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Written Testimony before the Senate Banking Committee
"Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act"
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Chairman Dodd, Ranking Member Shelby, and members of the Committee, thank you for the opportunity to testify about the progress Treasury has made in implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act).

Introduction

Two months ago, against tough odds, Congress enacted the strongest set of financial reforms since those that followed the Great Depression. The Dodd-Frank Act will ultimately reshape our financial system and will affect us all in a number of important ways.

The Act builds a stronger financial system by addressing major gaps and weaknesses in regulation that helped cause the financial crisis that led to the recession. It puts in place buffers and safeguards to reduce the chance that another generation will have to go through a crisis of similar magnitude. It protects taxpayers from bailouts. It brings fairness and transparency to consumers of financial services. And it lays the foundation for a financial system that is pro-investment and pro-growth.

Mr. Chairman, passing this bill was no easy task. It would not have happened without your strong commitment and that of your colleagues to make sure that meaningful reform became a reality.

You stood on the right side of history and with the millions of Americans who have lost their jobs, homes and businesses as a result of a crisis caused by basic failures in our financial system.

But the work is far from done. Enacting financial reform was just the beginning.

Guiding Principles

Implementing the Dodd-Frank Act is a complex undertaking. Effectively describing the process requires terms that are often unavoidably dense, making reform seem distant to many. So before outlining the steps we have taken to date, I want to detail the broad principles guiding our efforts.

First, we are moving as quickly and as carefully as we can.

Wherever possible, we are quickly providing clarity to the public and the markets. But the task we face cannot be achieved overnight. We have to write new rules in some of the most complex areas of finance; consolidate authority spread across multiple agencies; set up new institutions for consumer protection and for addressing systemic risks; and negotiate with countries around the world. In getting this done, we are making sure to get it right.

Second, we are bringing full transparency to this process.

As we write new rules, we will be consulting a broad range of groups and individuals. And as we seek their input, the American people will be able to see who is at the table. Draft rules will be published. Everyone will be able to comment. And those comments will be publicly available.

Third, wherever possible, we will streamline and simplify government regulation.

Over the years, our financial system has accumulated layers upon layers of rules, which can be overwhelming. That is why alongside our efforts to strengthen and improve protections through the system, we will avoid duplication and seek to eliminate rules that do not work.

Fourth, we will create a more coordinated regulatory process.

Ahead of this crisis, gaps and inconsistencies between regulators proved to be a major failure. Gaps allowed risks to grow unattended and inconsistencies allowed an overall race to the bottom. Better coordination will help prevent a recurrence.

Fifth, we will build a level playing field.

A level playing field must exist not just between banks and non-banks here in the United States, but also between major financial institutions globally. We are setting high standards at home while working tirelessly to persuade the international community to follow our lead. We welcome the agreement just reached in Basel. It substantially raises the level of capital major banks must hold whether they operate out of New York or London or Frankfurt.

Sixth, we will protect the freedom for innovation that is absolutely necessary for growth.

Our system allowed too much room for abuse and excessive risk. But as we put in place rules to correct for those mistakes, we have to achieve a careful balance and safeguard the freedom for competition and innovation that are essential for growth.

Seventh, we are keeping Congress fully informed of our progress on a regular basis.

Implementation Update

Treasury has been working hard to implement the sweeping reforms of the Dodd-Frank Act since enactment.

Immediately after passage, we put in place a governance structure that oversees Treasury's role to implement financial reform. The bulk of the work is being done by teams dedicated to our core responsibilities such as helping to establish the Financial Stability Oversight Council (Council); laying the groundwork for the Office of Financial Research (OFR); launching the Consumer Financial Protection Bureau (CFPB); and creating a Federal Insurance Office (FIO).

These teams provide an update to a steering committee of senior Treasury officials who meet every day and consider options, make decisions, push implementation forward, and, where appropriate, make recommendations for the Secretary

Let me now discuss in greater detail our actions around each of our core responsibilities.

The Financial Stability Oversight Council

With respect to the Council, we are focused on three things: approach, structure and execution.

First, the Council has a clear statutory mandate and overarching responsibility to identify risks to financial stability, respond to any emerging threats in the system and promote market discipline. This is a mandate that previously did not exist. In the lead-up to this crisis, the regulatory framework focused regulators narrowly on individual institutions and markets, which allowed gaps to grow and inconsistencies to emerge that allowed arbitrage and weakened standards. Before the Dodd-Frank Act, no single institution had responsibility for monitoring and addressing risks to financial stability. The Act fixes that through the creation of the Council.

To carry out its mandate, the Council has been given an important role in several consequential regulatory decisions. These include which major nonbank financial and critical financial market utilities firms will be subject to heightened supervision, and what prudential standards should be applied to those firms. The Council will also closely monitor the financial system as a whole, looking out for any emerging threats and, where they exist, make recommendations on how to address them.

As Chair, Treasury respects the critical independence of regulators to fulfill their responsibilities. We must develop an approach that maintains that independence while maximizing the coordination required for the Council to achieve its mission of financial stability. The Dodd-Frank Act makes agencies collectively accountable for this mission. While each agency has authority and mandate for a specific part of the financial sector or for certain aspects of its functioning, we need to develop an approach for the Council and its members of collective accountability for financial stability. This approach will promote the coordination, cooperation, and information sharing necessary for success.

Our second focus is on structure.

Tomorrow, the Council will have its first meeting. In advance of that meeting, senior officials from each member agency have been looking at how best to set up the Council's governance structure. They have drafted bylaws, and I expect those will be considered tomorrow.

Member agencies have also discussed setting up a committee structure to promote shared responsibility and make the best use of each member's expertise. This plan would entail forming committees around the Council's various statutory responsibilities, and around core issues that relate closely to systemic risk where more than one agency has a significant interest.

For example, we have proposed committees for designating certain nonbank financial firms and financial market utilities, for drafting recommendations for heightened prudential standards, and for monitoring and reporting on threats to financial stability. The Council members and their deputies would set the priorities for each of the committees, which will draw upon the expertise of each member agency and be chaired by one or more members.

Our third focus is on execution.

While we settle on structure, the Council has already begun its work because its duties commenced immediately upon enactment. Member agencies have already formed staff working groups to begin taking action. And, thanks to significant, joint work by staff of the member agencies, we expect that the Council will be in a position to take important steps toward fulfilling several of its core responsibilities at its meeting tomorrow.

At that meeting, in addition to adopting organizational documents, I expect the Council to consider a resolution to seek public comment on the criteria for designating nonbank financial companies for heightened supervision.

I also expect the Council will consider tomorrow a resolution to seek public comment to inform recommendations the Council will make on how to implement statutory restrictions on banking institutions' proprietary trading and investments in private funds (the "Volcker Rule"). In addition to that study, the Council must also study and make recommendations for implementing the concentration limit; study the macroeconomic effects of risk retention requirements; and study the economic implications of financial regulation. Work on those reports is also underway.

The Office of Financial Research

In drafting the Dodd-Frank Act, Congress recognized that better information and analysis will be critical to the success of the Council and its member agencies. In the lead-up to this crisis, financial reporting failed to adapt to an ever evolving financial system. Both supervisors and market participants lacked data about the buildup of leverage in the rapidly growing shadow banking system. Policymakers and investors responded to the crisis with inadequate information about the interconnectedness of firms and associated risks. That is why the Dodd-Frank Act created the Office of Financial Research.

As the statute requires, the OFR will have a Data Center to set standards for financial reporting and improve the quality of data that supervisors and market participants rely to manage risk.

These standards will make it easier to spot emerging threats. For example, more consistent and complete reporting of derivatives will make it easier to track how they redistribute risk through the system. Data standards will also improve market discipline as individual firms will be better able to assess their own risks, and standardization may lower firms' costs over the long run.

In addition to standards, the Data Center is required to develop and publish key reference data that identify and describe financial contracts and institutions. Regulators and supervisors as well as private firms and investors rely on such reference data to analyze risk. Gaps and inconsistencies in existing reference sources inhibit meaningful analysis. The OFR will seek to close gaps and increase consistency to improve risk analysis and strengthen market discipline.

To help the Council fulfill its role, the Dodd-Frank Act mandates that the OFR have a Research and Analysis Center. Although no analytic effort, no matter how thoughtful, can anticipate all risks, the OFR can help identify undue concentrations of risk such as took place at AIG before the crisis. And the OFR can help ensure that when the next crisis begins to emerge the government has the information and analytical tools it needs to respond appropriately.

The OFR will be headed by a director nominated by the President and confirmed by the Senate. The director will have an independent obligation to report to Congress on threats to the financial system. We envision a director who combines the capacity to lead a cutting edge research program with experience both in managing data systems and in risk analysis.

Until there is a confirmed Director, the Treasury staff team working on creating the OFR has been hard at work planning its functions and gathering input from regulators and private parties. Our OFR team will continue to coordinate closely with other members of the Council.

We will move quickly to complete a census of existing data standardization initiatives and existing sources of reference data. The OFR will work to maximize the effectiveness of existing private sector efforts.

The OFR must not duplicate existing government data collection efforts or impose unnecessary burden. That is why we are working with the regulators to catalogue carefully the data they already collect to ensure the OFR relies on their data whenever possible, as the Act requires. The OFR will help government get the most out of existing data by facilitating sharing among agencies. We are also identifying existing private data sources to improve risk monitoring without imposing new burdensome data collection mandates.

When we have finished assessing existing public and private data initiatives, we will move quickly to draw up detailed plans for OFR to facilitate and advance these initiatives without duplication or unnecessary burden. We also are developing organizational structure, hiring procedures and pay structures, information technology, and other requirements.

Our efforts to establish the OFR will stay focused on ensuring that the OFR protects private information and trade secrets. The Act provides strict protections for data security and confidentiality and we take seriously our obligation to implement these protections fully. In the coming months our OFR team will be developing confidentiality policies and procedures for the OFR and its data centers that meet the highest data security standards.

We will in all these efforts continue to seek advice and expertise from the private sector, academia, and Congress. Working with the Council we will seek to formalize our outreach by establishing advisory committees. The lessons and information we take back will be built into the foundations of the OFR.

The Consumer Financial Protection Bureau

The CFPB will be an independent bureau of the Federal Reserve with the mission of ensuring transparency in consumer financial products and services and protecting consumers from abuse and deception. It will consolidate existing rulemaking authorities for consumer financial products and services. And it will consolidate agencies' existing functions for supervising the very largest banking institutions for compliance with consumer financial protection laws. It also will supervise many non-bank financial firms that sell consumer financial services, an entirely new federal function.

The Act charges the Secretary with standing up the CFPB. Under his leadership we set up a staff implementation team with a clear division of responsibilities right after enactment. The team has working groups focused on setting up key functions of the CFPB such as research, preparing for the supervision of financial institutions, and working with the transferor agencies. Other working groups are focused on building the CFPB's supporting infrastructure (e.g., finance and budget, records management, legal services, human resources, information technology, procurement, and other operations).

Elizabeth Warren is leading Treasury's effort to create the CFPB as the Secretary's Special Advisor. She will chair a steering committee of senior Treasury officials dedicated to overseeing CFPB implementation and reporting to the Secretary.

The team is tracking and projecting the CFPB's expenses, working with GAO to build audit requirements for FY 2011, and developing a budget model. The team is also analyzing and aligning salary structures of agencies transferring staff to the CFPB, and building a pay and compensation system that fulfills the unique requirements of the Act. Initial privacy protocols are being developed and data management systems are being built.

The Secretary has designated July 21, 2011, as the date on which the CFPB will assume existing authorities of seven agencies (OCC, OTS, FDIC, NCUA, FRB, FTC, and HUD). Six of these agencies will also transfer staff to the CFPB. We are developing protocols with these agencies for determining how many people will transfer and for determining how the agencies will jointly identify which specific employees will transfer.

We have made substantial progress preparing the CFPB to incorporate staff and assume authorities from other agencies. We have begun planning and preparations for certain rules mandated by the Dodd-Frank Act so the CFPB can meet statutory deadlines. We have met with the agencies that will transfer rulemaking authority to coordinate and ensure a smooth transfer. We are coordinating fulfillment of certain rule writing mandates under the Dodd-Frank Act with the Federal Reserve Board to speed clarity for the market and meet statutory deadlines.

We are also hard at work to ensure a smooth transfer of consumer compliance supervision for banks, thrifts, and credit unions with assets exceeding $10 billion. Senior experts in consumer compliance supervision of large banks – detailed to Treasury from the banking agencies – are laying plans for staffing, training, and information systems. We will make sure to coordinate examination schedules with prudential regulators to avoid unnecessary burden.

Federal Insurance Office

FIO will provide the federal government for the first time dedicated expertise regarding the insurance industry. The Office will monitor the insurance industry, including identifying gaps or issues in the regulation of insurance that could contribute to a systemic crisis in the insurance industry or the United States financial system. The director of FIO will advise the Council on these matters as a nonvoting member. FIO may receive and collect data and information on and from the insurance industry and insurers; enter into information-sharing agreements; analyze and disseminate data and information; and issue reports.

Under the Act, the director of this office must be a senior career civil servant, and we are committed to finding a top caliber person to fill the job. Last week we posted a vacancy notice and we will move as fast as the civil service hiring process allows. Meanwhile, existing Treasury staff has started the work of FIO.

We will make every effort to ensure a cooperative and collaborative relationship with the National Association of Insurance Commissioners (NAIC). Senior Treasury officials and staff are engaging frequently with the NAIC as well as other interested parties. We are establishing with NAIC a framework within which FIO and the States, as the functional regulators, can work hand-in-hand.

And we are also making plans for a system that will provide FIO with industry and insurer data and information, including data to monitor access to affordable insurance products by traditionally underserved communities and consumers, minorities, and low- and moderate-income people.

We are working to engage effectively with representatives of other countries on insurance prudential issues. We will also be working closely with the United States Trade Representative.

Conclusion

This economic crisis was caused by fundamental failures in our financial system. And over the past few years, those failures have cost us dearly – millions of lost jobs, trillions in lost savings, thousands of failed businesses, homes foreclosed, retirements delayed, educations deferred.

Financial reform addresses those failures so no future generation has to pay such a price. But it also rebuilds our financial system so that it can once again be an engine for economic growth.

For much of the last century our financial system was the envy of the world. From London to Shanghai, it was analyzed and even emulated for its creativity and efficiency in finding innovative ways to channel savings towards credit and capital, not just for the biggest companies but also for the individual entrepreneurs who had a good idea and a solid plan.

The Dodd-Frank Act will help ensure that our financial system becomes safer, stronger and, just as in the past century, the world leader.

Thank you.