



# The Trans Atlantic Financial Services Agenda

## ECMI EVENT

Mark Sobel  
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**Remarks by Deputy Assistant Secretary Mark Sobel**

**at the Center for European Policy Studies, Brussels, Belgium**

### **Transatlantic Cooperation on Financial Regulatory Reform**

*As Prepared for Delivery*

#### **Introduction**

Let me thank the Center for European Policy Studies (CEPS) and Karel Lanoo for inviting me to discuss Trans-Atlantic cooperation on financial regulatory reform. From the start, CEPS has been a leader in promoting US/EU collaboration on financial regulatory reform, and I thank them for bringing attention to this important cause.

Today, I want to emphasize three key points.

First, the United States is implementing a bold program of financial repair and regulatory reform.

Second, good progress on regulatory reform is being made at the global level under the auspices of the G-20 Leaders, and the U.S. and EU are working closely and cooperatively together.

Third, the U.S. and EU, in working together to promote a sound global system, have different traditions and legal foundations, which give rise to some differences in our approaches. Our challenge is to work through these differences, ensuring that we reach similarly robust solutions anchored in the global system and maintaining the benefits of open financial systems.

#### **Financial Repair and Regulatory Reform in the United States**

The United States has taken aggressive policy action to promote economic recovery and restructure our financial system. At the beginning of the Obama Administration, Secretary Geithner launched the Financial Stability Plan, including our bold

and transparent "stress tests" aimed at identifying the capital needs of financial institutions. Since then, banks have raised more than \$150 billion in high-quality capital and they are also writing down bad loans. Based on recent IMF data, US banks have written down over three-fourths of the IMF's forecasted write-downs through the remainder of this year. We are winding down our crisis-related programs as quickly as possible: more than 70% of the TARP program's equity injections have been repaid and the Capital Purchase Program, under which the bulk of support was provided, is now closed. The cost of stabilizing the financial system through our TARP program will be dramatically lower than previously expected, less than one percent of U.S. GDP. In no way, however, should we minimize the ongoing challenges we face in repairing our financial system, and addressing the broader costs to the economy of the crisis, and in particular the human toll, including persisting high unemployment and lost savings. In the United States, we are moving forward, consistent with the proposals set forth in Treasury's White Paper on Financial Regulatory Reform. The House of Representatives has already passed legislation addressing these issues and the Senate is now taking up this issue. These reforms will provide greater protection for consumers, better address micro and macro-prudential supervision, confront excessive risk-taking, reduce moral hazard, and take on the problem of financial firms that are perceived as "too big to fail" (TBTF).

On macro-prudential supervision, a subject of great interest on this continent as Europe moves to create the European Systemic Risk Board, the United States will create a Financial Services Oversight Council to monitor emerging risks and coordinate policy responses. Like you, we have found that the risks to the system can come from all corners of the financial markets and from the interconnectedness of our financial institutions.

There is no silver bullet to tackling TBTF. Instead, doing so requires a comprehensive set of reforms in three areas.

- First, we must act to constrain risk-taking by major firms by raising prudential standards. Importantly, we must strengthen capital, liquidity, and other prudential standards; increase disclosure, transparency and market discipline, including through more granular disclosures and increased use of stress testing; and prevent individual firms from taking on too large a share of risk in the financial system and engaging in higher-risk activities unrelated to customer business.
  - Second, we must build stronger shock absorbers across financial markets and infrastructure to lessen the spread of shocks. Critical to this endeavor is comprehensive regulation of OTC derivatives markets. We have also acted to extend the perimeter of regulation to create a strong regime for credit rating oversight, impose risk retention requirements for the securitization markets, and require registration of advisers to hedge funds and other private pools of capital above a de minimus threshold.
  - Third, we must put in place tools and authority to manage the failure of a major firm without exposing taxpayers to losses. This entails implementing an enhanced prompt correction framework and a robust resolution authority to unwind and break up a major failing financial firm in a manner that replaces culpable management, forces losses on shareholders and ensures that the financial industry, not taxpayers, will shoulder the costs in the event that a large financial company should falter.
- On consumer financial protection, the United States is aiming to create one independent agency with the clear mission to

prevent abusive and deceptive practices and to promote transparency and consumer choice. The agency will write rules of the road for the entire consumer financial marketplace and ensure they are enforced consistently. With a dedicated agency setting ground rules and looking out for ordinary people in our financial system, we will empower consumers with clear and concise information when they're making financial decisions. So instead of competing to offer confusing products, companies will compete by offering better products. And that will mean more choices for consumers, more opportunities for businesses, and more stability in our financial system.

### **International Cooperation to Promote Regulatory Reform**

While we have a robust domestic reform agenda, I want to emphasize that the United States is committed to pursuing financial reform on a multilateral, as well as domestic, basis. Indeed, we have been leaders in advancing the international agenda through our work in the Financial Stability Board and the G-20. Our domestic proposals are closely aligned with the international agenda, and contrary to reports suggesting that the international agenda is languishing, good progress is being made. Last weekend, Secretary Geithner underscored the critical imperative that the Pittsburgh commitments be implemented in full and in a timely manner. Let me review the progress that is being made in a few of the key areas in the Pittsburgh Summit Declaration.

The Pittsburgh Summit called for developing by end-2010 internationally-agreed upon rules to improve both the quantity and quality of bank capital, to strengthen liquidity risk standards and to discourage excessive leverage. As you know, the Basel Committee on Banking Supervision put forward a consultative document in December 2009 that addresses these issues, solicited comments, and is now undertaking a quantitative impact study and preparing for a calibration exercise that will take place later this year. In addition, the Basel Committee announced higher risk weights for the trading book and securitized products in July 2009. It will be important to understand the cumulative impact of these and other proposals, and the calibration exercise will certainly examine this issue. We appreciate the complexity of this exercise, but we must finish the job. Critically, it is fundamental to recognize that the crisis showed that the system was undercapitalized and, as Secretary Geithner has emphasized, that strengthened capital requirements are the core reform for making the system more resilient. The United States remains committed to moving forward with the implementation of the Basel II capital accord on a comprehensive basis. Ten of our largest financial firms, accounting for over half of total banking system assets, will be on their parallel run period by mid-2010 which would put them on a schedule to implement Basel II around mid-2011.

On OTC derivatives, the G-20 has agreed that all OTC derivative contracts should be reported to trade repositories; that all standardized contracts should be cleared through central counterparties and traded on exchanges or electronic platforms, where appropriate; and that non-cleared, customized contracts should be subject to higher capital charges.

Furthermore, as we work to strengthen our respective financial systems, we must also continue our work together in multilateral and bilateral fora to build a strong global framework, based on common rules and consistent implementation, to oversee OTC derivatives markets in a way that mitigates the risk of regulatory arbitrage and provides for a level playing field.

Resolution authority is a challenging endeavor at the national level, let alone on a cross-border basis. In the United States,

in addition to our legislation putting forward an orderly resolution authority for systemically important non-bank financial firms, we back international proposals to require major firms to prepare and regularly update credible plans for their rapid resolution in the event of severe financial stress. The Basel Committee's recent recommendations on cross-border bank resolution, drawn from a working group chaired by one of our country's top regulators, focus on enhancing prompt corrective action and national resolution powers and frameworks and promoting effective cross-border information sharing. Our prompt corrective action could serve as an important model, which we have discussed with our counterparts around the world.

As you know, there has been substantial discussion about financial risk and responsibility fees lately, following in the footsteps of U.S. proposals to develop an ex post fee on large complex firms' liabilities to recoup the financial cost to taxpayers of this crisis. We think it important that such fees observe three principles they should (1) to the fullest extent possible be internationally consistent to mitigate arbitrage opportunities; (2) ensure that tax payers do not bear the costs of financial crisis interventions; and (3) force our largest financial firms to internalize the costs that their excessive risk taking can impose on our financial systems.

Accounting issues are another prominent part of the regulatory reform landscape. The Pittsburgh Summit was extremely clear and concise it called on the IASB and FASB to redouble their efforts to achieve a single set of high quality, global accounting standards within the context of their independent standard setting process, and complete their convergence project by June-2011. It also called on the IASB to further enhance the involvement of stakeholders.

There are undoubtedly different views internationally regarding the roles that investor transparency and financial stability should play in accounting standards, especially with respect to fair value accounting treatment for certain types of financial instruments. The challenges facing the FASB and IASB are considerable.

Still, important progress has been made. Last November, the FASB and IASB reconfirmed the commitment to achieving convergence and pledged to meet together monthly to complete each major project by mid-2011. In February of this year, the SEC which since 2009 already has allowed foreign firms to list publicly using IFRS in the United States reaffirmed its support for a single, globally-accepted set of accounting standards and described the milestones that need to occur before mid-2011 in order to allow U.S. companies to report under IFRS in the coming years. And earlier this year, Commissioner McCreevy signed a letter enabling the Monitoring Board of the IASB to begin exercising greater accountability over the IASB, enhancing the its legitimacy. Again, much difficult work lies ahead in achieving accounting convergence and in doing so, it will be critical to respect the independence of the standard-setting process. There are other areas of G-20 cooperation on financial sector reform, to be sure. But the discussion of these major areas demonstrates the simple reality that there is a huge and ambitious international agenda on financial sector reform; the international community is working flat out to implement it in standard-setting bodies, the FSB, and the G-20; and the US and EU are at the heart of these groupings and our cooperation is strong. This cooperation bodes well for our ability to reach out to other global players to ensure that our financial regulatory agenda promotes cooperation, raises standards and improves financial stability around the world.

### **Addressing Differences in US/EU Approaches**

The United States and European Union have been discussing financial market issues for many years in the U.S.-EU Financial Market Regulatory Dialogue. We have found that when translating high level principles and standards into action, given diverse legal and historical approaches, differences can emerge which need to be managed. So, the challenge we face is how to ensure that robust global standards are put in place, while respecting national differences and maintaining the benefits of open, flexible financial markets. We have done so on a number of high visibility items, including Sarbanes-Oxley, the Financial Conglomerates Directive, and, as I mentioned previously, the mutual recognition of US GAAP in the EU and IFRS in the U.S.. But, while these high profile issues are important ones that garner lots of attention, it is the day to-day cooperation and communication between our regulators and policy experts that is the bread and butter of ensuring strong, compatible rules and policy solutions across the Trans-Atlantic space. We have almost constant interaction on policy issues, regulation, and supervision that in a less obvious way creates common approaches and mindsets toward the governance and supervision of the financial sector.

With the significant reform agenda we face today, this cooperation both high profile and mundane is even more essential.

For example, on Credit Rating Agencies, our supervisors are working extremely closely as we both seek to enhance regulation and supervision. The SEC is working closely with CESR as CESR moves to implement the EU's recent Regulation on Credit Rating Agencies.

On OTC Derivatives, as I've mentioned, we have worked closely together both at the top level with CFTC Chairman Gensler's visits and in numerous staff level exchanges. And, we are both developing approaches that closely mirror each other.

There remain challenges to work through. Recently, there has been much attention to hedge funds, or alternative investment fund managers. Let there be no doubt. The United States and EU fully agree that AIFMs must be subjected to a tough and rigorous oversight regime and we are both putting such regimes in place. However, we must ensure that more rigorous oversight goes along with adherence to the principles of non-discrimination and a level playing field. We look forward to continuing to work with our EU colleagues to ensure that this is the case in this and other areas.

### **Conclusion**

As I look back on not just the last two years of crisis response but the last eight years of increasing cooperation with my European colleagues on financial regulation, I am proud of the framework of cooperation that we have created. Frictions are understandable. Differences of opinion are to be expected. But, with hard work at all levels, we have instilled habits of cooperation that have helped us to not only deal with the immediate impact of one of the most severe financial crises in the last half century, but to make substantial progress towards putting in place a more robust system of regulation and supervision that will help us avoid future crises. U.S. and EU cooperation sets a bar high for global standards, and lays a strong foundation for broader, global collaboration and cooperation in financial regulation.

### About ECMI – The European Capital Markets Institute

ECMI is an independent non-profit organization created to provide a forum in which market participants, policy-makers and academics alike can exchange ideas and opinions concerning the efficiency, stability, liquidity, integrity, fairness and competitiveness of European capital markets and discuss the latest market trends.

These exchanges are fuelled by the publications ECMI regularly produces for its members: quarterly newsletters, annual reports, a statistical package, regular commentary and research papers, as well as occasional workshops and conferences. ECMI also advises European regulators on policy related matters, acts as a focal point for interaction between academic research, market sentiment and the policy-making process, and promotes a multidisciplinary and multidimensional approach to the subject.

ECMI is managed and staffed by the Centre for European Policy Studies (CEPS) in Brussels. Its membership is composed of private firms, regulatory authorities and university institutes.



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### About CEPS – The Centre for European Policy Studies

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