street lawsuits on any of numerous cost-benefit requirements, this legislation would take economic analysis out of the hands of the hundreds of

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[6] The industry-funded report is Institute for International Finance, "The Cumulative Impact on The Global Economy of Changes In The Financial Regulatory Framework", Washington, DC, September 6, 2011. See Table I.1 for U.S. lending rate estimate. For an example of independent studies finding far lower impacts, see e.g. Santos, Andre Olveira and Douglas Elliot, "Estimating the Costs of Financial Regulation", International Monetary Fund, IMF Staff Discussion Note SDN 12/11, September 11, 2012. See Table 6 for cumulative U.S. lending rate estimate. This study also provides a literature review of other studies.

[7] For example, international regulators consulted seven different academic models in estimating the benefits of raising bank capital standards. While on average these models showed strong benefits from increasing capital from current levels, the benefits varied from extremely high to in one case almost zero. See Annex II, Table A2.1, in Basel Committee on Banking Supervision, "An Assessment of the Long-Term Economic Impacts of Stronger Capital and Liquidity Requirements", Bank of International Settlements, August, 2010.

[8] Basel Committee on Banking Supervision, "An Assessment of the Long-Term Economic Impacts of Stronger Capital and Liquidity Requirements", Bank of International Settlements, August, 2010; Macroeconomic Assessment Group, "Final Report: Assessing the Impact of the Transition to Stronger Capital and Liquidity Requirements", Bank of International Settlements, December, 2010; Macroeconomic Assessment Group, "Assessment of the Macroeconomic Impact of Higher Loss Absorbency For Global Systemically Important Banks", Bank of International Settlements, October 10, 2011; Macroeconomic Assessment Group on Derivatives, "Macroeconomic Impact Assessment of OTC Derivatives Regulatory Reforms", Bank of International Settlements, August, 2013.

high-level economists employed by the agency and place it in the hands of judges and lawyers who may have no formal economics training at all.

Section 9 – International Negotiations

Section 9 of this bill requires an extensive schedule of public consultation and comment before and after any employee of the Federal Reserve Board, FDIC, or Treasury "enters into negotiations" with any foreign or multinational entity. The regulation of global financial markets involves extensive consultations with foreign regulators, including regulators of banks active in the U.S. markets, and interactions with foreign and multinational entities are routine for U.S. regulators. The vague definition of 'enters into negotiations' and the extensive consultation requirements in this section would place an impossible administrative burden on financial regulators, potentially requiring volumes of paperwork before any phone call with their international counterparts.

It is also ironic that this section does not improve or increase public transparency in an area where improved public transparency is desperately needed, namely international trade negotiations and the activities of the U.S. Trade Representative (USTR) regarding financial regulatory issues. The USTR conducts extensive secret multi-year negotiations that can have profound impacts on a range of financial regulatory issues, and provides very little transparency or access into the process. In contrast, financial regulators, including multinational consultative groups, provide significant detail on their regulatory recommendations and proposals to the public, and solicit public comment in advance of final recommendations.[9]

While AFR would favor improved transparency for international negotiations, such transparency must be compatible with the capacity of financial regulators to work with their international counterparts free of excessive bureaucratic burdens. And the first priority for such transparency should be trade negotiations, not financial regulatory issues where significant transparency is already available.

Other Provisions of the Bill

Other sections of this legislation include some provisions worthy of further exploration on their own. This includes various provisions in Section 8 that would permit Federal Reserve governors to hire their own staff and possibly certain ethics requirements, as well as provisions that increase the number of times the Federal Reserve chair testifies on monetary policy.

Section 2 of the legislation proposes an extensive set of new requirements around monetary policy. AFR has not taken positions in this area.

In sum, we urge you to reject "The Federal Reserve Accountability and Transparency Act". Instead of genuinely improving accountability and transparency at the Federal Reserve, the effect

[9] See for example the Financial Stability Board web site at www.financialstabilityboard.org which contains information on international processes and proposals, as well as the Bank of International Settlements at www.bis.org .

of this bill would be to empower Wall Street to prevent effective Federal Reserve oversight of the nation’s largest banks.

Thank you for the opportunity to express our views on this legislation. Should you have additional questions on this issue, please contact Marcus Stanley, AFR’s Policy Director, at marcus@ourfinancialsecurity.org or 202-466-3672.

Sincerely,
Americans for Financial Reform

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.

- AARP
- A New Way Forward
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Income Life Insurance
- American Sustainable Business Council
- Americans for Democratic Action, Inc
- 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
- Center for Effective Government
- 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
- Green America
- Greenlining Institute

- Good Business International
- HNMA Funding Company
- Home Actions
- Housing Counseling Services
- Home Defender's League
- Information Press
- Institute for Agriculture and Trade Policy
- 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
- Lawyers' Committee for Civil Rights Under Law
- Main Street Alliance
- Move On
- NAACP
- 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 Council of Women's Organizations
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Resource Center
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Nurses United
- National People's Action
- National Urban League
- Next Step
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO National Network
- 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

List of State and Local Partners

- 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
- New Economy 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

- New Yorkers for Responsible Lending
- 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
- UNET