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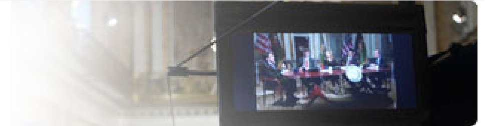

Remarks by Treasury Secretary Jacob J. Lew at a Better Markets Event on the Fifth Anniversary of the Dodd-Frank Act

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As prepared for delivery

Good afternoon. Thank you, Dennis, for that kind introduction and for organizing this event. It is a pleasure to be here with all of you today to mark the fifth anniversary of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

It is a particular honor to join Senator Chris Dodd and Congressman Barney Frank, the two central architects of the law we gather here to celebrate. Their tireless efforts, along with those of the President and members from both sides of the aisle, led to the passage of the most far-reaching and comprehensive financial reforms since the Great Depression. On behalf of everyone here, I want to thank them for their leadership, their vision, and their unrelenting determination.

Today, as we mark this anniversary, I want to reflect on the progress we have made over the past five years. And I'd like to begin by putting Wall Street Reform in the context of the crisis and of what I see as the key ingredients for a healthy relationship between the economy and the financial system.

When President Obama took office our country was in the depths of the worst financial crisis of our lifetimes. During its darkest moments, our economy was contracting at the fastest rate in 50 years. Companies were shedding more than 800,000 jobs a month. Unemployment topped 10 percent. The American automobile industry nearly collapsed. And millions of families lost their homes and their savings.

The recession started with a financial crisis, but the loss of confidence in our financial system spiraled into a broad economic crisis — one that hurt families and businesses on Main Street as well as Wall Street. Though financial stability can at times seem like an abstract concept, the crisis demonstrated that excess risk within the financial system can have a real impact on the lives of all Americans. When people discuss wholesale roll back of Wall Street reform, it is important that we remember those that suffered through the worst recession of our lifetimes: the boarded-up store fronts, the surge of foreclosure signs, the lost retirement savings, and all those Americans who lost their jobs. Make no mistake: an unstable financial system harms us all.

Stability is a critical ingredient of a functioning financial system. But we also need a financial system that promotes sustainable, long-term economic growth, maintains transparent and deep capital markets, and extends credit to creditworthy homeowners, consumers, and small businesses.

To that end, the Wall Street Reform set out to transform the way the financial system operates so that it is more stable, more transparent, and more focused on serving customers. Five years later, with nearly all of the major rules written, the economy is growing, banks are lending, and there is no doubt that Wall Street Reform is working.

FINANCIAL STABILITY

First, our financial system is safer, stronger, and more resilient. Before this law was enacted, many financial institutions were undercapitalized, over-leveraged, and focused on reaping short-term profits. The incentives were to take too much risk, and it turned out that a significant portion of the risk was borne by customers, creditors, and taxpayers. To realign our system, Wall Street Reform required banks to manage their businesses more prudently, and to maintain sufficient buffers so they can bear the costs of their own failure. During the financial crisis, this burden was borne by others — through private losses and public action. Going forward, financial reform made clear that this had to change.

One of the most significant enhancements is the requirement that banks hold more capital in their businesses. The additional capital serves as a shock absorber allowing banks to better weather economic downturns. Too often we hear capital characterized incorrectly as money banks "hold back" and pile up on the sidelines — that more capital leads to less lending. But the opposite is true: A bank with insufficient capital is a bank that cannot lend. Over the last six years, bank shareholders have added another $600 billion of capital, which is 600 billion more dollars that will be available to absorb unexpected losses.

During the crisis, the largest, most complex financial institutions often held the least capital, and their distress threatened the stability of other firms. To address the danger posed by these institutions, Wall Street Reform created a tiered and tailored regulatory framework that

applies differently to the largest, most complex firms. While the regulation of all of the nation's nearly seven thousand banks was improved by Wall Street Reform, only the 31 largest firms, those with more than $50 billion in assets, are subject to "enhanced prudential standards." These heightened requirements include capital and liquidity rules, living wills, and stress tests, tests designed to ensure that our largest financial institutions can weather severe storms and continue lending to support the economy.

Wall Street Reform also recognized that risks to financial stability are not confined to traditional banks. In 2008, no government entity was accountable for looking across the broader financial system and over the horizon to ask tough questions and monitor emerging threats. For example, there was inadequate regulation of large interconnected nonbank financial firms, such as AIG and Lehman Brothers, and no accountability to identify and respond to the risky practices that ballooned across the financial system. When several of these nonbank companies experienced financial distress in the lead-up to the financial crisis, they shook the stability of the financial system and damaged the economy more broadly.

To address these gaps in our regulatory framework, Wall Street Reform created the Financial Stability Oversight Council, also known as the FSOC. The FSOC brings together federal and state regulators to monitor the entire financial system and identify and respond to threats to financial stability. The FSOC's approach has been data driven and deliberative and has resulted in greater scrutiny of potential risks posed by institutions and a range of activities across the financial system. Since its creation, the FSOC has made actionable recommendations to enhance financial stability and designated eight financial market utilities and four nonbank financial companies for additional oversight to help address the risks they could pose.

Through the work of the FSOC and the work of agencies like the Securities and Exchange Commission, reform has also addressed risks in the money market fund industry. During the crisis, some funds were susceptible to runs; new protections were needed. The SEC is working to put in place additional reforms for these important financial products.

To keep taxpayers from ever having to step in to save a financial firm again, Wall Street Reform ended "too big to fail" as a matter of law. Regulators also have modern, commonsense tools to protect taxpayers: in the event of a crisis or failure, regulators can seize large financial institutions and wind them down in an orderly way. And since we know that financial crises do not respect national borders, we are finalizing a new international standard on total loss absorbing capacity (TLAC) for global banks at the G-20 this year, and we have supported changes to financial contracts that will help prevent fire sales and contagion at home and abroad in the event of future failures.

ENHANCING TRANSPARENCY IN FINANCIAL MARKETS

But ensuring stability and preventing excessive risk taking is not enough. Functioning markets require transparency and the free flow of information to ensure both safety and fairness. That is why Wall Street Reform tackled the vast derivatives market, which, in 2008, was notionally valued at more than $600 trillion. Prior to reform, derivatives were traded privately between two parties, leaving market participants and policy makers unable to see or understand the market as a whole. The result was a massive web of invisible interconnections. During the crisis, losses and potential losses from derivatives led to panic across the market. Many market participants were highly leveraged, and had to sell their positions, exacerbating the shock. Today, thanks to Wall Street Reform, derivatives are subject to a comprehensive regulatory framework, and many are centrally cleared and traded on exchanges or transparent platforms.

Transparency requirements are at work in other aspects of Wall Street Reform as well. For example, the law now requires that hedge fund advisers register with, and report data to the SEC. Furthermore, the law seeks to improve corporate governance by increasing transparency around compensation practices. And, Wall Street Reform created the Office of Financial Research, which informs the public by delivering high-quality financial data, standards, and analysis. This office is also leading the development of international data standards and the implementation of a global legal entity identifier, which will make financial data easier to use and understand. But as the system changes, we must continue to look out for new risks and continue to monitor new dynamics and ensure that markets remain transparent and participants have access to clear and accurate information.

SERVING CUSTOMERS AND CONSUMERS

Safer banks and more transparent markets are essential, but they are a means to an end: a financial system that supports a growing economy through responsible lending to businesses and consumers. Before Wall Street Reform, many financial institutions had lost sight of this purpose. Reform encourages banks to take a long-term view in their investing decisions, and to halt business strategies built around extracting unfair and sometimes hidden fees from mortgage borrowers or making short-term bets in securities markets.

One of the cornerstones of Wall Street Reform is the Volcker Rule, the major components of which go into effect tomorrow. The Volcker Rule prohibits risky proprietary trading, like the London Whale transactions, while protecting the depth, liquidity, and stability of our capital markets, and ultimately safeguarding taxpayers. It allows banks to provide core services to its customers, protecting core financial activities such as market-making, underwriting, risk-mitigating hedging, and trading in certain government securities.

Wall Street Reform did not just set out to repair capital markets; it also sought to make sure banks are invested in the success of the loans they originate. Another cornerstone of reform, therefore, is the requirement that a lender — before extending a mortgage loan — make a reasonable, good faith determination that the borrower has the ability to repay the loan. This approach was too rare in the years leading up to the financial crisis. For example, many lenders during the housing bubble loaded mortgages with points and fees to get their compensation up front before selling the loan to a third party. Excessive points and fees encouraged lenders to "steer" borrowers into expensive products even when they qualified for lower-cost options. These abusive lending practices and unclear underwriting standards

resulted in risky mortgages that hurt consumers and ultimately threatened financial stability. Wall Street Reform eliminated these predatory practices and extended protections to all home buyers while maintaining access to credit for borrowers under terms they can understand and afford. And so that more qualified borrowers have access to safe and affordable mortgages, we have been working with the Federal Housing Administration (FHA) and the Federal Housing Finance Agency (FHFA) as they seek to address frictions in the housing market and provide clarity to lenders on issues like put-back risk. We must also strengthen our resolve to pursue comprehensive reform of the housing finance system.

Reform has also brought greater fairness to credit markets by improving information. Consumers now benefit from new mortgage disclosure forms, which are shorter and less complex and make borrowing for a home simpler and more understandable. Similar reforms have been adopted or are being developed for student loans, auto loans, and payday loans. The effect of these reforms is that lenders must now focus on extending credit on fair terms and in good faith. They must out-compete other lenders by offering better terms, not by finding a way to sell consumers products that they don't really need and can't really afford.

The independent Consumer Financial Protection Bureau, the first regulator solely dedicated to defending Americans from financial fraud and deception, is focused on formulating and enforcing these rules of the road. Through these rules, the CFPB has established consumer protections that are preventing the kinds of predatory behavior that contributed to the financial crisis. The Bureau is making the financial marketplace work better for all Americans. It is transforming mortgages so they are clear and safe for customers, it is putting a stop to discrimination in auto lending, and it is tackling abusive payday lending practices that trap some of the poorest Americans in debt. In addition, because of the CFPB, we have put debt collectors under federal supervision for the first time and are reining in unscrupulous lenders who prey on the elderly.

Before Wall Street Reform, victims of financial fraud rarely saw their money returned to them. Now, with the help of the CFPB's enforcement division, money is flowing back to people's pockets. That includes military families targeted by predatory lending schemes, consumers bilked by dishonest marketing tactics, and homeowners hit by deceptive mortgage servicing practices. All told, in the last five years alone, the Bureau has secured more than $10 billion in relief for more than 17 million consumers harmed by illegal practices in the financial marketplace.

MAINTAINING VIGILANCE

One of the greatest strengths of the American financial system is one generation after another of innovative financiers. The goal of reform is not to quench the desire or ability to innovate, but to make sure that the oversight of our financial system keeps up with the pace of transformation. The work of reform is ongoing; it is constant, and we must be unyielding in our pursuit of it. The progress we have made must be renewed with each Administration, with each Congress, with each generation, if we are to avoid another financial crisis like the one we experienced in 2008. We cannot afford to take a break from this pursuit.

In the past, policy makers have been tempted, especially when the economy is doing well and when an emergency seems improbable, to roll back regulations, weaken reforms, and reduce oversight. We are seeing this kind of movement now on Wall Street and on Capitol Hill. For example, we are hearing calls to water down new rules out of concern they are adversely affecting liquidity in some markets. We all share an interest in properly functioning markets, and we need to make certain that we do not return to the pre-crisis way of doing things. As we learned in 2008, broker-dealers with too little capital cannot provide liquidity when it is needed most. Worse still, the painful process of broker-dealer deleveraging further cripples markets and spreads contagion across the system.

It is a mark of progress that we now have to remind ourselves of the lessons we learned. But it would be a grave mistake to think that banks can self-regulate, that forces that produce excessive risk-taking are a thing of the past, and that risks taken on Wall Street will not harm Main Street.

Instead of slowing down our work, we must sustain and build on the progress we have made.

In the next five years, we must build on these accomplishments. We must focus on improving the financial system for the users of financial services, not just for its providers. We must continue our efforts to expand access to credit and bring private capital back into the housing market by completing comprehensive housing finance reform. We must work together with Congress to strengthen reform and enhance the ability of community banks and other financial institutions to continue to serve Main Street. As regulators continue to implement new rules, they must use the flexibility provided by Wall Street Reform to make sure that smaller, less complex institutions are regulated differently from larger, more complex firms. But calibrating reforms for smaller banks is not the same as erasing important laws that place a higher level of review on the largest thirty or forty largest banks in the country.

We simply cannot afford to take the risk to our financial system of making changes to this law that would weaken consumer, investor, or taxpayer protections, or impede the ability of regulators to carry out their missions. We must fund our regulators so that they can keep pace with changing markets. Wall Street Reform increased the scope of the CFTC's responsibilities, but they need a stable source of funding to conduct their work. Congress should bring their budget in line with their regulatory peers and allow the agency to fund its operations using fees assessed on the primary beneficiaries of their oversight.

We must also protect the ability of the FSOC to ask the hard questions and to identify potential risks to the financial system, wherever those risks reside. The FSOC is critical to understanding how new developments change the landscape of the financial system. Today, our financial system is growing more through the assets of hedge funds, pension funds, and mutual funds than it is through the assets of

large, complex financial institutions. This evolution in our financial system means that we must consider a different kind of risk and be open to different kinds of policy responses, and we need to always be looking ahead and asking “what are the risks of the future?” to make sure our financial system is safe. And we must finalize important rules, like the ones that raise standards on analysts who provide retirement and investment advice, and the ones that fix compensation practices to align incentives between executives and shareholders, creditors, taxpayers, and customers.

We have seen attempts to roll back key safeguards by slipping complex provisions into unrelated bills. This tactic of using riders on must-pass legislation to chip away at crucial financial reforms is unacceptable. And let me be clear: this Administration will strongly oppose these efforts. Faced with bills that threaten to turn the clock back to 2008 and leave the American people vulnerable to another crippling crisis, I will recommend the President veto them.

In closing, I want to point out that in the aftermath of the 2008 crisis, we saw proof of what we have always known — the American people are resilient and determined, capable and creative, fiercely independent and profoundly generous. Rather than be disheartened, Americans took the actions needed to emerge from economic catastrophe. They paid down their debts, got an education, and expanded their skills. They chose to save up for new homes, start new families, and secure their retirement. They chose to create new businesses and new industries. And they chose to rebuild our nation on a new foundation and lead the world once again. Around the world the ability of the U.S. economy, the American people, and our political process, to bounce back is once again admired and serves as an ideal to which others aspire.

The purpose of Wall Street Reform is to make sure our financial system is worthy of America’s people. That is why, five years ago, we worked hard to make Wall Street Reform the law of the land, and that is why, today, tomorrow, and far into the future, we will work hard to keep this law strong, both in statute and in practice.

Thank you.

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