

**The Group of 30 Report Initial Selection of Press Coverage January 15, 2009**

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**CNBC video of the press conference**

**<http://www.cnbc.com/id/15840232?video=999674801>**

Financial regulation

## How to fix finance

Jan 15th 2009 | NEW YORK  
From Economist.com

***An influential group makes some provocative proposals for re-regulating global finance***



WITH the fires still raging, scorching industry after industry, it might seem premature to ask what should rise from the ashes. But policymakers are understandably keen to start work on redesigning their financial systems. If 2008 was the year when the flaws in the old model became painfully clear, 2009 is likely to be the one when governments embrace re-regulation in an effort to fix it. A weighty report published on Thursday January 15th is sure to play a crucial role in shaping the agenda.

The Group of Thirty's "Financial Reform: A Framework for Financial Stability" is important both because of the concreteness of its 18 recommendations and because of who was involved. The authors were led by Paul Volcker, a former head of the Federal Reserve who, as an economic adviser to Barack Obama, has the president-elect's ear. Other members of the G30 include Tim Geithner, Mr Obama's nominee for treasury secretary, Larry Summers, another economic adviser, and Jean-Claude Trichet, president of the European Central Bank. Although they recused themselves from direct participation, they are understood to support the bulk of the findings. "Everyone stands behind the report in spirit. No one disowned it," says an insider.

And muscular stuff it is. Under the proposals, banks that are deemed systemically important would face restrictions—in the form of "strict" capital requirements—on high-risk proprietary activities, that is bets made using their own money. While this would not quite mean a return in America to the separation of commercial banking and investment banking that ended with the repeal of the Glass-Steagall act in 1999, it would strongly encourage the investment-banking arms of universal banks to focus on client businesses, such as merger advice, rather than trading. One reason for separating these functions is that they seem to be "unmanageable in financial conglomerates", says Mr Volcker.

The report also calls for raising the level at which banks are considered to be well-capitalised. This should be expressed as a broad range, it says, with the expectation that banks will operate at the upper end when markets are frothy.

The recommendations concerning non-bank financial institutions—the so-called “shadow” banking system that has contributed so much of the pain—are no less radical. One proposal is sure to make the hair stand up on hedge-fund managers' necks: pools of private capital that live on borrowed money should have to register with a regulator and produce regular reports, disclosing things such as leverage and performance. The biggest of them would even be subject to capital and liquidity standards. The report even recommends bank-like regulation for money-market funds that give assurances about maintaining a stable net-asset value, as most presently do. And it calls for legislation in America to set up a mechanism for dealing with non-bank failures, the lack of which has caused no end of regulatory consternation. For banks and non-banks alike, the report calls for a more refined analysis of liquidity in stressed markets and more robust contingency-planning.

Central banks should have a stronger role in policing such things, the authors argue, and need to be especially vigilant in good times, when credit is expanding quickly. They should also be more involved in supervising bank safety and soundness—although, to safeguard central-bank integrity, the role of chief firefighter is best played by others once trouble ignites. Central bankers “need to be more concerned about financial stability, but less involved in crises,” says Tommaso Padoa-Schioppa, one of the G30.

Of the other areas covered by the report, three are particularly eye-catching. It advocates a formal system of regulation for over-the-counter derivatives, such as the type of credit swaps that sank American International Group, an insurer. It urges regulators to force banks to hold on to a significant portion of credit risk when they package loans into securities and sell them on, in order to curb reckless underwriting of mortgages and other debt. And it calls for a rethink of certain accounting principles that may exacerbate downturns through pro-cyclicality, including the practice of marking assets to the current market value; “more realistic guidelines” are needed for illiquid instruments and distressed markets. It also wants to see more flexibility in guidelines for loan-loss reserves. Some regulators take a dim view of banks that squirrel away extra reserves in good times, on the grounds that this constitutes earnings manipulation, even though it leaves them better prepared to ride out the bad times.

The other important message is that a global crisis requires a global fix. International co-ordination should go beyond rule-making to closer harmonisation, including enforcement, say the authors, and more needs to be done to curb the uneven application of international rules at national level—although they shed little light on how this could be achieved.

It is quite a package. At the press conference to unveil the document Mr Volcker was typically modest, insisting it was more an agenda for discussion than a hard-and-fast blueprint. But, given his closeness to Mr Obama, it is hardly far-fetched to imagine much of it becoming official policy. All that talk of the biggest overhaul of financial regulation since the 1930s just took a step towards reality.

## **Bloomberg**

### **Group Led by Volcker Urges More Oversight of Banks**

By Alison Fitzgerald

Jan. 15 (Bloomberg) -- A group led by Paul Volcker, an adviser to President-elect Barack Obama, called for a regulatory crackdown that would curtail risk-taking by systemically important financial institutions and limit their share of deposits.

The panel of former central bankers, finance ministers and academics known as the Group of Thirty advised that regulators impose capital limits on proprietary trading and bar large banks from running hedge funds and private-equity firms that mix their own and their clients' money. In a report released today, the group also urged governments worldwide to tighten supervision of insurance companies, investment banks and large broker-dealers.

The recommendations come as U.S. lawmakers and the incoming Obama administration consider ways to overhaul regulation after major financial institutions reported almost \$1 trillion in losses and writedowns stemming from the credit crisis.

Volcker, former chairman of the Federal Reserve, said at a press conference in New York that he'll make the recommendations to Obama, adding that the report is "a reasonable indication of the direction in which we might go." He was named by Obama to lead a panel of advisers on how to pull the U.S. out of the recession.

The financial system has "failed the test of the marketplace," said Volcker, 81, chairman of the Trustees of the G-30. He endorsed the recommendations as an individual and not as a representative of the incoming Obama administration, the statement said.

Volcker characterized the banking system using "a four- letter word: It's a mess."

#### **Advisory Board**

Volcker is set to be chairman of the President's Economic Recovery Advisory Board after Obama takes office Jan. 20.

"The worst Wall Street financial crisis has gone global, and not a regulator worth his salt will back down from tightening up the regulatory regime," Chris Rupkey, chief financial economist at Bank of Tokyo-Mitsubishi UFJ Ltd. in New York, said before the report was released. "Volcker has Obama's ear and there is no doubt that the U.S. will be on the same page as most of these G-30 recommendations for greater financial- services regulation."

#### **Distinctions**

Volcker's report calls for clear distinctions between institutions, such as former investment banks, that deal mainly in capital markets, and commercial banks that take deposits and make loans.

"We are making a distinction between what appears to be institutions that are becoming larger and doing banking business," Volcker said at a news conference in New York today. "They should give their loyalty to their clients and customers. Those functions should not be carried out in the context of an institution that is carrying out very risky capital market activities."

He said the report seems to speak directly to news this week that Citigroup will sell off many of its businesses and that Bank of America Corp. has asked the government for an additional capital infusion to help it complete the purchase of Merrill Lynch.

“It’s been proven that they’re unmanageable, the existing conglomerates,” he said.

### **Not Glass-Steagall**

Volcker said the recommendation fall short of a revival of the Glass-Steagall law that separated insurance, commercial banking and investment banking.

The 18 sets of guidelines call for greater transparency, stricter corporate-governance standards and tougher oversight of financial firms whose failure could bring down the financial system.

The goal is to “restore strong, competitive, innovative financial markets to support global economic growth without once again risking a breakdown in market functioning so severe as to put the world economies at risk,” Volcker said in the statement.

The group recommends that money-market mutual funds that offer banking services reorganize as special-purpose banks and submit to supervision. It also calls for government oversight and capital requirements for hedge funds and private-equity firms that are deemed “too big to fail.”

The report’s co-chairs were former Italian Finance Minister Tommaso Padoa-Schioppa, and Arminio Fraga, former president of the Central Bank of Brazil. The three principals said not all members of the group, which includes Bank of England Governor Mervyn King, TIAA CREF Chief Executive Roger Ferguson, and Bank of Israel Governor Stanley Fischer, agreed with the report.

### **Reining in Risk**

The goal of the recommendations is to create a system that would avoid a repeat of the current financial meltdown by reining in risk and boosting oversight. The report is entitled “Financial Reform: A Framework for Financial Stability.”

“There were major failures in risk management to a point that is mind boggling,” Fraga-Neto said today.

The group recommends that money market mutual funds that offer traditional banking services reorganize as special-purpose banks and submit to supervision and that a systemic-risk regulator oversee and impose capital requirements on hedge funds and private equity firms that are deemed “too big to fail.”

“It’s quite clear that hedge funds can be big enough, and volatile enough to be systemically important,” Volcker said.

### **Credit Ratings**

Regulators should also recommend a different payment model for credit ratings that would avoid the conflicts of interest inherent in the current system, in which major rating firms, such as Moody’s and Standard & Poor’s, are paid by the firms issuing debt, the group said. Companies that use credit ratings should seek independent opinions.

Some of the group’s recommendations, including the one regarding rating companies, jibe with proposals that Obama put forth during his campaign.

Obama has pledged to replace the government-sponsored mortgage finance giants Fannie Mae and Freddie Mac “with a structure that is engaged in helping people buy homes, not engaging in market speculation.” The companies were placed into government receivership in September. Volcker’s group recommends against “hybrids with private ownership and government sponsorship.”

Obama said he’ll streamline overlapping regulatory agencies, and that he wants any company borrowing from the federal government to be subject to regulation. He’s also looking to strengthen capital requirements on mortgage securities and derivatives, and require financial institutions to better disclose to investors and companies with whom they do business the kinds of assets they hold.

The G-30 report recommends countries “reevaluate their regulatory structures with a view to eliminating unnecessary overlaps and gaps in coverage and complexity” and it also calls for transparency in credit default swaps, and structured and securitized products.

## **G30 says financial system badly needs repair**

By Pedro Nicolaci da Costa

NEW YORK, Jan 15 (Reuters) - The G30, a group of high-profile economists and policy-makers, on Thursday called for changes in international financial regulation to help avoid future meltdowns, but its recommendations were vague and non-binding.

In findings that made no reference to the issue of executive compensation, the group of bankers and policy-makers indicated that big firms that pose a risk to the entire system should be subject to particularly close scrutiny.

The global economy has been reeling from a financial crisis that began with a popping U.S. housing bubble and has since infected the entire financial system, shaking confidence and breeding mistrust.

The G30 report said countries should avoid having multiple regulators working at cross-purposes, a complaint that has been widely made of the U.S. supervisory system.

Taking aim at the process of securitization, the report suggests that financial firms should not be allowed to repackage opaque debt instruments and sell them without holding any exposure.

"Participation in packaging and sale of collective debt instruments should require the retention of a meaningful part of the credit risk," the report said, making a recommendation that is not new.

Paul Volcker, a former Federal Reserve Chairman and currently an informal adviser to President-elect Barack Obama, chairs the G30's steering committee, and was charged with delivering the findings on Thursday.

One novel recommendation was that money market funds stop acting too much like banks, and offer only "conservative" investment options without a government guarantee.

### **HEDGING BETS**

Despite the fraud scandal surrounding hedge fund manager Bernard Madoff, who is accused of having stolen billions of dollars in a high-finance pyramid scheme, the G30 stopped short of calling for regulation of hedge funds but did not rule it out either.

It suggested regulators should have the authority to establish "appropriate standards for capital, liquidity and risk management" for "private pools of capital" that are large enough to threaten the entire system.

"There are compelling grounds for the regulations of hedge funds," the report said.

The G30 findings also appeared to take a swipe at the widely criticized model of government sponsored enterprises in the U.S. mortgage sector.

"Hybrids of private ownership with government sponsorship should be avoided," the group said.

The report urged rating agencies to change the way they receive compensation. At the moment, the agencies are paid by the firms whom they are rating.

But again the G30 aimed low: "Regulators should encourage the development of payment models that improve the alignment of incentives."

In an apparent swipe at the Federal Reserve, which has indicated a willingness to lend against risky assets such as real estate bonds, the G30 indicated such loans should be avoided.

"Central bank liquidity support operations should be limited to forms that do not entail lending against or the outright purchase of high-risk assets," the group said.

While executive compensation, which many believe is at the crux of the crisis, was not directly addressed, Volcker did say he believe pay structures were a problem.

"Compensation packages contributed to an excess of risk taking on Wall Street," Volcker told reporters.



## **G30 dice sistema financiero está roto y necesita ser reparado**

Por Pedro Nicolaci da Costa

Reuters - Noticias Latinoamericanas

Spanish

NUEVA YORK, ene 15 (Reuters) - El Grupo de los 30 pidió el jueves cambios en la regulación financiera internacional para ayudar a evitar futuras turbulencias, pero sus recomendaciones fueron algo vagas y no son vinculantes.

En conclusiones que no hicieron referencia al tema de los salarios de los ejecutivos, el grupo de banqueros y de funcionarios indicó que las grandes firmas que suponen riesgos para todo el sistema deberían estar sujetas a un control mayor.

La economía global está sufriendo las consecuencias de una crisis financiera que comenzó con la explosión de la burbuja inmobiliaria estadounidense y que posteriormente contagió a todo el sistema.

El reporte del G30 dijo que los países deberían evitar tener múltiples reguladores trabajando con propósitos cruzados, una queja que suele hacerse sobre el sistema regulador estadounidense.

Sobre el complejo proceso de securitización, el informe sugiere que no debería permitirse que las firmas financieras reempaqueten instrumentos de deuda poco transparentes y luego los vendan sin tener ninguna exposición.

"La participación en el empaquetamiento y la venta de instrumentos de deuda colectiva debería requerir la atención de una parte significativa del riesgo crediticio", señaló el informe.

Paul Volcker, un ex presidente de la Reserva Federal y actual asesor del presidente electo estadounidense Barack Obama, preside el comité del G30 responsable de fijar las políticas y estuvo a cargo el jueves de presentar las conclusiones del informe.

## **Volcker/G30: Biggest Complex Banks Need Partic Close Regltn**

15 January 2009

- Non-Governmental Group Proposes Framework for Fin. Sys. Fix
- Sees Compelling Grounds for Hedge Fund Regulation
- GSEs Shouldnt Intervene in Mortgage Market
- GSE Portfolio Activities Should Be Spun Off to Private Entities

By Claudia Hirsch

NEW YORK, Jan 15 (MNI) - A newly proposed framework for reform of the global financial system released Thursday called for the elimination of gaps in regulation, more coordination among international supervisors and enhanced surveillance of the biggest core financial institutions.

Paul Volcker, chairman of the trustees of the Group of Thirty, a non-governmental group of public and private representatives that assembled the report over the past six months, said during a press conference that the framework can provide an "agenda" for a "sorely needed" debate on overhauling the regulatory and supervisory backbone of the financial system.

The "Framework for Financial Stability" report provides 18 sets of recommendations aimed at tightening industry oversight, especially of the largest bank organizations that essentially "run" the financial system, the former Federal Reserve chairman said.

"The general approach is to strengthen the oversight and stability of systemically important institutions that serve the needs of individuals, businesses and governments and that are largely responsible for maintaining the market infrastructure," said a summary of the report.

Members of the steering committee that assembled the report emphasized that it makes a distinction between these largest, most complex service institutions and market players like hedge funds and equity funds, which would receive less scrutiny by comparison. Such trading funds, however, should be subject to greater transparency. And Volcker told reporters that if a hedge fund grows "big enough, we can start worrying about capital requirements."

In its prepared statement, the G30 noted that "there are compelling grounds for the regulation of hedge funds," and also called for improved oversight of a "variety of other private pools of capital," including money market mutual funds. All such market players must boost their capital, liquidity and risk management practices and their overall transparency. If necessary, they should be subject to explicit capital requirements and liquidity restraints, the group said.

In one of the more strongly worded recommendations, the reform proposal called for the eventual end of the government-sponsored housing enterprises intervention in the mortgage market.

In any policy resolution regarding the U.S. government-sponsored housing enterprises, Fannie Mae and Freddie Mac, the report read, there should be a "clear separation of the functions of private sector mortgage finance risk intermediation from government sector guarantees or insurance of mortgage credit risk."

It continued, "Hybrids of private ownership with government sponsorship should be avoided," to which Volcker added, "This kind of institution that is a combination of private ownership" and implied government backing "inherently leads to conflicts."

At some point, the report recommended, "existing GSE mortgage purchasing and portfolio activities should be spun off to private sector entities, with the government, if it desires, maintaining a capacity to intervene in the market through a wholly owned public institution."

The report suggested consolidation of regulatory bodies, but stopped short of advising which agencies should be merged.

"We are dealing with how we think the financial system ought to look, how it ought to be regulated, but not who does the regulation in any detail," Volcker said. The G30 report also emphasized greater international coordination of financial regulatory efforts. And it proposed consideration of "nationwide limits" on deposit concentration to "guard against excessive concentration in national banking systems" that might impede oversight, management control and effective competition.

Volcker, who also serves as a special economic adviser to U.S. President-elect Obama, said a copy of the report has been sent to the administration and will likely form part of the White House discussion of a fix to the financial system. Ultimately, however, the administration will decide how it should approach a solution, Volcker added.

The full proposal can be downloaded from the G30s Web site, [www.group30.org](http://www.group30.org) [<http://www.group30.org>].

JANUARY 15, 2009

## **G30 Advises On International Financial Regulation**

By Emily Barrett  
Of DOW JONES NEWSWIRES

NEW YORK (Dow Jones)--International experts responded Thursday to the regulatory weaknesses exposed by the prolonged financial crisis with a plan to extend both the reach and the depth of financial sector oversight.

Former U.S. Federal Reserve Chairman Paul Volcker presented a hefty report from the steering committee he now heads for the Group of 30. It called for closer scrutiny of "large, systemically important banking institutions," whose distress could have a far-reaching impact on the health of the financial system.

Their oversight must meet "high and common international standards," the report said.

This recommendation is the clearest yet of the need to identify firms "too big to fail" - a need reinforced by the dramatic circumstances of Lehman Brothers' collapse and the \$85 billion bailout of insurance giant American International Group. AIG Vice Chairman Jacob Frenkel, who also heads the Group of 30, said Thursday that "we believe that policymakers must adopt changes that improve prudential regulation and supervision."

The report also recommended bringing regulatory powers to bear on previously untouched areas of the financial community - it sees "compelling grounds" for regulation of hedge funds.

The G30 wants firms to take more responsibility for the performance of their products, by keeping on their books "a meaningful part of the credit risk." That could rile the securitization industry, which thrived in recent years by repackaging debt - including some risky mortgage deals - into so-called collateralized debt obligations, many slices of which have since become worthless.

Special measures for safeguarding markets also featured in the report - specifically the privately negotiated trades in derivatives. The G30 ventured further than most, advocating "legislation to establish a formal system of regulation" for these markets, currently valued at around \$350 trillion worldwide.

These were the standouts among the 18 sets of recommendations in "Financial Reform - A Framework for Financial Stability." The project was launched in July last year by the G30, a nonprofit group comprising senior representatives of the public and private sectors and academia worldwide. It comes ahead of the Jan. 20 inauguration of U.S. President-elect Barack Obama, who has pledged a "21st century regulatory framework" for the country. How the new administration will use these recommendations is unclear, but the report will be presented formally to the Group of 20 industrial and developing nations in April.

The report didn't discuss the potential for further emergency action in a crisis that has stretched the mandate of central banks around the world. The Fed has drawn criticism for lending billions of dollars to financial institutions, under terms less exacting than some - including Volcker - deem appropriate.

Such actions, along with programs to buy securities backed by mortgages and other forms of consumer debt, helped push the Fed's balance sheet to a record \$2.3 trillion as of the year end.

In a clause particularly relevant to the Fed, the report recommended that central bank emergency lending be kept in future for "highly unusual and exigent circumstances," requiring political authorization. Moreover, it rejected lending against or buying high-risk assets, or other forms of long-term capital support by the central bank, saying such measures are more appropriately taken by "directly accountable government entities."

The report made no recommendations on how to proceed in the current crisis, noting only that "difficult questions of weaning markets and financial institutions from official life support are sure to arise."

The report was more explicit about the duty of central banks to preserve financial stability. In what could be a rebuke for the years of easy credit under former Fed Chairman Alan Greenspan, the report said such concerns are relevant not only in times of crisis, "but also in times of rapid credit expansion and increased use of leverage."

In line with the European Commission's efforts to curb this use of leverage, or magnified borrowing, the G30 recommended that regulators cooperate worldwide to monitor and report on firms' unfunded liabilities.

Indeed, cooperation between central banks was a key theme in the report, which also recommended they strengthen their role in prudential regulation.

### **Strong U.S. Focus**

In keeping with calls for an overhaul of the U.S.'s fragmented system of agencies and state departments, the G30 also advocated consolidation of the regulatory industry. It said countries should eliminate "unnecessary overlaps and gaps in coverage and complexity, removing the potential for regulatory arbitrage, and improving regulatory coordination." Moreover, the report said those authorities should be independent from "political and market pressures."

The federally chartered firms that are the biggest buyers of mortgages in the U.S. also received special attention in the G30 report. The future of Fannie Mae and Freddie Mac as quasipublic companies has been in doubt since their government rescue in September. The report noted that such entities should have explicit statutory backing and financial support, and "hybrids of private ownership with government ownership should be avoided."

"In time, existing GSE mortgage purchasing and portfolio activities should be spun off" to the private sector, "with the government, if it desires, maintaining a capacity to intervene in the market through a wholly owned public institution," the report said.

The report was less expansive on guidelines for risk management within principles put forward by the Counterparty Risk Management Group and the Institute of International Finance.

JANUARY 15, 2009

# Former Fed Chief Volcker: Fincl System Failed Marketplace Test

By Emily Barrett and Romy Varghese  
Of DOW JONES NEWSWIRES

NEW YORK (Dow Jones)--The financial system as it currently stands has failed the test of the marketplace, and the largest institutions in particular must accept sharper scrutiny of their practices, former Federal Reserve Chairman Paul Volcker said Thursday.

Speaking as head of the Group of 30's steering committee on the release of its recommendations for international regulatory reform, Volcker wouldn't say whether the best solution would be a return to the directives of the Glass-Steagall Act. This act, which in 1933 introduced a separation of commercial and investment banking businesses, and insisted on restrictions on information sharing to counter conflicts of interest, has suffered some erosion in the past decade.

"We are not saying these institutions can't do what was the traditional investment banking business," he said, without adding further clarity. Among the recommendations of the report is that "large, systemically important banking institutions should be restricted in undertaking proprietary activities that present particularly high risks and serious conflicts of interest."

The former central banker agreed with an audience member at the presentation that executive compensation had "contributed to excessive risk taking on Wall Street," and was "indicative of a real problem." But he wouldn't push a specific solution. "This is a consideration to be taken into account by supervisors" of the relevant institutions, he said.

The report's future as a guide to public policy is unclear, since President-elect Barack Obama's incoming administration will have its hands full preventing further meltdown in the U.S. financial system. The latest blows come from the plummeting stock prices of Bank of America (BAC) and Citigroup (C), which has announced plans to shed a third of its operations.

Volcker wouldn't comment directly on the problems currently facing U.S. banking institutions, but did point out that the latest on Citigroup reinforces the findings of the G30's report.

He said that it was "up to the Administration to decide what they want to do" with the recommendations, and they are a "contribution to the debate" over reform of the financial system.

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## **The Financial Times**

### **Congress to create systemic risk regulator**

By Krishna Guha in Washington and Aline van Duyn in New York

January 15 2009

The US Congress will legislate in coming months to create regulatory powers to combat systemic risk, with authority almost certainly awarded to the Federal Reserve, a leading member of the House of Representatives has told the Financial Times.

Barney Frank, the powerful chairman of the House financial services committee, said that “by the spring I believe we will have passed a bill which empowers a systemic risk regulator”. He added it had “almost certainly got to be the Fed”.

The regulator would be empowered to deal with currently unregulated entities such as hedge funds or private equity firms and would monitor systemic risk “not by institution but by activity”.

The remarks were made as financial experts, including Paul Volcker and Lawrence Summers, put their weight behind drastic regulatory reforms of the global financial system, including severely curbing the ability of large banks to trade or invest for their own account.

The report by the Group of Thirty (G30) also recommends that hedge funds and private equity groups become regulated, and that the status of money market funds be reviewed to reflect the risks highlighted by recent runs on such funds.

Though not any part of their role in the administration of Barack Obama, the president-elect, the report sheds light on the thinking about the regulatory future by administration heavyweights such as Mr Volcker, former chairman of the Federal Reserve, and Mr Summers, the incoming director of the White House’s National Economic Council.

Hedge funds and private equity funds in which the banks own capital together with their clients should be “prohibited”. “Large proprietary trading should be limited by strict capital and liquidity requirements,” the report said.

The private markets were for now exercising tight discipline on borrowing and risk-taking by financial firms, Mr Frank said. But he said Congress needed to put in place a systemic risk regulator “before the animal spirits of capitalism return”.

Mr Frank said that while it would be desirable to streamline the number of US financial regulators, “I do not think this needs to be tackled right away”.

Ben Bernanke, the Federal Reserve chairman, and Tim Geithner, Mr Obama’s nominee for Treasury secretary, favour giving the Fed powers to take action on the basis of a threat to the stability of the system as a whole, even if the financial institutions in question were not in breach of any specific regulations.

- Mr Obama’s pick to head the Securities and Exchange Commission told lawmakers on Thursday that the institution would need to have “a laser-like focus on fraud and investor protection”, Reuters reports.

Mary Schapiro, a veteran regulator, was greeted warmly by members of the Senate banking committee, which is expected swiftly to approve her nomination.

She raised the possibility of placing SEC examiners at credit-rating agencies and said one of the first things she would do if confirmed would be to “take the handcuffs off” the SEC’s enforcement division.

“With investor confidence shaken, it is imperative that the SEC be given the resources and the support it needs to investigate and go after those who cut corners, cheat investors and break the law,” she said.

If confirmed by the full Senate, she would take over an agency blamed for failing to help prevent the biggest financial crisis in decades and criticised for missing Bernard Madoff’s alleged \$50bn (€38bn, £34bn) fraud.

**Washington Post**

# Obama Adviser Presents Plan to Alter Global Financial System

By Anthony Faiola

Washington Post Staff Writer

Thursday, January 15, 2009

NEW YORK -- A top economic adviser to the incoming Obama administration unveiled a plan today to radically rethink the global financial system, including a host of measures that would dramatically expand government control over banking and investment in the United States.

The plan -- which recommends limiting the size of banks, setting guidelines for executive pay and regulating hedge funds -- offers the first hint of the kind of changes to the financial system President-elect Barack Obama might push for in the coming weeks and months. Obama has pledged to present a comprehensive series of changes to prevent a repeat of the current financial crisis before world leaders gather in London for a major economic summit in April.

The report today was issued by the Group of 30, an organization of international economists and policy makers. But the recommendations were immediately seen by observers as a building block to an Obama plan because the lead author is Paul Volcker, the former chairman of the Federal Reserve during the Carter and Reagan administrations who will serve as a special Obama White House adviser. Part of Volcker's role is to help mastermind what could ultimately be the biggest overhaul of the U.S. financial system in decades.

Volcker said he would press the new administration to consider the measures, "but it's up to the administration to decide what they want to do."

The proposal offers 18 major recommendations that would insert government regulators into the board rooms of financial institutions as never before. The plan recommends vastly increased oversight of major banks, going as far as to recommend the end of an era of mega banks whose size makes their failure potentially catastrophic to the global financial system. To limit their size and scope, banks, the document states, should be prohibited from managing hedge funds or private equity funds.

In addition, major mutual funds should be required to operate as commercial banks, subjecting them to stricter government oversight. Those that choose not to comply should be forced to sell only relatively safe financial instruments offering investors low risk, and, most probably, limited room for outsized profits.

The document suggests that rating agencies should also face a battery of government regulators.

"The issue posed by the present crisis is crystal clear: How can we restore strong, competitive, innovative financial markets to support global economic growth without once again risking a breakdown in market functioning so severe as to put the world economies at risk?" Volcker said in a statement. "We hope that our proposals, which explicitly relate to the weaknesses that have become evident in the financial system over the last year, will be a useful contribution to the debate about needed reforms both by private financial institutions and by public authorities."

The proposal suggests that the U.S. government should clarify the status of mortgage giants Fannie Mae and Freddie Mac, either making them into government agencies or regulating them as independent mortgage brokers.

The plan's recommendations for greater international cooperation on regulation and the creation of new laws to oversee exotic financial derivatives echo similar calls from major world leaders made during an emergency economic summit in Washington on Nov. 15. With cautious support by President Bush, plans are moving forward, for instance, to enhance international cooperation in overseeing major banks. But European leaders have eagerly awaited a signal from Obama about what his plan for creating a new set of rules for the global financial system might look like.

It remains unclear how many of the recommendations will ultimately make their way into Obama's final plan, but the proposal released today could lift the spirits of Europeans who have called for stricter government oversight on executives' pay and risk management in financial institutions -- an area where the Bush administration has offered only tepid support. The report today calls for government to enforce systematic board-level reviews for executive pay and the creation of new parameters for a firm's risk tolerance.

## Volcker: Regulate to prevent future crisis

### ***Economists' group led by ex-Fed chief says more regulation needed in the financial sector, outlining several necessary reforms***

By [David Goldman](#), CNNMoney.com staff writer

January 15, 2009: 11:00 AM ET

NEW YORK (CNNMoney.com) -- Financial markets must be made more transparent - with closer attention paid to risk management - in order to prevent another global economic collapse, according to a report released Thursday by a body of top economists led by former Federal Reserve Chairman Paul Volcker.

Volcker, the head of President-elect Barack Obama's special economic recovery advisory board, presided over the Fed from 1979 to 1987, a period of extreme financial unrest. He is known for raising interest rates to historic highs under the Carter and Reagan administrations in order to combat out-of-control inflation.

"The issue posed by the present crisis is crystal clear," said Volcker. "We [must] restore strong, competitive, innovative financial markets to support global economic growth without once again risking a breakdown in market functioning so severe as to put the world economies at risk."

The economists' group, named the Group of 30, called for tighter regulation of the financial sector, improving coordination between government and international regulators. They also suggest regulators be allowed to work independently from politics, as political and market pressures can compromise their goals.

Central banks should be strengthened, according to the report, but not just in times of crisis. It says the Fed and other central banks should promote and maintain financial stability even when the economy is at its strongest, since market participants often make their riskiest deals during those periods.

For instance, the current credit crisis stems from unscrupulous lending practices of banks and mortgage lenders during the peak of the housing boom, which passed through without stringent government regulation. Only when the housing market collapsed were the risky deals widely uncovered.

Regulators should pay particularly close attention to relatively new and largely unregulated financial instruments such as credit default swaps, collateralized debt obligations and over-the-counter derivatives, the group said. Many analysts have said that regulators have failed to keep up with the growing complexity of Wall Street investment techniques, leading to shady and mostly unnoticed dealings.

The report also said the United States should establish a regulator that deals exclusively with non-bank financial institutions and create a way of dealing with failed non-depository financial institutions. Currently the government will take over failed depository banks, guaranteeing a certain amount of deposits through a Federal Deposit Insurance Corporation's fund.

But the government needed to make up new rules to save other kinds of failing institutions, such as American International Group Inc. ([AIG](#), [Fortune 500](#)), during the credit crisis.

Furthermore, the Group of 30 said the largest and most complex financial institutions should be subject to the most regulation and forbidden from engaging in activities that pose particularly high risk to the overall market.

With the financial markets tangled like a web, the biggest banks have become the most systemically important, hence the multi-billion dollar bailouts of Bear Stearns, Citigroup ([C, Fortune 500](#)) and American International Group ([AIG, Fortune 500](#)) in the past year.

Thursday's report was a follow-up to an earlier Group of 30 study released in October. That study found that a lack of appropriate and necessary banking regulation by governments around the globe led to the current worldwide economic crisis. ■

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## Group of 30 Calls for Sweeping Reform

By Riley McDermid, Senior Reporter

A group of economists led by former central bankers and a previous chairman of the Federal Reserve on Thursday called for a sweeping overhaul of the global financial system, including increased regulatory oversight and greatly reduced risk-taking activities.

The Group of Thirty released the 18 recommendations in a report, *Financial Reform: A Framework for Financial Stability*, all of which aim to create a comprehensive restructuring of financial institutions and markets. The group is led by former Federal Reserve Chairman Paul Volcker, who served as the U.S. central head banker from 1979 to 1987 in both the Carter and Reagan administrations.

"The issue posed by the present crisis is crystal clear: How can we restore strong, competitive, innovative financial markets to support global economic growth without once again risking a breakdown in market functioning so severe as to put the world economies at risk?" said Volcker, in a statement. "We hope that our proposals, which explicitly relate to the weaknesses that have become evident in the financial system over the last year, will be a useful contribution to the debate about needed reforms both by private financial institutions and by public authorities."

Indeed, at a Thursday morning news conference, Volcker, who is also an economic adviser to president-elect Barack Obama, took square aim at risky banking practices and exorbitant salaries paid on Wall Street as helping create the current financial crisis.

"Compensation packages contributed to an excess of risk taking on Wall Street," Volcker said at the news conference. But he went on to stress that regulating financial compensation should not be the purview of regulators, but rather the responsibility of banks constantly vigilant about the "soundness" of their practices.

The group said that as part of restoring market confidence, international regulators must step up unprecedented reforms that would include imposing capital limits on proprietary trading and more closely policing private equity and hedge fund groups. The report also advises regulators to overhaul the way they oversee investment banks, insurance companies and any financial institution with "significant" systemic effects on the global financial system.

"On the prudential side [the reforms] include the regulatory treatment of the so-called parallel banking system, the role of the central bank in maintaining financial stability and the need to improve information standards and to regulate over-the-counter derivatives markets," said Arminio Fraga, the group's steering committee's vice chairman and a founding partner at Gavea Investimentos and former Governor of Banco do Brasil, in a statement.

"Given the pervasive failures in risk management in financial institutions, the report also emphasizes the role of proper governance and incentives, including the important link between risk taking and compensation systems," said Fraga. "Finally, on the crisis management side the report focuses on how far the access to lender-of-last-resort facilities should go and on the importance of having in place a proper resolution mechanism for failed financial institutions."

January 15th 2009

## **G-30 calls for far-reaching reforms**

Victoria Pennington

### **The Group of 30 outlines radical reforms it deems necessary to strengthen the global financial system**

WASHINGTON, DC - "The pervasive and deep-rooted financial crisis has amply demonstrated that our financial system is broken and it requires thorough-going repair," says Paul Volcker, chairman of the trustees of the Group of Thirty (G-30).

A report released today entitled 'Financial reform - A framework for financial stability' includes four core and 18 specific recommendations that aim to strengthen the oversight and stability of the systemically important financial institutions largely responsible for maintaining the market infrastructure. The first recommendation emphasises the need for the largest and most complex banking organisations to be subject to particularly close regulation and supervision, meeting high and common international standards. The G-30 says these institutions should be restricted in undertaking proprietary activities that present particularly high risks and serious conflicts of interest.

Much of the report concerns the governance, operations, regulation and supervision of banks but capital market participants, including hedge funds and equity funds, would also be required to meet higher standards of transparency, paying greater attention to capital, liquidity and risk management practices.

Attention is also directed to the practices of credit rating agencies, settlement and clearance arrangements for derivatives, approaches towards common international accounting standards and the treatment of fair value accounting, and the need for closer international co-operation and co-ordination. The report calls for the creation of a framework for national level consolidated prudential regulation and supervision over all large insurance companies in countries where such a structure is lacking - namely the US.

The report also proposes that an appropriate prudential regulator be designed for large investment banks and broker-dealers not organised as bank holding companies. It states there are compelling grounds for the regulation of hedge funds, and it also recommends increased supervision of money-market mutual funds and a variety of other private pools of capital.

Arminio Fraga, the G-30 steering committee's vice-chairman, founding partner at Gavea Investimentos and former governor of Banco do Brasil, says: "The report recommends a series of significant reforms. On the prudential side, they include the regulatory treatment of the so-called parallel banking system, the role of the central bank in maintaining financial stability, and the need to improve information standards and to regulate over-

the-counter derivatives markets. Given the pervasive failures in risk management in financial institutions, the report also emphasises the role of proper governance and incentives, including the important link between risk taking and compensation systems. Lastly, on the crisis management side, the report focuses on how far the access to lender-of-last-resort facilities should go, and on the importance of having in place a proper resolution mechanism for failed financial institutions."

The G-30 stresses that the recommended regulatory policies and accounting standards should guard against procyclical effects and are consistent with maintaining prudent business practices. The report also states that regulatory capital standards should be enhanced and benchmarks for bank capital raised.

A host of recommendations in the report are based on the key conclusion that financial markets and products must be made more transparent, with better-aligned risk and prudential incentives. The report adds that the infrastructure supporting such markets must be more robust and resistant to potential failures of even large financial institutions. Several sections of the report emphasise that, given the global nature of the markets, it is essential that there be consistent regulatory frameworks on an international scale, and national regulators should share information and enter into appropriate co-operative arrangements with authorities of other countries responsible for overseeing activities.

The report also proposes strengthening the role of central banks. In countries where the central bank is not the prudential regulator, the G-30 recommends central banks should have: (i) a role on the governing body of the prudential and markets regulator(s); (ii) a formal review role with respect to proposed changes in key prudential policies, especially capital and liquidity policies as well as margin arrangements; and (iii) the supervisory role in regard to the largest systemically significant firms, as well as critical payment and clearing systems.

Click here to read the full report: <http://www.group30.org/index.htm>

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**CEP NEWS** (Canada)

## **G30 Advises Tougher Regulations for Financial System**

Thu Jan 15, 2009



(CEP News) - The U.S. regulatory system is in need of an overhaul, with tougher standards and oversight over financial entities, said Former Fed Chairman Paul Volcker, speaking as head of the Group of Thirty at a press conference in New York.

The recommendations also call for more oversight of banks and hedge funds and, in particular, targets firms that present "systemic risks" to the economy. Volcker also called for rules geared at curbing unnecessary risk taking.

The recommendations come at a time when the U.S. regulatory system is being carefully examined, as a new SEC Chairperson is being interviewed by Congress and a new Treasury Secretary is being discussed on Capitol Hill.

Volcker also heads an independent advisory body, whose mission is to find ways for bringing the U.S. out of recession. The body was created by U.S. President-elect Barack Obama, who considers Volcker one of his closest advisers.

## **Banks that survive need tougher rules, economists say**

By **KEVIN G. HALL** McClatchy Newspapers

WASHINGTON -- The blossoming global financial crisis is provoking a consolidation in banking that will leave surviving institutions more powerful than ever, giving greater urgency to new and comprehensive rules and regulations, the influential Group of Thirty said Wednesday in a much-anticipated report.

Composed of some of the biggest names in economics and finance, and led by a top adviser to President-elect Barack Obama, the Group of Thirty called for tough new regulations of the finance sector in the United States and globally.

Many of its recommendations are similar to a blueprint provided last year by departing Treasury Secretary Hank Paulson, and the group carries weight because its members are the current or former presidents of important central banks and the chief executive officers of some of the biggest financial companies. They're no longer calling for self-regulation and want tough and transparent new rules. "The pervasive and deep-rooted financial crisis has amply demonstrated that our financial system is broken and it requires thoroughgoing repair," Paul A. Volcker, the chairman of the Group of Thirty's trustees, said in a statement that accompanies the detailed report.

Volcker is the larger-than-life former Federal Reserve chairman who held the post from 1979 to 1987. He crushed inflation in the early 1980s and ushered in two decades of economic prosperity. He's a close adviser to Obama and will become the chairman of a new Economic Recovery Advisory Board after next week's inauguration. Obama has promised to act swiftly on serious financial revisions, and one member of the influential Group of Thirty is his embattled pick to head the Treasury Department, Timothy Geithner. The presence of Volcker and Geithner in the Group of Thirty adds weight to its recommendations.

Before offering 18 recommended changes to the regulatory structure, the group warned that the deep global financial crisis has provoked failures and mergers that have left a "small number of exceptionally large bank holding companies" at the core of the U.S. financial system.

"These core institutions are gaining even larger dominant positions in terms of credit and capital market activities, large-scale corporate banking, nationwide deposit taking and many other segments of the corporate and retail financial business," the report says, adding that "these developments pose public policy issues, including questions of excessive concentration" that could yield monopoly-like powers.

Among the recommendations is a call to merge regulators so that there's a single one that looks at the largest, most complex banking organizations. These large institutions should be prohibited from commingling their money in private equity funds and hedge funds on the grounds that these private pools of money present high systemwide risks and conflicts of interests, the report says.

Also noteworthy, the Group of Thirty acknowledged that self-regulation of hedge funds, which are private funds for the ultra-wealthy, wasn't enough, since "volatility has been greater than anticipated" and contributed to more uncertainty in financial markets. The group calls for national regulation of private pools of capital if they employ substantial amounts of borrowed money, a process called leveraging.

Echoing a controversial call from Treasury Secretary Paulson, the Group of Thirty also called for national regulation of the insurance industry, saying that the failure of regulation allowed American International Group to capture a large share of an unregulated insurance like market called credit-default swaps. AIG was on the verge of collapse when the federal government took partial ownership of the giant insurer in September.

## ***Volcker Proposes Radical Financial Plan Thursday,***

January 15, 2009

Julie Crawshaw

Key Obama adviser Paul Volcker is the lead author of new and radical economic plan that would effectively alter the global financial structure.

The plan contains 18 major recommendations that would give regulators more power over financial institutions than they have ever had before, including creating new laws to regulate financial derivatives, limit the size of banks, set guidelines for executive pay, and regulate hedge funds.

The report — entitled "Financial Reform: A Framework for Financial Stability" — was issued by the Group of 30, which Volcker heads. Volcker was chairman of the Federal Reserve under Presidents Jimmy Carter and Ronald Reagan.

Other recommendations in the plan include requiring major mutual funds to operate as commercial banks and forcing funds that choose not to comply to sell only low-risk, and less profitable, financial products.

The plan report also advises regulating venture capital groups and rating agencies, and prohibiting banks from managing private equity or hedge funds.

"We hope that our proposals, which explicitly relate to the weaknesses that have become evident in the financial system over the last year, will be a useful contribution to the debate about needed reforms both by private financial institutions and by public authorities," Volcker said in a statement.

Volcker, whose role will be to help President-elect Barack Obama overhaul the U.S. financial system, says he will press the new administration to consider adopting the measures.

Obama has said his administration will come up with a way to prevent a repeat of the current financial crisis before April, when world leaders meet for a major economic summit.

"Volcker has Obama's ear and there is no doubt that the U.S. will be on the same page as most of these G-30 recommendations for greater financial-services regulation," Bank of Tokyo-Mitsubishi Chief Economist Chris Rupkey told Bloomberg.

"The worst Wall Street financial crisis has gone global, and not a regulator worth his salt will back down from tightening up the regulatory regime."

### Group of 30 urges national insurance regulation

By Mark A. Hofmann  
Jan. 15, 2009

WASHINGTON—A group headed by one of President-elect Barack Obama's chief economic advisers is calling for "national-level" regulation of large insurance companies.

In a report issued Thursday, the Group of 30—a nonprofit group of international financial experts—calls for greatly increased regulation of a variety of financial institutions and products, such as forbidding "large, systemically important banking institutions" from sponsoring or managing hedge funds under most circumstances.

The report, "Financial Reform: A Framework for Financial Stability," also addresses insurance specifically, recommending that "for those countries lacking such arrangements, a framework for national-level consolidated prudential regulation and supervision over large internationally active insurance companies should be established."

States are currently responsible for regulating insurance in the United States, although some insurers and producers as well as risk managers advocate the creation of a system of optional federal charters for insurers and producers that would prefer federal regulation.

Paul Volcker, a former chairman of the Federal Reserve who now serves as a special adviser to President-elect Obama, was the report's chief author. He is chairman of the Group of 30's trustees.

The complete list of the report's recommendation can be found at [www.group30.org](http://www.group30.org).

## Group of 30 unveils bank regulation plans

WASHINGTON, Jan. 15 (UPI) --

An international economists group lead by a U.S. adviser to President-elect Barack Obama unveiled Thursday a plan to extensively overhaul banking regulations.

The Group of 30 plan, with lead author former Federal Reserve Chairman Paul Volcker, recommended steps to limit the size and scope of banks, preventing them from reaching superstore status in a manner that could ripple through economic structures should one of them fail, The Washington Post reported.

In the plan, a form of which may make it to an international summit in London in April, banks would be prohibited from managing hedge funds or private equity funds, the Post said.

Large mutual funds, in turn, would be required to operate under the same regulatory oversight as banks. Rating agencies, the plan says, should be placed under strict regulatory control, the Post reported.

The issue posed by the present crisis is crystal clear: How can we restore strong, competitive, innovative financial markets to support global economic growth without once again risking a breakdown in market functioning? Volcker said in a statement.

Volcker said he would lobby for the reforms, but it's up to the administration to decide what they want to do.

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## **TAPPED** *The group blog of The American Prospect*

### **REGULATE GOOD TIMES, C'MON!**

One of the signature challenges of the current recession is its global aspect; no matter what policy changes are undertaken here in the United States, the interconnected nature of the world economy leaves conditions here in the U.S. somewhat at the mercy of decision makers in other countries. More than one observer has suggested that it is time to revisit an international economic regulatory regime ala the post-World War II Bretton Woods agreement. Which is why it is interesting that today a report on just that subject has been released by a group of top international economists. Its lead author is Paul Volcker, former Fed Chair and current Obama adviser.

The report [PDF] contains 18 recommendations focused on preventing the untenable situation we refer to as "too big to fail." That condition comes about when a financial institution makes bad business decisions but its size and reach prevent the government from allowing it to fail because of potentially devastating economic consequences. Thus, the report suggests creating unitary national regulatory authorities, limiting the size of bank holdings and executive compensation, and restricting the amount of risk that different financial institutions would be able to take on, preventing, for instance, banks from managing private equity or hedge funds, and mutual funds from acting as investment banks. It's the kind of stuff that might prevent future financial crises and help ensure the smooth working of our capitalist system, if properly implemented.

It's also the kind of thing that will make Wall Street furious. The enormous profits of the financial industry are based on taking enormous risk. Of course, when those enormous risks don't pay off, it's not the private companies that take the heat, it's the public. Businesses have a right to operate in a free market environment until their actions have a detrimental effect on everyone else, but then the government must step in. These proposed regulations are part of a general initiative -- one that will be led here in the U.S. by Congressman Barney Frank -- to limit public risk by regulating private business.

Of course, it's difficult to create effective regulatory regimes, especially on the international level. This will be a thorny problem sure to consume a good deal of time, post-stimulus, for Obama's economic team.

For further reading on this topic, let me suggest Harold Meyerson's article in our most recent issue, "A Global New Deal."

-- *Tim Fernholz*