Federal Financial Analytics, Inc.

PETROU PARSES PRACTICAL PROBLEMS IN TBTF REFORM

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Washington, DC - Karen Petrou, managing partner of Federal Financial Analytics, today delivered the attached remarks on the Brown-Vitter bill that seeks to end TBTF banking. The talk is based on the firm's analysis of the legislation, which is also attached for your convenience. Both are on the record.

"I think it's critical to get past the 'says-you' aspect of this too-big-to-fail debate," Petrou said. "We can throw opposing data around all day, but would the Brown-Vitter bill work as planned? Or, does it have practical problems and perverse consequences that must be reasonably addressed before a meaningful policy debate on the rest of the bill advances? I think the measure has some major stumbling blocks that, if not removed before action advances, could make banking more risky, not less so," she continued.

In the talk delivered this morning before the Lawyers' Council of the Financial Services Roundtable, Petrou highlights several serious flaws:

- The single-minded focus only on very high levels of equity capital assumes all risks in banks are credit risks. They are not and setting one requirement this high means far

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less resources to protect against operational and liquidity risk – proven systemic hazards as past crises vividly attest.

- The bill for some reason only covers bank holding companies and a limited class of S&L holding companies, carefully carving out huge firms that own insured depositories. Why? Does this just encourage huge, unregulated entities with all the privileges of the behemoth banks that are the bill's target?

- At the same time many non-bank companies that own banks are exempted from the bill's sanctions, some non-banking activities in bank holding companies are put under the new high leverage capital standards designed for banks. This dramatically alters broker-dealer and similar business models, in part because it adds new risk to these business lines.

- The restrictions on transactions between banks and non-banks designed to protect the federal safety net also apply only to some owners of insured depositories. Why? Also, the bill doesn't take account of the high-risk activities now allowed directly in banks. Wouldn't these restrictions create strong incentives for parent companies to shovel as much risk as they can into an insured depository?

- Many of these unintended effects can be addressed, Petrou says. But, she goes on to note that they need to be carefully considered before any of these proposals advance. "It doesn't matter if Brown-Vitter lives or dies," Petrou concluded. "Much in the bill is under active consideration by regulatory agencies and could be accomplished without new law. It's thus vital to think these seemingly-technical issues through now

and do so very, very carefully."

Federal Financial Analytics, Inc. has provided objective advice on financial-industry policy and strategic issues since 1985. Clients include large financial-services firms, regulators, investors in this sector and others whose names may be found on the firm's website. The firm does not lobby for clients.

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