From: RDavis [mailto:rdavis@femto-second.com]
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To: LLPComments
Subject: Legacy Loans Program

March 29, 2009

Dear Mr. Feldman,

I am please to present the following Legacy Loans Program comments.

Respectfully,

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Before discussing the FDIC proposal, it is worth looking at the consequences to another insurance issuer, AIG. The largest insurance company in the world started issuing Credit Default Swaps (CDS) and when the paper insured lost value, AIG needed Government help [1]. There really was nothing wrong with the AIG model, or the FDIC proposed approach for that matter. Nevertheless, the root cause has yet to be addressed and until it does any such approach remains at risk.

Following the collapse of the Bear Stearns investment bank, the then SEC Chairman, Christopher Cox, testified before congress that by all regulatory measures, four days prior to the collapse, Bear Sterns was healthy. He went on to describe the run on the bank due to a False Rumor [2].

To explore false rumors consider the next example. On Monday (Sept. 8, 2008), a six-year old article about 'United air Lines' (UAL) inadvertently re-posted to a news media web page, caused a sell-off where the stock lost $1 billion in value in a matter of minutes [3]. Today, most large traders rely on computer programs designed to kick in when certain news surfaces. These programs typically run without human intervention. The programs are referred to as "algos." In 2007 they accounted for 30 percent of all equity trades [4].

Consider a financial institution and methodology for determine safety and soundness. Other factors, such as the company stock price affect the credit ratings for the company. Regulatory oversight must take a holistic view that includes factors never consider core to bank examinations. Consider, Lehman Brothers was the largest bankruptcy in US history [5]. And this occurred after efforts to prevent another Bears Sterns were put into place. In his testimony before the House Government Oversight Committee, Lehman Brothers Holdings CEO Richard Fuld blamed the collapse of his company on false rumors, short-selling, and a general lack of confidence on Wall Street [6]. The tragedy is that Lehman Brothers, by regulatory standards, was healthy and sound. Following the Lehman collapse, the dominos fell fast and this is where we are today.

There are computer [programs operating without human intervention that are controlling the financial stability of the nation. Would the Department of Transportation allow plans to fly by computer without pilots? Why then is the financial health of the nation allowed to operate without human intervention? So what has changed to prevent another occurrence of multiple bank failures?

The challenges do not stop here. During Senate Commerce, Science, & Transportation hearings on cybersecurity, Dr. Ed Amoroso, Chief Security Officer, AT&T, testified cyber-crime exceeded drug trafficking as the most lucrative illegal global business; now exceeding $1 trillion per year [7]. What controls are in place to ensure that Cyberattacks do not decimate the financial markets?

The regulatory agencies are not addressing the root cause of the current problem. A financial institution could have 100% AAA instruments and still be wiped out in hours by silent runs and nefarious Cyberattacks. Technology has outpaced the regulatory practices and risk factors have dramatically changed. The Government has the technology and ability to tame this beast but has yet to focus on the core issue surrounding the financial maelstrom.

References:

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