



MARKETS IN MOTION

developments that matter in financial markets

Financial Regulatory Reforms in the US

"The crisis that has led to so much economic carnage in the lives of middle class Americans was caused by the long-standing failure of our regulatory structure to adapt to our changing financial system and prevent the sort of dangerous risk-taking that led us here."

Senator Chris Dodd, Chairman, Senate Banking Committee, US


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Introduction

The recent global financial and economic crisis has clearly demonstrated the need for meaningful financial regulatory reforms that protect the integrity of the financial system. The near-collapse of the world financial system in 2008 and the trillions of dollars in losses generated by US financial institutions led to demand for changes in the regulatory system.

The US government bailouts of some of the biggest financial companies in the US, including Bear Stearns, Fannie Mae, Freddie Mac, and the American International Group, only accentuated the pressure for reforms.

US President Barack Obama first proposed a new regulatory structure for the country's financial system in June 2009. On March 15, 2010, Senator Christopher J Dodd, Chairman of the Banking Committee, introduced a bill on financial regulatory reforms.

The proposed bill aims to end government bailouts for failing financial institutions and such institutions will be shut down without threatening the stability of the US economy. It will create an advance warning system in the economy. It will ensure that all financial practices are exposed to transparency. It will protect consumers from unsafe financial products, such as the subprime mortgages that led to the financial crisis.

Highlights of the New Bill

Consumer Protection Authority: The bill creates a new, independent Consumer Financial Protection Agency with the authority to protect American consumers from unfair trade practices.

Advance Warning System: The bill creates a systemic-risk regime that would rein in the size and scope of too-big-to-fail institutions so that they never again have the ability to nearly topple the economic system.

An End to Too-Big-to-Fail Bailouts: The bill creates a safe way to liquidate failed financial firms. It will impose tough new capital and leverage requirements that make it undesirable to get too big

Federal Bank Supervision: The bill streamlines bank supervision with clear lines of responsibility, reducing arbitrage, and improving consistency and accountability. For the first time, there will be clear lines of responsibility among bank regulators.

Executive Compensation and Corporate Governance: The bill provides shareholders with a say on pay and corporate affairs with a non-binding vote on executive compensation.

Investor Protection: The bill provides tough new rules for transparency and accountability for credit rating agencies to protect investors and businesses.

Regulations on the Books: The bill strengthens oversight and empowers regulators to aggressively pursue financial fraud, conflicts of interest and manipulation of the system that benefit special interests at the expense of American families and businesses.

Conclusion

The bill would bring regulation for the first time to a portion of the over-the-counter market for derivatives. It would create a process for dealing with troubles at very large financial institutions that might pose a risk to the financial system and the economy, and require large firms to contribute to a fund to help with an orderly dissolution of those institutions if they are in danger of failing. And the bill includes a number of other provisions to address executive compensation and regulation of hedge funds.

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