Policy Update
December 7, 2009

Last week, Federal Reserve Chairman Ben Bernanke went through four hours of grilling before the Senate Banking Committee in his bid for confirmation for a second term. His current term expires January 31, 2010. The Chairman was criticized for a whole range of decisions and actions taken by the Fed and was admonished to make any number of goals his number one priority going forward. Final Senate confirmation is expected, although four Senators have already come out in opposition to his confirmation.

Meanwhile, FDIC Chair Sheila Bair announced in an interview that she will not seek a second term. Her current term expires in 18 months.

The final staging was completed for full House consideration of omnibus financial services reform legislation this week. On the Senate side, committee staff and members continue to work to develop a bill that keeps centrist Democrats on board while adding a few Republicans. No committee legislation is expected to emerge until next month.

House to Consider Financial Reform

The House Financial Services Committee reported out the final piece of comprehensive financial reform legislation, a new approach to dealing with systemically important institutions. This bill has been added to other bills passed by the committee and other committees in the House into one 1,279-page behemoth, H.R. 4173.

During the consideration of this legislation, FHLBanks raised a number of concerns that, by and large, were satisfactorily addressed during the markup process. These amendments include exempting FHLBanks from the reach of the new Consumer Financial Protection Agency and from concentration limits on institutions identified as systemically important. An additional issue that will likely be addressed this week on the House floor will be the exemption of FHLBanks from a provision that would impose loss sharing by secured creditors of failed systemically important institutions. The amendment addressing the issue will be offered on the floor by the sponsors of the original problematic amendment, Reps. Miller (D-NC) and Moore (D-KS).

As this legislation moves beyond the House, we will be working on additional issues, including the removal of FHLBanks from any obligation to contribute to a systemic resolution fund; the exemption of FHLBanks from statutory leverage limits that might be imposed on systemically important entities; and mitigation of the impact on the Bank resulting from derivatives reform. It is quite possible that additional issues will arise.

The major elements of H.R. 4173 are:

- The Consumer Financial Protection Agency (CFPA);
- An inter-agency Financial Stability Council to monitor systemic risk;
- Resolution authority to handle the collapse of large institutions;
- Shareholder “say on pay” on executive compensation with authority for regulators to monitor incentive-based provisions in contracts;
- The regulation of the Over-the-Counter derivatives market;
- New mortgage reform legislation;
- Reform of credit ratings agencies and their conflicts of interest;
- Creation of a Federal Insurance Office; and
- The required registration of private pools of capital with the Securities and Exchange Commission (SEC).

Derivatives Legislation Update

House Financial Services Committee Chairman Barney Frank and House Agriculture Committee Chairman Frank Peterson announced a compromise between two versions of legislation on the regulation of derivatives, which previously passed their respective committees. The chairmen agreed the CFTC and SEC, and not the clearinghouses, should decide what trades would require a clearinghouse process. The two did not, however, agree on whether end-users exempt from the clearinghouses should post higher margin requirements, a position supported by the Treasury.

Treasury Secretary Tim Geithner testified before the Senate Agriculture Committee on derivatives legislation, maintaining the Administration’s position that all “liquid and standard” derivatives contracts should trade through clearinghouses. He stated that the Treasury continues to work with the House and Senate on finding the right balance for granting “carefully crafted exemptions” for end-users, although no agreement exists at this time. Secretary Geithner asserted that any derivatives free of the clearinghouse requirement should post higher margin and capital, increasing the incentives to move toward standardized clearinghouses. The Lehman Brothers bankruptcy received attention as well, as several Senators stated the need for segregation of collateral in future legislation, a provision supported by the FHLBanks.