AGA-Austin Chapter
Program & Luncheon Meeting Minutes
Meeting Date: September 8, 2011

The meeting was called to order at 11:45 a.m.

Regular Business

Debi Weyer, Program and CPE Event Chair, welcomed everyone to the first luncheon of the 2011-2012 Chapter year.

1st time attendees included:

- Susan Pennington – Texas Workforce Commission
- Scot Leith – Teacher Retirement System
- Amanda Jenami – Water Development Board

Kadie Weyer, Membership Chair, made the following announcements:

- A Facebook page and a Twitter page have been created for the Chapter. For Twitter, Google AGA Austin Twitter. In Facebook, search for Association of Government Accountants. Check 'em out! Great job Kadie!
- The Austin Chapter currently has 103 members.
- The National Office is sponsoring "Ready, Set, Grow" which rewards current members with a free year of dues when six of their referrals become AGA members. Recruit one new member before April 31st and be eligible to win an iPad. When you recruit 10 new members, your name will be placed into a drawing for a $200 American Express gift card.
- The Chapter's first Meet & Greet of the year will be held from 4:00 pm to 7:00 pm at Garrido's on Friday, September 24th. Garrido's is located on Neches at 3rd Street in Austin.

Program Speaker

Debi Weyer introduced Joe Collins, Certified Fraud Examiner.

Joe Collins began his financial career in San Antonio in 1993 and after three years of training in the art of target marketing he returned to American Express Financial Advisors to build a franchise from scratch. In January 1998 he earned his Series 7 (General Securities Representative Exam), then his Series 63 (Uniform Securities State Law Exam, which allows individuals to become securities agents and to solicit orders for any type of security in a particular state), and finally his Group I.

Joe worked with several advisors to conduct seminars and he developed the first multiple employer 401(k) plan in Texas using the Nationwide product.

In 2003, Joe and a business partner created a Wealth Management team that offered personalized investment strategies along with risk management and diversification. Diversified strategies included stocks, bonds, CDs, mutual funds, closed-end funds, ETFs, publicly traded REITS, annuities, and tax advantaged life insurance. Joe has also performed stock option and pension planning analysis, and has experience in estate and trust management.

2008 Stock Market Crash – A Disaster in the Making

What really happened?

- Greed
- Easy Credit
- Feeling that housing prices will go up forever
- Adjustable Rate Mortgages
- Low interest rates
- Speculation
- Regulators "asleep at the wheel"
- Predatory lending

Joe treated the attendees to a video that was a collage of "It's A Wonderful Life" interspersed with congressional testimony heard at the height of the crises. He also showed the movie trailer from "Inside Job". If you rent this movie, Joe highly recommends viewing the deleted scenes.

A History Lesson

The Banking Act of 1933, also known as the Glass Steagall Act, created the Federal Deposit Insurance Corporation and introduced reforms in part to control speculation. It also allowed the Federal Reserve to control interest rates on savings accounts. Provisions of the act that prohibited a bank holding company from owning other financial companies was repealed in 1999 by the Graham Leach Bliley Act, which allowed the government to set interest rates. The repeal effectively removed the separation that existed between investment banking, which issued securities, and commercial banks, which held deposits. In addition, the deregulation removed the conflict of interest prohibitions between investment bankers serving as officers of commercial banks.

Economists believe this repeal directly contributed to the severity of the 2008 financial crisis by allowing Wall Street investment banking firms to gamble with depositors' money. Citigroup, the largest U.S. bank in 1999 began to underwrite and trade instruments such as mortgage-backed securities and collateralized debt obligations and to establish structured investment vehicles that bought those securities. The year before the repeal, sub-prime loans were just five percent of all mortgage lending, but approached 30 percent by the beginning of the credit crisis.

The Federal Reserve was left as the only government entity with the power to prevent what happened in the mortgage industry and yet it failed to prevent it. Hank Paulson left a multi-million dollar salary at Goldman Sachs to become the US Treasury Secretary until January 2009.

By the arrival of the 1st weekend in September, 2008, Ben Bernanke, Chairman of the Federal Reserve, and Hank Paulsen were faced with two options:

- Risk the total collapse of the banking system, or
- Inject trillions of taxpayer dollars into the system

In 2007, 10 of the largest commercial banks held 55% of the financial industry's assets, and debt held by the financial sector had ballooned to $36 trillion, an increase of 1100% since 1978.

Mortgage Backed Securities

Created in 1985, mortgage-backed securities (MBSs) are shares of a home loan sold to investors. A bank lends a borrower the money to buy a house and collects the monthly payments on the loan. This loan and a number of others -- perhaps hundreds -- are sold to a larger bank that packages the loans together into a mortgage-backed security. The larger bank then issues shares of this security, called tranches (French for "slices"), to investors who buy them and ultimately collect the dividends in the form of the monthly mortgage payments.

Each tranch is rated as to the quality of the mortgages that are packaged into them. Ratings range from AAA (prime mortgages) down to B ("liar loans"). These tranches can be further repackaged and sold again as other securities, called collateralized debt obligations (CDOs). CDOs include packaged credit card debt, auto loans, second mortgages, sub-prime loans, corporate debt, and commercial mortgages.

Shadow Banking

Shadow banks are financial intermediaries that facilitate the creation of credit across the global financial system, but whose members are not subject to regulatory oversight.

The shadow banking system escaped regulation primarily because it did not accept traditional bank deposits. As a result, many of the institutions and instruments were able to employ higher market, credit,

and liquidity risks, and did not have capital requirements commensurate with those risks. Subsequent to the 2008 meltdown, the activities of the shadow banking system came under increasing scrutiny and regulations.

The shadow banking system also refers to unregulated activities by regulated institutions. Intermediaries not subject to regulation include hedge funds, unlisted derivatives, and other unlisted instruments and their names may be familiar to you such as Lehman Brothers and Bear Stearns. Examples of unregulated activities by regulated institutions include credit default swaps.

Credit default swaps (CDSs) are swap contracts and agreements in which the "protection" buyer of the CDSs makes a series of payments to the "protection" seller, and in exchange, receives a payoff if a credit instrument (typically a bond or loan) experiences a "credit event". It is a form of reverse trading.

CDSs were a bet on home prices not rising so fast, and not a bet on home prices collapsing – a way of gambling on sub-prime mortgage bonds going down. By the end of 2007, the total market value of CDSs was $38.8 trillion. American International Group sold $20 billion in CDSs to Goldman Sachs who racked up $400 million in riskless profits each year! AIG used $10 billion in TARP funds to repay what it owed to Goldman Sachs.

AIG made $500 billion bets that housing prices would continue to rise and sold "insurance" against the mortgage market failing. The federal government bailout of AIG totaled $180 billion because of concerns that their collapse would trigger cascading losses throughout the financial system.

Not a single person convicted as a result of the 2008 crisis has ever served any prison time. They instead have been allowed to pay massive fines.

In the end, the crisis resulted in:

- 26 million Americans out of work
- 3 million foreclosures in 2010
- 9 million estimated foreclosures in 2011

Financial Crisis Inquiry Commission

After the meltdown, the federal government created the Financial Crisis Inquiry Commission, whose first public hearing was held in January 2010, but which took a full year to publish its findings.

The commission concluded that the crisis:

- was avoidable
- was caused by widespread failures in financial regulation, including the Federal Reserve's failure to stem the tide of toxic mortgages
- was a dramatic breakdown in corporate governance with financial firms acting recklessly and taking on too much risk
- was the result of an explosive mix of excessive borrowing and risk by households and Wall Street
- was in part due to a lack of a full understanding by key policy makers of the financial system they oversaw
- was a result of widespread breaches in accountability and ethics at all levels

Conclusion

Unfortunately, the CDS market is growing again and they are being sold in Europe, Japan, and China. The world as we know it has changed.

In conclusion, Joe stated "We must design systems and processes that keep this from happening, rather than prosecuting afterwards."

Joe remembers the days during his financial planning years when it was all about “kayaks and sunsets”.

Sources:

The Weekend That Changed Wall Street, Maria Bartiromo
The Big Short, Michael Lewis
Crash of the Titans, Greg Farrell
Conclusions of the Financial Crisis Inquiry Report

Adjournment

Number attending: 33 (including the speaker)

Next event: October 13, 2011

Luncheon
11:50 a.m. – 12:50 p.m.
Location: Corazon at Castle Hill

The meeting was adjourned at 12:55 p.m.

Lynne Pfeffer Date: October 7, 2011
Secretary