Our Perspectives:
Commentary on the economy & regulatory policies affecting financial companies

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National Institute of Finance*

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Consideration should be given to the creation and development of a National Institute of Finance organization modeled after the National Institutes of Health (NIH).

Just as the public supports NIH because it works with the private sector and focuses on basic research into significant health questions that effect everyone in the economy, so a National Institute of Finance would likewise focus on an issue of major importance to the country, namely the financial health of the country and its citizens, and would warrant similar support.

A National Institute of Finance could consider both current and future financial issues of importance to the maintenance and development of the U.S. as a financial center of the world. It could bring together active *participants* in the financial world to focus upon pressing issues as they arise. It could encourage development of systems and techniques that would lead to more competitive positioning for U.S. financial firms. It could provide the discipline needed to consider all aspects of financial activity to ensure that the product utilized addresses the concerns of all parts of the population.

There are natural divisions of finance that could serve as the parameters within the institute, such as secondary market finance, commercial and residential mortgage finance, consumer finance, public and quasi-public finance, international finance, global finance, and others.

Such institutes could provide unbiased systematic research into issues that arise and for which we now have no public or private institution designed to provide that research. It could have clinical arms that could engage in real time testing of different processes, parameters or products.

NIH is a logical model to consider when reflecting on the need for a design of a National Institute of Finance. While there are drawbacks to

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the model that NIH represents, it still is a good model demonstrating that public and private resources can be combined to address major issues in society. NIH institutions get appropriations from Congress and grants from private sources, usually directed to one of the specific institutes. Persons are employed as government employees or contract with NIH to perform research in certain specific areas — cancer research, alcoholism research, AIDS research, etc.

The combination has been successful, notwithstanding some glitches along the way. Starting as a one person "laboratory of hygiene" in the Marine Hospital Service[1] in Staten Island in 1887, it moved to D.C. a few years later and got its first appropriation recognition in 1901, when $35,000 was appropriated to build a building to house the laboratory. A year later, it received money to hire employees in the newly expanded laboratory, including PhDs in addition to M.D.s. In 1930, after the laboratory served admirably during and after WWI, an act of Congress renamed it the National Institute of Health, and when the National Cancer Institute was created 7 years later, an "s" was added to "Institute." It has expanded since then with different institutes focused on different health issues — mental health, heart, dental, arthritis, and allergies. Now there are 27 separate institutes.

The success of NIH is measured, in part, by the fact that over 138 NIH-supported scientists have won or shared in 83 Nobel prizes. Partnerships between individual private companies and NIH are a regular part of the NIH programs, the NIH side of the financing coming from individual institutes. Both the private sector and the public sector have benefitted from the organization.

For private sector financial companies, the benefit from the development of a National Institute of Finance would be an increase in knowledge and understanding about the potential causes and effects of various ideas generated by any of a variety of parties, such as those found in federal, state or local governments, the media, think tanks, universities, international financial organizations or regulatory bodies. An increase in reliable data would also be a by-product of the institute, as would the relationship between different regulatory schemes, either locally or globally, and the impact the difference would have on the creation of economic growth. It would be the logical repository of a national library of finance.

[1] The predecessor to the Public Health Service.

At the same time, the institute would be very useful to the public sector. Congress and the regulatory agencies, as well as agencies such as the Federal Reserve, the Treasury and the National Economic Council, have need of a research organization staffed by accomplished and knowledgeable individuals whose major interest is finding the source of financial problems and the effect on all parties of suggested solutions to those problems. Such an institute would have the added benefit of close ties to the private sector, so government agencies could interact directly with individuals and companies in the private sector in a protected environment.

Funding for basic research in the financial sector is disbursed among many entities, and in many cases, efforts are redundant. Trade associations and consumer activist organizations currently provide efficiency and do a very good job of limited research. The institute would make all of those organizations more productive.

Such an organization was necessary as Congress reflected on the major changes included in the Dodd-Frank Act, but such an organization did not exist and the parties developing the law were forced to make decisions on many crucial issues without a full knowledge of the effect of those decisions. In some cases they appeared to have made the right choice. In others, it appears they did not. In a third set of choices, they passed the authority to make crucial decisions to agencies, and those agencies, in turn, suffer from the same lack of good data. Similar problems have arisen frequently over time in the financial services sector as decisions have been made without good data behind them. A National Institute of Finance would not solve all of the problems, but it could solve many of them.

Fortunately, some steps have been taken toward such an institute. The Dodd-Frank Act created an Office of Financial Research, funded solely by the government, that could be used as the catalyst to develop such an institute. Its scope is too narrow, however, being created primarily to provide assistance to the Financial Stability Oversight Council. More important, it is entirely government-centric. Its purpose is to support government entities, and although there is a bow toward essential long-term research, the statute does not conceive of a partnership between the government and the private sector. That partnership is the backbone of the successful research that NIH has done in health issues, and a similar partnership could invigorate both the public and private sectors if applied to the financial services sector. Operating just as a government entity, however, it is doubtful that it will create the same kind of long-term successful research that NIH has accomplished.

Nevertheless, with the creation of OFA, the DFA demonstrated the Congressional belief that there is a need for basic financial services research. Moving from that belief to a broader vision of the method by which such successful research could be created could lead in many directions. One that has a successful counterpart is the development of a National Institute of Finance.

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