

Senator Harry Reid
522 Hart Senate Office Bldg
United States Senate
Washington, DC 20510

The Honorable Chairman Dodd
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, D.C. 20510

April 19, 2010

Dear Leader Reid and Chairman Dodd,

The over 250 consumer, employee, investor, community and civil rights groups who are members of Americans for Financial Reform (AFR) write to express our strong support for the Merkley-Levin amendment (modeled after the Merkley-Levin PROP Trading Act), which will strengthen provisions related to proprietary trading and conflicts of interest in the Senate financial reform package.

First, we want to express our strong support for the Banking Committee's vote to include the Volcker Rule in the Wall Street Reform Act (S. 3217). In the run-up to the crisis, major investment and commercial banks engaged in reckless proprietary trading that in some instances led directly to their collapse or need for taxpayer bailouts. Most of those remaining are now banks, but now their risky bets are backed by federal government and the taxpayers.

We agree with President Obama that we "cannot accept a system in which hedge funds or private equity firms inside banks can place huge, risky bets that are subsidized by taxpayers and that could pose a conflict of interest. And we cannot accept a system in which shareholders make money on these operations if the bank wins but taxpayers foot the bill if the bank loses."

However, we believe that the improvements in the Merkley-Levin amendment are critical to strengthen the bill.

The Merkley-Levin amendment would:

- Prohibit Goldman-Style Bets Against Clients: The amendment would prohibit securities originators from engaging in any transaction that would give rise to a material conflict of interest or undermine the value, safety, or performance of an asset-backed security during the period the security is outstanding. While Goldman Sachs has recently been charged with fraud for such a conflict of interest, there is evidence that the practice of creating toxic securities, selling them to clients and then betting against them was widespread on Wall Street. It should be banned outright.
- Remove the Study Requirement and Regulatory Deference: The financial reform bill would only allow regulations banning proprietary trading to be developed after a study by the Financial Stability Oversight Council and based on their recommendations. By taking this approach, rather than providing statutory restrictions, any newly-imposed regulations would be subject to the whims of Administrative politics—both in the years before they go into effect, and in the years to come. The Merkley-Levin amendment makes the prohibitions statutory, and provides for a study on how best to implement them.

- Close Loopholes in the Definition of Proprietary Trading: The bill takes a narrower approach to the definition of proprietary trading, exempting many types of trading including involving "market making activities" or "hedging activities," without defining those terms. The client-centered, market-making portfolios are where many firms are actually making many of their proprietary trades. The Merkley-Levin amendment will provide a broader definition, covering trading involving any purchase or sale of a security, or transaction involving a derivative (including swaps), as a principal, for a firm's own account. The amendment would permit federal regulators to carve out specific market making or hedging activities.
- Impose Higher Capital Standards and Position Limits on Non-bank Financial Companies: Both the Merkley-Levin amendment and the bill would impose additional capital requirements and limits on systemically important non-bank financial companies. The amendment makes it explicit, however, that additional capital is required for high-risk assets and trading strategies.

For the above reasons, Americans for Financial Reform strongly endorses this amendment. If you have any questions, please contact Heather McGhee, Washington Office Director of Demos, at hmcghee@demos.org or (202) 559-1543.

Sincerely,

A New Way Forward
 AFL-CIO
 Americans for Financial Reform
 Bold Nebraska
 California Reinvestment Coalition
 Campaign for America's Future
 Center for Media and Democracy
 Consumer Watchdog
 Consumers Union
 Demos
 International Brotherhood of Teamsters
 Jobs with Justice
 National People's Action
 Neighborhood Economic Development Advocacy Project (NEDAP-NY)
 Public Citizen
 Service Employees International Union (SEIU)
 U.S. Public Interest Research Group (PIRG)
 Union Plus