Levin Senate floor statement on the 'swaps push out' provision

Wednesday, December 10, 2014

WASHINGTON – Sen. Carl Levin, D-Mich., chairman of the Senate Permanent Subcommittee on Investigations, entered the following statement into the Congressional Record today:

Mr. President, 14 years ago, Congress made a grave mistake. In the dead of night, as part of the Consolidated Appropriations Act of 2001, Congress passed a little-noticed provision that prohibited all meaningful oversight and regulation of swaps, which then were the latest financial product in the fast-growing financial derivatives market. In that new regulatory void, the swaps markets grew to unprecedented size and complexity. And it was the swaps market that ultimately lead to unprecedented taxpayer bailouts of some of the largest financial institutions in the world.

Some have estimated that the cost of the last crisis was $17 trillion—with a “t”. To the families across the country, it meant lost jobs, home foreclosures and reduced home values for those who didn’t lose their homes. Far too many of my constituents, far too many Americans, are still struggling to recover. And it was all enabled by Congress passing a financial regulatory provision with little consideration, tucked inside a funding bill.

We enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act, in part, to address the significant risks posed by swaps and other financial derivatives. Section 716 was a key component of the financial reforms. That provision is titled “Prohibition Against Federal Government Bailouts of Swaps Entities.” It explicitly prohibited taxpayer bailouts of banks that trade swaps. And it set out a plan to help achieve that goal, by requiring bank holding companies to move much of their derivatives trading outside of their FDIC-insured banks.

This provision has come to be known as the “swaps push out” provision. Four years after its enactment, however, banking regulators have yet to finalize a rule to enforce compliance. And, before they do, some in Congress want to relieve them of the obligation altogether.

Some of the largest bank holding companies prefer to conduct their swaps trades in their government-backed, FDIC-insured banks because they have better credit ratings, which means lower borrowing costs and therefore higher profits. But, because the activity is within the bank, it puts the federal government—and taxpayers—directly on the hook for those bets that, as we saw in the financial crisis, can be unlimited in number, because banks can create an unlimited number of “synthetic” derivatives related to a particular financial asset.

A couple years ago, JPMorgan Chase lost billions of dollars on a bad bet in the credit derivatives markets. The Permanent Subcommittee on Investigations, which I chair, conducted an extensive investigation and issued a 300-page bipartisan report with its findings. JPMorgan’s risky trading by its bank was a disaster—costing the bank over $6 billion. And it was receiving the taxpayer subsidy the whole time.

To be clear, Section 716 does not cure all the risks posed by swaps. But it was an important part of the effort to protect us from another crisis. Along with the creation of the Consumer Financial Protection Bureau and the Merkley-Levin provisions on proprietary trading and conflicts of interest, these reforms form the backbone of the Dodd-Frank Act’s safeguards.

By repealing this provision, we would ignore the lessons of the last financial crisis and weaken Dodd-Frank’s protections against the next crisis.

American families and businesses deserve better than this. If there are provisions in the Dodd-Frank Act that need to be improved or reformed, the appropriate Senate committees should review, evaluate, and modify them. And they should be given time on the Senate floor for further review and improvement. The proponents of this legislation should explain why they think that deregulating swaps—before we ever started re-regulating them—is the right course of action. They should explain why taxpayers should run the risk of bailing out risky swaps trades gone bad. They should explain why, despite the loss of millions of jobs and trillions of dollars the last time Congress de-regulated derivatives, this time will be different. A legislative vehicle is the right place for considering these issues, not an urgent appropriations bill.

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