

THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT

The financial crisis cost millions of jobs, erased more than \$16 trillion in household wealth, and deeply scarred confidence in the integrity of the financial markets. The Dodd-Frank Wall Street Reform and Consumer Protection Act addresses key gaps and weaknesses in the system to help make future financial shocks less likely and less damaging. That's critical because investors need confidence in the underlying safety, stability, and integrity of the financial system if they are going to put their capital to work financing new products, new businesses, and new jobs. The Dodd-Frank Act's reforms are vital to restoring that trust and rebuilding a pro-growth, pro-investment financial system. It helps achieve those objectives by:

- *Promoting a Safer, More Stable Financial System Focused on Sustainable Growth and Job Creation.*
- *Putting in Place a Dedicated Watchdog for Consumers.*
- *Bringing the Derivatives Market Out of the Darkness and Into the Light of Day.*
- *Providing New Tools for Winding Down Failing Firms Without Putting the Economy in Jeopardy.*

Safer, More Stable Financial System Focused on Sustainable Growth and Job Creation. In the years leading up to the crisis, too much risk built up in the financial system. Firms focused on short-term profits rather than investments that finance sustainable, long-term growth. The Dodd-Frank Act provides a new framework for reining in excessive risk-taking on Wall Street and refocusing the financial system on activities that strengthen – rather than threaten – the health of our economy.

- ***Strong Oversight of Large, Interconnected Firms.*** Under Dodd-Frank, large interconnected financial companies will operate under prudential supervision by the Federal Reserve. Additionally, heightened prudential standards, including capital, liquidity and risk management standards, will help ensure that these companies do not escape strong oversight or threaten financial stability.
- ***Coordinated Oversight.*** The Financial Stability Oversight Council (FSOC), which brings together federal and state financial regulators, provides a mechanism to identify and respond to emerging system-wide threats to financial stability. The FSOC is promoting unprecedented cooperation among its members through information sharing, coordinated rulemakings, and its risk monitoring activities. In January, the FSOC released statutorily required studies on the Volcker Rule and on a concentration limit within the U.S. financial system. The FSOC will also soon release its inaugural annual report making recommendations to Congress, regulators, and market participants on steps to address emerging threats and vulnerabilities in the US financial system.
- ***Office of Financial Research.*** The Dodd-Frank Act created the Office of Financial Research (OFR) to support the FSOC by providing data and analysis to identify, evaluate, and respond to risks to financial stability. The OFR also seeks to promote

transparency and improve the quality of information in the financial system – in part by standardizing financial data. The OFR has already launched a global initiative to standardize how parties to financial contracts are identified: the Legal Entity Identifier (LEI) initiative. Such a system would not only help regulators and institutions monitor counterparty risk, it would also facilitate consistent reporting requirements across the federal regulatory system.

- ***Reforming Executive Compensation.*** Certain pay practices on Wall Street encouraged firms to focus on short-term profits rather than investments that strengthen long-term growth. Dodd-Frank helps address this issue by allowing the “clawback” of pay from executives responsible for a firm’s failure; providing greater independence for compensation committees; putting in place a “say on pay” vote for shareholders; and other important reforms. More than 2,500 public companies have already held “Say on Pay” votes under Dodd-Frank. Already, shareholder input has had an impact on incentive compensation programs and golden parachute payments, and shareholders at some companies have voted to reject executive pay packages.
- ***Volcker Rule.*** The Volcker Rule limits banking entities’ risky non-core business activities that are not customer focused. Banks will be prohibited from proprietary trading and limited in their relationships with hedge funds and private equity funds. Some financial institutions already have begun to wind down these business practices in anticipation of the implementation of this provision.
- ***Cracking Down on Abuses in the Mortgage Market.*** In the years leading up to the crisis, predatory lending proliferated, standards for mortgage loans deteriorated, and too many homeowners took on debt they couldn’t afford. Dodd-Frank includes critical anti-predatory lending protections, such as requiring mortgage brokers and banks to consider a family’s ability to repay when making a loan; banning abusive practices like those where brokers got paid more to steer families into higher priced loans than those for which they were otherwise qualified; and requiring lenders and Wall Street loan packagers keep “skin in the game” when selling off loans to investors. Those reforms will help prevent another race to the bottom in mortgage underwriting standards that had a devastating impact on homeowners, investors, and the entire economy.
- ***International Coordination.*** We are working closely with our international counterparts to ensure implementation of high, consistent standards – particularly for new capital rules, previously unregulated derivatives, and a coordinated response for cross-border resolution of large, interconnected firms. Separately, we have also reached agreement on the critical elements of a new “Basel III” agreement to raise amounts and quality of capital. Global consistency is essential if we are to have fair competition and avoid a race to the bottom either in regulatory standards or in company practices.

A Dedicated Watchdog for Consumers. Before the crisis, there was no single watchdog agency committed to ensuring that consumers have the financial information they need to make the

financial choices that are best for them. Dodd-Frank creates the Consumer Financial Protection Bureau (CFPB), whose mission is to promote transparency and consumer choice, and to prevent abusive and deceptive financial practices. CFPB is already hard at work in several key areas.

- ***Consolidation of Regulator Authority.*** As of July 21 2011, CFPB will consolidate the authority of seven other agencies and have clear accountability for policing abuses in consumer financial products like credit cards and mortgages and for making sure people have the information they need to make the decisions that are best for them. On that date, the CFPB will become the dedicated cop on the beat protecting American consumers.
- ***Mortgage Disclosures – “Know Before You Owe.”*** CFPB has launched an effort to simplify the forms that consumers receive when they shop for a mortgage. This simplification project aims to provide consumers with upfront, easy-to-understand information that helps them compare different mortgage offers and find the one that’s best for them. It also aims to reduce the regulatory burden by giving mortgage originators a clearer, less complicated form with which to work.
- ***Leveling the Playing Field.*** CFPB has taken initial steps required to protect Americans against abuses by certain parts of the financial industry that we were unable to monitor before the passage of Wall Street Reform. In addition to strengthening consumer protection, CFPB will level the playing field between banks and non-banks like pay day lenders and debt collectors. For too long, the uneven regulatory burdens between banks and nonbanks have distorted the competition for customers’ business, often placing banks and credit unions at a substantial disadvantage. When the CFPB is able to supervise both banks and nonbanks for compliance with consumer financial protection laws, those differences should subside.
- ***Servicemembers.*** Under the leadership of Holly Petraeus, a longtime advocate for military families and a member of a multi-generational military family herself, CFPB has worked hard to get an early start on helping servicemembers navigate the unique circumstances that affect their finances. Under Holly Petraeus’ leadership, the CFPB has entered into an agreement with the Judge Advocate Generals of all the armed services regarding the protection of servicemembers from financial abuse.
- ***Credit Cards.*** CFPB is pushing credit card providers to simplify their forms in order to make sure consumers can better understand the cost of credit. Credit cards are the most commonly used form of consumer credit. Almost two out of three families now have at least one credit card, and almost half of all families carry a balance. Millions of borrowers use credit cards to pay for medical expenses, to cover educational costs, to tide them over during a period of unemployment, to cover emergency expenses, or simply to make it to the end of the month. The CFPB is making clarity in this area a top priority.

Bringing the Derivatives Market Out of the Darkness and Into the Light of Day. Before the crisis, the over-the-counter (OTC) derivatives market operated largely in the shadows, without effective oversight or transparency. Firms took on huge risks that they – along with other investors and financial regulators – didn't fully understand or recognize, putting the health of the entire financial system in jeopardy. Dodd-Frank brings the derivatives market out of the darkness and into the light of day through the following reforms:

- ***Centralized Clearing, Trading on Open Exchanges.*** Centralized clearing and exchange trading of standardized swaps will reduce counterparty credit risk in the system while increasing transparency and market efficiencies.
- ***Strong Oversight of Derivatives.*** The largest, most active participants in the OTC derivatives market will be subject to regulatory oversight for the first time. Major dealers and participants, central clearing houses, exchanges, swap execution facilities and trade data repositories will be regulated by the CFTC or SEC.
- ***Trade Reporting.*** Reporting of all swap transactions will provide much needed information for regulators and market participants, bringing light to this previously opaque market.
- ***Capital and Margin Requirements.*** Capital and margin requirements will help reduce risk in this market, while preserving the ability of nonfinancial end-users, such as airlines and manufacturers, to manage business risk without the burden of additional costs to their bottom line.

New Tools for Winding Down Failing Firms Without Putting the Economy in Jeopardy.

Before the crisis, the government did not have the tools it needed to efficiently and effectively wind down a large, interconnected financial company on the verge of failure – such as AIG or Lehman Brothers. The lack of these tools dramatically accelerated the financial panic in the fall of 2008 and deepened the terrible economic damage caused by the crisis. The Dodd-Frank Act provides regulators the authority to wind down the most complex financial companies without putting taxpayers on the hook for losses and minimizing the impact on the broader economy.

- ***Wound Down and Broken Apart, Not Bailed Out.*** Any financial company that is placed into receivership under the Dodd-Frank Act's orderly resolution authority will be liquidated or sold; management and directors responsible for the failed condition of the firm will be removed; and creditors and share-holders – not taxpayers – will bear the losses. The FDIC continues to adopt rules to implement the orderly liquidation authority that would enable it to orderly wind down large firms that are failing.

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