



Faith and Finance: Finding Common Ground to Protect the Common Good

ICCR Financial Services Sector Team – October, 2010

Introduction

The engagement of the ICCR team with the financial services sector stretches back nearly forty years and has focused on a broad range of issues and themes. At the heart of this engagement has been the concern of faith based investors about the social purpose of economic activity and the fairness of the financial system which serves as its foundation. Our approach has been to examine ways in which the major institutional actors in the private sector have been attentive to our concerns: concerns that are succinctly captured in the principle, “the protection and promotion of the common good.”

Safeguarding and promoting opportunities for people across the world to participate in economic activity and to access the benefits that flow from credit and other financial services must be a top priority for any financial system that hopes to promote sustainable development and serve the well-being of people across the world. Our position and commitment as active, faith based and responsible shareholders has afforded us the opportunity to focus on the major actors in the financial services space, including commercial and investment banks, asset managers, credit rating agencies and insurance companies. Our commitment to faithful and responsible citizenship has also called us to examine and monitor the ways that U.S. and global policy makers e.g. Congress and other institutions (World Bank, International Monetary Fund) with legislative or regulatory power have been fulfilling their responsibility to both regulate the financial system and supervise the economic activities that the system makes possible.

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The current crisis and our response

The ICCR team was active before the recent financial crisis in addressing off balance sheet liabilities, predatory sub-prime lending and the extraordinary risk, instability and leverage that the use of derivatives and other practices was creating. In addition to the challenges that these tools and activities present to individual institutions, they also introduce unreasonable and unmanageable risk into a globally integrated financial system that impacts us all, yet disproportionately affects the world's poorest communities when a crisis occurs. In responding to the crisis, our statement in September 2008 called for greater transparency, accountability, risk management and the adoption of the precautionary principle to test and monitor the introduction of innovative mechanisms, tools and securitization models into the financial sector. We also called for vigorous debate and deliberation over the reforms that were necessary in the organizational structure and regulatory framework of the financial system.

Our May 2009 statement presented a summary of the lessons we learned concerning the causes of the crisis and recommended appropriate legislative responses. That report detailed the ways in which major financial institutions failed to safeguard society, and by extension the global community, and exposed loopholes in the regulatory framework that were designed to provide systemic stability through timely monitoring and regulation. We also identified the specific challenges that needed to be addressed in the United States, in the G20, and by those responsible for ensuring the stability of the global system, and proposed meaningful solutions to these issues.

We continue to monitor and study the findings of some of the numerous inquiry panels and public hearings that have been established to analyze the lapses in policy and practices that led to the near collapse of the financial system in Sept. 2008. (Financial Crisis Inquiry Commission; The Squam Lake Report)

Financial Regulatory Reform

A brief summary of the highlights of the Dodd-Frank legislation includes the following items:

- (1) A number of protections for consumers that call for greater transparency by companies providing services for mortgages, credit cards and debit cards as well as the fees that they charge have been enacted. A Consumer Financial Protection Bureau has been established to act as an advocate for consumers in most financial transactions.

- (2) Most derivatives that are now traded dealer to dealer will be traded on public exchanges and will be processed through separate clearinghouses. This will minimize the danger of contagion to the system brought on by the irresponsible risk-taking of individual players and counter parties.
- (3) A council is mandated to advise regulators on emerging threats and to provide consolidated oversight of financial products from mortgages to credit cards.
- (4) Regulators are given additional authority to seize any financial company that further threatens the financial system, an authority they did not previously have, to deal with rogue companies like Lehmann or AIG.

However, the legislation did not address the imposition of a possible bank levy (tax) or the adoption of more stringent requirements on capital and liquidity for individual institutions as a buffer in times of crisis. Proposals in these areas have been made to the G20 and will be considered at their next meeting in Seoul in November 2010.

The Way Forward

As we continue our commitment to engage some of the biggest and most powerful institutions in the sector and to expand our focus to include other actors in this space, we want to present an outline of our priorities going forward. This engagement presumes that political leaders and government authorities will direct economic activity towards the common good and that regulatory agencies will ensure the soundness and safety of the system.

1. An open, transparent, and well-regulated global financial system is vital to serve the needs of all stakeholders, especially the world's poor, who are even more vulnerable during times of financial crisis. The challenges that such realities as 'moral hazard' present need to be anticipated and addressed. The cooperation and support of the private sector, especially large financial institutions which operate at a global level and at a staggering pace, is essential to the achievement of this objective.
2. Transparent and secure markets are essential to price discovery and to the reliable conduct of financial transactions between market participants. All of the actors and participants in the system must be aware of the risk that is introduced into the financial system as a result of their illegal or imprudent activities and decisions and must be held accountable for the consequences.

3. An adequately resourced global network of integrated regulatory agencies at appropriate levels, with fairly compensated professional staffing, is essential in a globally integrated financial system. This requires enhanced cooperation between sovereign governments, international financial institutions and regional associations.
4. The revolving door between regulators, companies and industry associations must be closely monitored if public confidence in the system, the regulatory framework and the regulatory agencies is to be restored and maintained.
5. The risk management structure of financial institutions must be fully integrated into their business models and across all operations of their business. It must be transparent, adequately staffed and accountable directly to senior management and the board of directors.
6. Innovative tools and mechanisms as well as boutique services that are employed in business operations between lenders, borrowers, dealers, underwriters and investors in both individual institutions and across the industry must be tested, monitored and strenuously evaluated for soundness, suitability, integrity and safety. The application of the precautionary principle is especially appropriate in this regard.

If the concepts expressed in these priorities are implemented, we believe that we will be on our way to building a financial system that promotes sustainable development and protects and promotes the common good.

About ICCR

The Interfaith Center on Corporate Responsibility, currently celebrating its 40th year, is a membership organization comprised of 275 institutional investors representing faith communities, asset management companies, pension funds, unions and colleges with over \$100 million in assets under management. ICCR members work in coalition to promote ethical business practices across a wide variety of environmental and social justice issues.