**The Frank Dodd Act**

**Sanchez, Ray  
Panther ID #1739531  
FIN 4303  
Prof. Leonard Arvi  
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**Introduction**

In 2008, a worldwide recession took place and financial institutions began to collapse. Banks like Bear Sterns and Freddie Mac thought they were immune to market instability, but they were very wrong. These huge financial institutions begged the government to bail them out because they were “too big to fail”. The dollars of every taxpayer went to work to save these banks and make sure that thousands of people didn’t lose their jobs. The idea was that if these banks failed then it would create a snowball effect that would create world chaos.

Lenders began to lend less and savers began to pull their money out of the banks, money markets, and equities. Many were given the option to have a mortgage on a house even though they were considered a “sub-prime” candidate. They were making it possible for almost everyone to obtain a mortgage and “own” a home. These sub-prime mortgages eventually caught up to people when they couldn’t cover their monthly payment. The properties of many were foreclosed by the banks and people lost their homes. This destroyed the housing market which increased the snowball even more. The sub-prime mortgage “bubble” eventually popped and the downward spiral became evident.

Everyone began to spend less at the malls, restaurants, and everywhere else. Credit card companies were forced to raise their interest rates because of the number of consumers defaulting on their debt. In my experience, one of my credit cards went up to 29 percent even though I have never missed a payment. It was hard for me to meet my monthly payments because I was paying additional interest. I would not default on my debt though, no matter how bad it got. It was my duty and my responsibility to pay back the money that I borrowed and used to purchase my consumer needs. Too many people defaulted on their debts during this time and this made the whole situation even worse. Worldwide panic began to take place and every other country was affected because the markets are connected on a global scale. It has always been said, when the United States has a hiccup, the rest of the world will be aware of it.

Something needed to change and it needed to change very quickly. There was loss of wealth in all corners of the market and people were not happy about it. The Dodd-Frank Wall Street Reform and Consumer Protection Act was passed in 2010 to prevent another significant recession.

The Frank-Dodd Act is a major legislation reform that imposes regulations on our financial systems and was created to decrease the risk of future financial collapse. Senator Christopher J. Dodd and U.S. Representative Barney Frank were two key people that were involved in helping this legislation pass and that is why it was named after them. The United States government felt that they had to step in and create more regulations to prevent this turmoil from happening again.

Companies that were considered too big to fail had the support of the government during this financial crisis. These large financial institutions were essentially “bailed out” to prevent the total collapse of our economy. Financial organizations are now monitored even more closely and the government is preventing tax dollars from going into banks that aren’t financially stable enough. If the banks are too large, the government is now trying to make regulations to prevent this.

The government bailed out Fannie Mae, Freddie Mac, and AIG. An example of one bank that they let fail was Lehman brothers. Lehman Brothers had to file for Chapter 11 bankruptcy.

**CREATION OF NEW GOVERNMENT AGENCIES**

1. **Financial Stability Oversight Council**

The Financial Oversight Council was enacted to oversee the financial system and to pinpoint the different variables that could affect the financial system. The stability of our country would now be determined by this council after the Frank-Dodd Act was put into motion. The Financial Stability Oversight Council is a big advocate for market discipline and promotes it regularly. There are ten members that vote and five members that do not vote. Their jobs are not only to actively seek threats to the American financial system, but also to create a sense of responsibility for these large organizations. Companies should be responsible for their own demise and the taxpayers will no longer be there to back them up. It was not fair for the companies that were “too big to fail” to be bailed out by the American people. The Financial Stability Oversight Council will essentially be standing over the shoulders of these large financial institutions and promoting the incentive for trading restraint.

1. **Orderly Liquidation Authority**

The Orderly Liquidation Authority was setup to quickly liquidate a failing large financial company. In addition, it can divide larger banks into smaller ones so that there is less of a possibility of failure. Also, it helps prevent the possibility of future government bailouts. This will keep the taxpayers happy and prevent the government from unnecessary spending. There are varying opinions on the effectiveness and efficiency of the Orderly Liquidation Authority. How can a government regulator pinpoint the risks involved with a large corporation that has thousands of employees? The CEO’s of these companies can’t even clearly define where the risks lie. They are required to come up with a “living will” of the company during economic turmoil which states how the liquidation of the company will take place if they declare bankruptcy. This takes extra time and effort of many employees in the company and how do we know if it was beneficial or not.

1. **Federal Insurance Office**

The Federal Insurance Office figures out who the insurance companies are, it keeps track of them, and determines which ones are risky. Before the financial crisis, there were many flaws in the regulation of insurance companies. One of the largest insurance companies, AIG, began to fail and it helped snowball the financial crisis. The Federal Insurance Office is part of the United States Treasury Department. It doesn’t enforce the rules, but instead monitors insurance practices and suggests legislation accordingly. The Federal Insurance Office is also on the advisory board of the Financial Stability Oversight Council, so they overlap each other. Monitoring the risk of these giant insurance companies is no easy task. This is another watchdog type organization that will have to overlook the daily operations of an insurance company to assess their risks and the effect of the company’s actions on the total economy. This would create government jobs that may or may not get in the way of business operations. The insurance companies may view these regulators as “hall monitors”, but the insurance regulators believe that they are making a difference. In theory, the taxpayers would appreciate the stability that the Federal Insurance Office will bring and it will prevent the taxpayers from bailing out large insurance companies like American Insurance Group, which previously happened in the financial crisis of 2008. The American people shelled out 85 billion dollars to cover the collapse of AIG. AIG could sell parts of their businesses quickly but without hurting the economy further. Now the federal government owned 80 percent equity of the largest private insurance company.

1. **Consumer Financial Protection Bureau**

The Consumer Financial Protection Bureau was created to protect the people from financial products such as mortgages and other products. They are the ones that give more power to the people and increase consumer protection from these giant financial institutions. Mortgage lenders would influence people to buy homes that were out of their price range. These home buyers were signing up for home loans that put a strain on their financial situation. The mission of the Consumer Financial Protection Bureau is also to help the consumer understand the mortgage by increasing the simplicity of the documents. Taking out a loan for home is a huge commitment and most people don’t read the fine print. Even if they do read the fine print, the document was written by a team of lawyers and it may be hard to understand. The Consumer Financial Protection Bureau website offers financial information and webinars for free that help the American people educate themselves on financial matters. Whether it is refinancing a home mortgage, saving for a rainy day, or planning for retirement, this organization has the tools that everyone will need to financially succeed. Also, you can submit a complaint about a financial product or service. They have handled over 800,000 complaints and have helped over 25 million receive relief.

1. **Office of Credit Ratings for the Securities and Exchange Commission**

This new office was setup to come up with accurate credit ratings for businesses and governments. The credit ratings are vital indicators of the company’s strength and volatility. During the financial crisis, credit rating agencies like Moody’s Investor Service were lying about the credit ratings. Companies that were low-quality debt securities were given high marks to increase profits. Despite the changes since the financial crises, these false credit ratings continue to happen. These credits rating agencies were responsible for billions of dollars lost during this economic crisis and it will continue to be this way until there is strict enforcement on the regulations that were set.

The Volcker rule was created to regulate the way that banks could invest and it changed the way that the derivatives were traded. A derivative is simply a tradable security that fluctuates based on the movements of other assets. The Volcker Rule was created because of all the speculative trading that banks were engaged in. Experts believe that this helped contribute to the downfall of the financial systems and the collapse. Theoretically, banks would not be allowed to invest into hedge funds because that would be a conflict of interest. It was named after Paul Volcker which was once a chairman of the United States Federal Reserve. President Barack Obama was the first to support the Volcker Rule when it was created. Last year, the House of Representatives tried to delay some of the Volcker Rule by two years. President Obama tried to veto a bill that Republicans were trying to pass to stall the enforcement of the rule. The democrats want to speed up these rules to go into effect to increase the stability of the American citizens and to regulate the trading on Wall Street.

The derivatives that presented the most risk were the credit default swaps. The Frank-Dodd Act aimed to regulate these credit default swaps via the Securities and Exchange Commission. This would be possible using a clearing house which would allow the trade to be transparent. The risks could then be identified by the regulators and the actions to prevent economic turmoil would follow. A credit default swap is basically something that you buy to hedge your bets. It is betting on when someone won’t pay their debt. The institution that sells the credit default swap is usually confident that the debt security will not default. On the other hand, the person buying the credit default swap is confident that the debt security will default. As you can see, this is a very risky trading platform and it is traded over the counter. This means that the credit default swaps are not regulated. This can increase the entire market snowball, which we saw in the financial crisis, and the potential investor losses could be huge if they are on the wrong side.

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