

MEMO# 25258

June 7, 2011

ICI Comment Letter on the Financial Stability Board's Note on Shadow Banking

[25258]

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TO: INTERNATIONAL MEMBERS No. 23-11
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 37-11
SEC RULES MEMBERS No. 66-11 RE: ICI COMMENT LETTER ON THE FINANCIAL STABILITY BOARD'S NOTE ON SHADOW BANKING

On June 3, the Institute submitted a comment letter on the background note issued by the Financial Stability Board ("FSB") entitled "Shadow Banking: Scoping the Issues" ("Note").

[\[1\]](#) In response to a directive from its member institutions to develop recommendations to strengthen the oversight and regulation of the "shadow banking system," the FSB established a task force to consider the following: (1) a definition for "shadow banking"; (2) potential approaches to monitoring the "shadow banking" system; and (3) possible regulatory approaches to address systemic risk and regulatory arbitrage concerns posed by the "shadow banking" system. The Note describes the current thinking of the FSB's task force, particularly on the definition of the "shadow banking system."

The Institute's letter states that, as a preliminary matter, the Institute strongly objects to the use of the terms "shadow banks" and "shadow banking" because they are inherently inaccurate and misleading. The letter urges the FSB to use more precise and neutral terminology when discussing the various roles of non-bank financial intermediaries. Although the roles may share some similarities, there are critical differences between banks and non-bank financial intermediaries, and these differences should be respected.

The Institute's letter acknowledges that it is appropriate for the FSB to consider whether additional or different regulatory measures for non-bank financial intermediaries may be important to strengthening the global financial system. It stresses, however, that the proposed regulatory responses offered by the Note are quite broad and amorphous, and that certain interpretations of possible policy responses would be very problematic.

The Institute's letter also expresses deep concerns with the tenor of much of the Note's lengthy discussion of the perceived deficiencies or laxity of regulation to which "shadow banks" are currently subject. The letter states that evaluating the regulation of non-bank

financial intermediaries solely through a banking lens distorts and ignores the very substantive regulation and oversight to which these entities are subject through the securities laws. It is imperative, in our view, for the FSB to acknowledge and respect the differences that exist between banking and securities and their respective regulatory frameworks. The letter urges the FSB to reevaluate the “universal bank” framework set forth in the Note, and carefully consider the long history, in the United States and elsewhere, of parallel systems for intermediation that capital markets and banks provide. The letter further states that it is critically important that the FSB identify those specific features and activities of capital markets that pose potential risks to the global financial system, why such risks arise, and how existing regulation does not address those risks.

To assist the FSB, the Institute’s letter contains three appendices. Appendix A outlines the history in the United States of the successful co-existence of the banking and securities industries, as well as the origins of the Investment Company Act of 1940. Appendix B describes how capital markets and entities that operate in them provide credit intermediation in a manner that is quite different from banks. Appendix C describes how the existing regulatory structure of the Investment Company Act addresses risks that otherwise could arise from mutual funds, including the specific rules applicable to money market funds.

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[Attachment](#)

endnotes

[1] Financial Stability Board, Shadow Banking: Scoping the Issues, April 11, 2011, available at http://www.financialstabilityboard.org/publications/r_110412a.pdf (“Note”).

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