



Americans for Financial Reform
1825 K St NW, Suite 210, Washington, DC, 20006
202.263.4533

June 11, 2010

Chairman Christopher Dodd
United States Senate
Washington, DC 20510

Chairman Barney Frank
United States House of Representatives
Washington, DC 20510

Re: Support Senate Derivatives Reform Sec. 716: Separation of swaps dealing from taxpayer-protected banks

Dear Senator/Representative:

We write on behalf of Americans for Financial Reform, an unprecedented coalition of over 250 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, religious and business groups as well as Nobel Prize-winning economists. We write to express our strong support for maintaining the Senate financial reform bill's Section 716 policy of protecting taxpayers from losses in the \$600 trillion derivatives market through a mandatory separation of swaps dealing from taxpayer-protected banks.

Reckless swaps and derivatives trading played a critical role in the financial crisis, turning the fallout from the crash of the domestic housing market into a global economic catastrophe. As the House and Senate conference committee sit down to align their respective financial services bills, Americans for Financial Reform believes that making section 716 a part of the final bill is a critical element of enhancing the security of our financial system, and refocusing our banks on sound lending to consumers and businesses.

No More Gambling with Taxpayer Money

The five largest banks in the United States — Goldman Sachs, Morgan Stanley, JP Morgan Chase, Citigroup and Bank of America — have anticompetitive control over 90% of the U.S. swaps and derivatives market. Currently, these five bank-dealers can fund their swaps trading units with FDIC-insured deposits. They have access to the Federal Reserve's discount window, which allows them to borrow money for gambling in swaps at near-0% interest rates. Ironically, these government supports were originally created to reassure the public that their deposits are safe, and to protect banks from runs on their deposits — not to help banks finance their own Wall Street casinos. Section 716

of the Senate derivatives title will end this subsidy of these giant players risky derivatives business.

More Bank Capital for Main Street Lending

In effect, Section 716 will require the five largest swaps dealer banks to spin off their swaps desks into **separately-capitalized affiliates**. As a leading global investor surveyed by Bloomberg News notes, this “would ensure that capital is not taken from other banking areas and used to meet regulatory requirements of derivative trading or cover the losses being experienced in derivative trading...**This will mean that capital needed for the real economy, personal and corporate lending, won’t be taken up by fictitious investments.**”

Contrary to industry lobbyist claims, if Section 716 is implemented, banks will still be able to serve their customers in the same manner they always have. **Their affiliated swaps desks will still be able to sell a full range of financial products and they will still be able to hedge their own risks.** Under the Senate bill’s comprehensive exchange-trading regime, banks will use the exchange-traded futures market to hedge risk like any other market participants. However, unlike today, customers’ deposits and savings accounts – and the banks’ ordinary lending business – will be protected from the fallout from highly risky swaps transactions.

Unique Strengths of Section 716

First, Section 716 requires the big banks to spin off their derivatives desks, which would separate this risky business from the Federal Reserve window, FDIC insurance, and the taxpayer guarantee. No other measure in the House or Senate bills protects the taxpayers in this manner.

Second, Section 716 increases competition. Currently, the big banks make up 90% of the derivatives market. Requiring the big banks to put their trading desks into separately capitalized affiliates will bring transparency to the pricing of derivatives, remove the unfair subsidy provided by the commercial banks special privileges, and will encourage competition from other entrants into the market.

Third, Section 716 increases stability in the system. Capital inadequacy was a key cause of the financial crisis. The additional robustness of the capital requirements created by housing derivatives desks in separate entities will reduce risk by shrinking the enormous exposure of a few very large banks that can threaten the stability of other financial institutions. **It will reduce the artificial financial leverage of the products Warren Buffet has called “weapons of mass financial destruction” — and will greatly increase stability in the system.**

Finally, Section 716 reduces counterparty risk in the system by shifting risk to smaller institutions and encouraging participation by more counterparties. Even if the spun off institutions in which derivatives desks will be housed are affiliates of the big banks, they will be substantially smaller than the banks and will have smaller capital reserves. This means that non-bank entrants, who are currently locked out of the market because they cannot compete with big banks, will be encouraged to participate. This will increase the

number of counterparties and, therefore, lower risk across the system. The fact that the Bank of International Settlements estimates 31% of all OTC derivatives transactions are between dealers means that the symbiotic relationship among these five major banks remains a ticking time bomb. If one “too big to fail” bank collapses, it can cause the collapse of another behemoth bank, and ultimately lead to another economic crisis.

Merkley-Levin Not A Substitute

AFR strongly supports the Volcker Rule and the amendment to strengthen it, offered by Senators Merkley and Levin. However, these provisions are not interchangeable with Section 716. The Volcker Rule deals only with propriety trading (when Goldman-Sachs for instance, trades for its own account). Augmented by Merkley-Levin, the Volcker Rule would comprehensively ban bank holding companies and subsidiaries from engaging in this type of trading, and would further crack down on Goldman-style conflicts of interest in securities trading. But without Section 716, banks will still be able to divert capital from their core business to “make markets” in derivatives, exposing taxpayers to future bailouts. These two provisions are complementary and together move the bill towards the type of structural reform that is sorely warranted by the greatest financial crisis since the Great Depression.

Thank you for considering the Americans for Financial Reform position on these important issues. For more information on derivatives reform, please contact Heather Slavkin, AFL-CIO, at 202-637-5318 or hslavkin@aficio.org.

Sincerely,

Americans for Financial Reform

CC: Members of Financial Reform Conference Committee

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.

National Organizations

- A New Way Forward
- AARP
- Accountable America
- Adler and Colvin
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Family Voices
- American Income Life Insurance
- Americans for Democratic Action, Inc.
- Americans for Fairness in Lending
- American Sustainable Business Council
- Americans United for Change
- Business for Shared Prosperity
- Calvert Asset Management Company, Inc.
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- 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
- Community Law Center
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO
- CTW Investment Group

- Demos
- Economic Policy Institute
- Essential Action
- Green America
- Greenlining Institute
- Good Business International
- Help Is On the Way, Inc
- HNMA Funding
- 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
- Keystone Research Center
- Krull & Company
- Laborers' International Union of North America
- Lake Research Partners
- Lawyers' Committee for Civil Rights Under Law
- Leadership Conference on Civil Rights
- MoveOn.org Political Action
- NAACP
- NASCAT
- National Association of Consumer Advocates
- National Association of Investment Professionals
- National Association of Neighborhoods
- National Coalition for Asian Pacific American Community Development
- 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 Institute
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Peoples Action
- National Council of Womens Organizations
- National Workright Institute
- Next Step
- OMB Watch
- Opportunity Finance Network
- Partners for the Common Good
- National People's Action (NPA)
- PICO
- Progress Now Action
- Progressive States Network
- Poverty and Race Research Action Council
- Public Citizen

- Responsible Endowments Coalition
- Sargent Shriver Center on Poverty Law
- Scam Victims United
- SEIU
- Sojourners
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Carrots and Sticks Project
- The Fuel Savers Club
- The Seminal
- UNET
- Union Plus
- United for a Fair Economy
- U.S. PIRG
- Unitarian Universalist for a Just Economic Community
- United Food and Commercial Workers
- United States Student Association
- USAction
- Veris Wealth Partners
- Veterans Chamber of Commerce
- We The People Now
- Western States Center
- Woodstock Institute
- Working America
- World Business Academy
- World Privacy Forum

State Organizations

- 207 CCAG
- 9 to 5, the National Association of Working Women (CO)
- AARP Rhode Island
- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans for Responsible Lending
- Arkansas Community Organizations
- Arkansas Public Policy Panel
- Association for Neighborhood and Housing Development (NY)
- Audubon Partnership for Economic Development LDC (New York, NY)
- Aurora NAACP
- BAC Funding Consortium Inc. (Miami, FL)
- Beech Capital Venture Corporation (Philadelphia, PA)
- Bell Policy Center (CO)
- California PIRG
- California Reinvestment Coalition
- Center for Media and Democracy
- Center for NYC Neighborhoods
- 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)
- Club Change of Martin County (Florida)
- Coalition on Homeless Housing in Ohio
- Coffee Party of Pensacola, Florida
- Coffee Party of Union Square, New York City
- Colorado AFL-CIO
- Colorado Center on Law and Policy
- Colorado Immigrants Rights Coalition
- Colorado PIRG
- Colorado Spring NAACP
- Community Action of Nebraska
- Community Capital Development
- 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, AR)
- Connecticut Association for Human Services
- Connecticut Citizen Action Group
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (New York, NY)
- Cooperative Fund of New England (Wilmington, NC)
- Corporacion de Desarrollo Economico de Ceiba (Ceiba, PR)
- CWA 7777 (CO)
- Delta Foundation, Inc. (Greenville, MS)
- Economic Opportunity Fund (EOF) (Philadelphia, PA)
- Empire Justice Center (NY)
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing Enterprises, Inc. (Berea, KY)
- Fitness and Praise Youth Development, Inc. (Baton Rouge, LA)
- Florida Consumer Action Network
- Florida PIRG
- Forward Community Investments (Madison, WI)
- Funding Partners for Housing Solutions (Ft. Collins, CO)
- Georgia PIRG
- Grow Iowa Foundation (Greenfield, IA)
- Homewise, Inc. (Santa Fe, NM)
- Humanitas Community Development Corporation
- Idaho Chapter, National Association of Social Workers
- Idaho Community Action Network
- Idaho Nevada CDFI (Pocatello, ID)
- Illinois PIRG
- Impact Capital (Seattle, WA)
- Indiana PIRG

- Indiana University PIRG
- Information Press (CA)
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc. (Mayville, NY)
- Keystone Research Center
- 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
- Massachusetts Fair Housing Center
- MASSPIRG
- 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
- Montana Community Development Corporation (Missoula, MT)
- Montana PIRG
- Mortgage Recovery Service Center of L.A.
- 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
- Next Step (MN)
- NOAH Community Development Fund, Inc. (Boston, MA)
- Nonprofit Finance Fund (New York, NY)
- Nonprofits Assistance Fund (Minneapolis, MN)
- North Carolina Association of Community Development Corporations
- North Carolina PIRG
- Northern Community Investment Corporation (St. Johnsbury, VT)
- Northside Community Development Fund (Pittsburgh, PA)
- Ohio Capital Corporation for Housing (Columbus, OH)
- Ohio PIRG
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance (Charlottesville, VA)
- Rhode Island PIRG
- Rights for All People
- The Rocky Mountain Peace and Justice Center
- Rural Community Assistance Corporation (West Sacramento, CA)
- Rural Organizing Project OR
- San Francisco Metropolitan Transportation Authority
- Seattle Economic Development Fund dba Community Capital Development

- SEIU Local 105 (Colorado)
- SEIU Rhode Island
- Siouxland Economic Development Corporation (Sioux City, IA)
- Southern Bancorp (Arkadelphia, AR)
- TexPIRG
- The Association for Housing and Neighborhood Development
- The Fair Housing Council of Central New York
- The Help Network
- The Loan Fund (Albuquerque, NM)
- Third Reconstruction Institute (NC)
- V-Family, Inc.
- Vermont PIRG
- Village Capital Corporation (Cleveland, OH)
- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty – Florida
- Washington Community Action Network
- WashPIRG
- Westchester Residential Opportunities Inc. NY
- Wigamig Owners Loan Fund, Inc. (Lac du Flambeau, WI)
- WISPIRG

Businesses

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Env. Planning
- Hayden & Craig, PLLC\
- The Holographic Repatterning Institute at Austin
- Mid City Animal Hospital (Phoenix, AZ)
- UNET