



Americans for Financial Reform
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June 10, 2014

Dear Representative:

Americans for Financial Reform urges you to reject the two pieces of legislation before you concerning the Financial Stability Oversight Council (FSOC), HR 4387, the FSOC Transparency and Accountability Act, and the discussion draft, the FSOC Designation Moratorium Act.¹

The FSOC is a crucial and necessary part of the Dodd-Frank Act's response to the 2008 financial crisis, which caused well over \$10 trillion in damage to the U.S. economy and led to millions of job losses and home foreclosures. The capacity to designate non-banks critical to the U.S. financial system for appropriate regulatory oversight is a central element of FSOC's powers. The FSOC designation procedure includes multiple procedural safeguards and opportunities for appeal, and is already a lengthy process. Yet the FSOC Designation Moratorium Act would impose an arbitrary and unjustified six-month moratorium on such designations.

While AFR agrees that there are a number of useful steps that could be taken to enhance FSOC transparency, HR 4387, the FSOC Transparency and Accountability Act, is not a responsible attempt to accomplish this goal. HR 4387 does not adopt reasonable measures recommended by the General Accounting Office in their 2012 study of the issue, such as mandating the release of transcripts of FSOC closed meetings after a suitable time period or necessary redactions.² Instead, HR 4387 would burden FSOC operations by almost tripling the number of voting members of the Council from 10 to 28. It would also impose excessive, impractical, and unprecedented requirements for non-member access to FSOC and FSOC-related meetings, including meetings of representatives of FSOC member agencies. These measures would damage FSOC's practical ability to function in ways that that would be far out of proportion to any transparency benefits gained.

Background: The Significance of FSOC

The FSOC was created as a response to the 2008 financial crisis, which revealed grave weaknesses in the U.S. system of financial regulation and oversight. Many of these weaknesses

¹ Americans for Financial Reform is an unprecedented coalition of more than 200 national, state and local groups who have come together to reform the financial industry. Members of our coalition include consumer, civil rights, investor, retiree, community, labor, faith based and business groups.

² www.gao.gov/products/gao-12-866

were related to the fragmented and divided nature of our regulatory apparatus, which no longer reflected the reality of the modern financial system. After the Gramm Leach Bliley Act repealed the last vestiges of the Glass-Steagall divisions between banking, insurance, and trading markets, the financial system became more highly interconnected, allowing for the rapid transfer of risk between insurance companies, commercial banks, broker-dealers, and large hedge funds.³ Problems emerging in any one of these sectors can easily impact the others, and if the risks involved are large enough they can threaten the stability of the entire financial system. But even as the financial system grew more deeply interrelated, our regulatory system continued to rely on over a half a dozen separate and siloed financial regulators that often did not share information and failed to spot critical emerging risks.

This problem clearly made a direct contribution to the financial crisis of 2008 and its disastrous impact on the U.S. and world economy. Commercial and investment banks transferred hundreds of billions of dollars in mortgage risk to an insurance company, AIG, escaping the supervision of banking and securities regulators. AIG eventually received the largest government bailout in U.S. history. Broker-dealers which were not commercial banks, such as Bear Stearns, Lehman Brothers, Morgan Stanley, and Goldman Sachs, were at the center of the Wall Street network that created and distributed the ‘toxic assets’ central to the crisis. Hedge funds were also key intermediaries in the distribution and structuring of these toxic assets.⁴ The failure of a single money market mutual fund, the Reserve Primary Fund, triggered a massive run on prime money funds followed by a government bailout of the entire sector, which is a crucial part of the asset management industry. Of course, the nation’s largest commercial banks were also central to the crisis, ranging from the failed Washington Mutual to ‘too big to fail’ entities such as Bank of America and Citibank, which were rescued by the Federal government.

In the Dodd-Frank Act, Congress took a measured approach to addressing the problem of the fragmentation of the regulatory system. The Dodd-Frank Act eliminated only one financial regulator (the Office of Thrift Supervision). Other financial regulators were directed to coordinate their efforts through a joint committee, the Financial Stability Oversight Council (FSOC), which has a new research arm (the Office of Financial Research, or OFR) dedicated to gathering information and performing analyses that track risks in the financial system as a whole. Based on the input of all participating financial regulators, as well as data gathered by the OFR, the FSOC has the power to designate large non-banks that play a crucial role in the financial system for heightened prudential oversight by the Federal Reserve. Such oversight applies only to specified financial activities of companies so designated and may or may not be ‘bank like’ in nature, depending on what type of supervision is appropriate for a specific company.

³ See Billio, Monica & Getmansky, Mila & Lo, Andrew W. & Pelizzon, Loriana, 2012. "[Econometric measures of connectedness and systemic risk in the finance and insurance sectors](#)," [Journal of Financial Economics](#), Elsevier, vol. 104(3), pages 535-559.

⁴ For one example, see, Eisinger, Jesse and Jake Bernstein, "[The Magnetar Trade: How One Hedge Fund Helped Keep the Housing Bubble Going](#)", ProPublica, April 9, 2010.

The question of exactly which non-banks should be designated as systemically significant and how such institutions should be regulated is a complex and institution-specific question. However, given the central role of non-banks in both the financial crisis and in the modern financial system, the general need for a designation power is clear. Furthermore, the role of the FSOC and OFR in scrutinizing the financial sector for emerging risks, including gathering the necessary information to do so, should not be controversial at all. Without such a central point for the gathering and analysis of data, the fragmentation of our regulatory system could lead to a repetition of past failures to ‘connect the dots’ of financial risk.

The FSOC Designation Process And the FSOC Designation Moratorium Act

As detailed in the attached table, the FSOC has laid out an extensive multi-step process for the designation of systemically significant non-bank financial companies. This process involves extensive communication between the FSOC and the company under consideration and permits the company multiple opportunities to challenge a potential designation. For example, if the FSOC issues a Proposed Designation of a company – a decision that requires a two-thirds vote of the Council, including a positive vote by the Treasury Secretary – the company may challenge the proposal in a private hearing with the FSOC. If the FSOC then votes (again by a two-thirds majority) to designate the company for increased prudential supervision, the company may appeal this decision to U.S. District Court. The District Court is then able to review the designation record and overturn the designation if it finds that the FSOC acted in an arbitrary and capricious manner.

This process requires extensive examination of each company and has proven to extend for multi-year periods. For example, the FSOC did not designate the recipient of the largest single-company cash bailout in U.S. history, the American International Group (AIG), for increased prudential supervision until July 2013. This was three years after the FSOC’s creation.

The FSOC Designation Moratorium Act would create an arbitrary and unjustified six-month moratorium on the final designation of any non-bank financial company, thus further extending what is already a lengthy and cumbersome process. While the six month time period involved is not long compared to the multi-year processes of designation that have been typical, this bill appears intended to send a negative message regarding FSOC designation authority that is in no way justified by the actions of the Commission or by the importance of the ability to designate non-bank financial companies that are central to the U.S. financial system. We urge you to reject it.

FSOC Transparency And HR 4387

As should be clear from the preceding discussion and the attached table, the FSOC designation process includes a large amount of transparency and interaction for the specific companies under consideration for designation. However, there have been legitimate concerns raised about the

transparency of FSOC proceedings to the public. The FSOC has committed to making its meetings open to the press and public “wherever possible”, and often does conduct open and accessible meetings through live web stream. However, the Commission also conducts many closed meetings in cases where they judge an open meeting would reveal any of a wide range of types of information the FSOC believes should remain confidential. These include information generated by regulatory or supervisory operations, information that may lead to financial speculation, information that includes trade secrets or commercial and financial information considered confidential, or agency memoranda not otherwise available publicly.⁵

A 2012 General Accounting Office examination of the FSOC includes a number of sensible suggestions concerning transparency, including the delayed release of closed meeting transcripts after a suitable time period has passed and/or suitable redactions have been made. AFR believes this recommendation deserves serious consideration. Other possibilities for improving transparency include reconsidering the currently extensive list of information types that trigger closure of an FSOC meeting. While some reasons for closing a meeting are clearly appropriate, others may be overly broad.

However, by vastly expanding the number of individuals with access to closed FSOC meetings, HR 4387 takes a different approach that we believe would burden and hinder the legitimate operations of the FSOC in a manner that is far out of proportion to any transparency improvement. It also does so in a manner that is more likely to lead to increased political manipulation by inside players, not increased transparency or accountability for the broader public.

. By making all members of regulatory boards or commissions full members of FSOC, HR 4387 would almost triple the number of voting FSOC members, from the current ten to as many as twenty eight. At its current size of ten voting members and fifteen total members the FSOC is already in danger of being an unwieldy organization.

Perhaps even more important, HR 4387 would vastly expand the number of non-FSOC members who could attend any Council meeting, or *any* meeting of representatives of FSOC member agencies. First, any FSOC member would be allowed to include any of their staff in any FSOC meeting, or in any meeting of the representatives of FSOC member agencies. Second, any member of the House Financial Services Committee or the Senate Banking Committee could attend any FSOC meeting, and the staff of these committees could attend any meeting of representatives of FSOC member agencies. These requirements would open any FSOC or FSOC-related meeting to literally hundreds of additional individuals. Even informal planning or technical meetings between any staff of FSOC member agencies could potentially be flooded by dozens of individuals who might be unfamiliar with the work being done or even opposed to it for political reasons. These requirements could make it extraordinarily difficult for the FSOC

⁵ <http://www.treasury.gov/initiatives/Documents/FSOCtransparencypolicy.pdf>

and its member agencies to do the difficult and critical work of coordinating financial regulatory efforts and sharing necessary information about risks to the financial system.

In sum, HR 4387 appears better calculated to hinder FSOC operations than to improve their transparency. Since the successful operation of the FSOC is crucial to the protection of American families and workers from the devastating impacts of another financial crisis, we urge you to reject HR 4387.

Thank you for your consideration. For more information please contact AFR's Policy Director, Marcus Stanley at marcus@ourfinancialsecurity.org or 202-466-3672.

Sincerely,

Americans for Financial Reform

STEPS IN FSOC DESIGNATION PROCESS FOR NON-BANK FINANCIAL COMPANIES

Step 1: Public data screen of companies	Compare publically available information on financial companies to pre-specified thresholds.
Step 2: Further review of selected companies	More detailed examination of public and regulatory data on selected companies.
Step 3: Inform company of consideration	Inform company that passes step two screen that they are under consideration for designation.
Step 4: In-depth analysis of selected company	In-depth information exchange with individual company under consideration. Likely to involve private and confidential data.
Step 5: Proposed Determination of company	FSOC votes on whether to issue a Proposed Determination of selected company. Proposed Determination requires two-thirds vote and affirmative vote of Treasury Secretary.
Step 6: Send notice and explanation to company	If a Proposed Determination is issued, FSOC sends a private notice and explanation to company.
Step 7: Opportunity for company challenge.	Company may request a confidential hearing with the FSOC to challenge a Proposed Determination.
Step 8: Final Determination of company	FSOC votes on whether to designate company for additional supervision. Requires two-thirds vote and affirmative vote of Treasury Secretary.
Step 9: Opportunity for company appeal.	A designated company may appeal a final designation to U.S. District Court, which has the power to overturn the designation.
Step 10: Continuing review of designation.	Each final designation must be reviewed on an annual basis by the FSOC and may be overturned by a two-thirds vote.

Following are the partners of Americans for Financial Reform.

All the organizations support the overall principles of AFR and are working for an accountable, fair and secure financial system. Not all of these organizations work on all of the issues covered by the coalition or have signed on to every statement.

- AARP
- A New Way Forward
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Income Life Insurance
- American Sustainable Business Council
- Americans for Democratic Action, Inc
- Americans United for Change
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- Center for Media and Democracy
- Center for Responsible Lending
- Center for Justice and Democracy
- Center of Concern
- Center for Effective Government
- Change to Win
- Clean Yield Asset Management
- Coastal Enterprises Inc.
- Color of Change
- Common Cause
- Communications Workers of America
- Community Development Transportation Lending Services
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO Mobile
- CTW Investment Group
- Demos
- Economic Policy Institute
- Essential Action
- Green America
- Greenlining Institute
- Good Business International

- HNMA Funding Company
- Home Actions
- Housing Counseling Services
- Home Defender's League
- Information Press
- Institute for Agriculture and Trade Policy
- Institute for Global Communications
- Institute for Policy Studies: Global Economy Project
- International Brotherhood of Teamsters
- Institute of Women's Policy Research
- Krull & Company
- Laborers' International Union of North America
- Lawyers' Committee for Civil Rights Under Law
- Main Street Alliance
- Move On
- NAACP
- NASCAT
- National Association of Consumer Advocates
- National Association of Neighborhoods
- National Community Reinvestment Coalition
- National Consumer Law Center (on behalf of its low-income clients)
- National Consumers League
- National Council of La Raza
- National Council of Women's Organizations
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Resource Center
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Nurses United
- National People's Action
- National Urban League
- Next Step
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO National Network
- Progress Now Action
- Progressive States Network
- Poverty and Race Research Action Council
- Public Citizen
- Sargent Shriver Center on Poverty Law
- SEIU
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Fuel Savers Club

- The Leadership Conference on Civil and Human Rights
- The Seminal
- TICAS
- U.S. Public Interest Research Group
- UNITE HERE
- United Food and Commercial Workers
- United States Student Association
- USAction
- Veris Wealth Partners
- Western States Center
- We the People Now
- Woodstock Institute
- World Privacy Forum
- UNET
- Union Plus
- Unitarian Universalist for a Just Economic Community

List of State and Local Partners

- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans For Responsible Lending
- Association for Neighborhood and Housing Development NY
- Audubon Partnership for Economic Development LDC, New York NY
- BAC Funding Consortium Inc., Miami FL
- Beech Capital Venture Corporation, Philadelphia PA
- California PIRG
- California Reinvestment Coalition
- Century Housing Corporation, Culver City CA
- CHANGER NY
- Chautauqua Home Rehabilitation and Improvement Corporation (NY)
- Chicago Community Loan Fund, Chicago IL
- Chicago Community Ventures, Chicago IL
- Chicago Consumer Coalition
- Citizen Potawatomi CDC, Shawnee OK
- Colorado PIRG
- Coalition on Homeless Housing in Ohio
- Community Capital Fund, Bridgeport CT
- Community Capital of Maryland, Baltimore MD
- Community Development Financial Institution of the Tohono O'odham Nation, Sells AZ
- Community Redevelopment Loan and Investment Fund, Atlanta GA
- Community Reinvestment Association of North Carolina
- Community Resource Group, Fayetteville A
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (NYC)
- Cooperative Fund of New England, Wilmington NC

- Corporacion de Desarrollo Economico de Ceiba, Ceiba PR
- Delta Foundation, Inc., Greenville MS
- Economic Opportunity Fund (EOF), Philadelphia PA
- Empire Justice Center NY
- Empowering and Strengthening Ohio's People (ESOP), Cleveland OH
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing
- Fitness and Praise Youth Development, Inc., Baton Rouge LA
- Florida Consumer Action Network
- Florida PIRG
- Funding Partners for Housing Solutions, Ft. Collins CO
- Georgia PIRG
- Grow Iowa Foundation, Greenfield IA
- Homewise, Inc., Santa Fe NM
- Idaho Nevada CDFI, Pocatello ID
- Idaho Chapter, National Association of Social Workers
- Illinois PIRG
- Impact Capital, Seattle WA
- Indiana PIRG
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc., Mayville NY
- La Casa Federal Credit Union, Newark NJ
- Low Income Investment Fund, San Francisco CA
- Long Island Housing Services NY
- MaineStream Finance, Bangor ME
- Maryland PIRG
- Massachusetts Consumers' Coalition
- MASSPIRG
- Massachusetts Fair Housing Center
- Michigan PIRG
- Midland Community Development Corporation, Midland TX
- Midwest Minnesota Community Development Corporation, Detroit Lakes MN
- Mile High Community Loan Fund, Denver CO
- Missouri PIRG
- Mortgage Recovery Service Center of L.A.
- Montana Community Development Corporation, Missoula MT
- Montana PIRG
- New Economy Project
- New Hampshire PIRG
- New Jersey Community Capital, Trenton NJ
- New Jersey Citizen Action
- New Jersey PIRG
- New Mexico PIRG
- New York PIRG
- New York City Aids Housing Network
- New Yorkers for Responsible Lending

- NOAH Community Development Fund, Inc., Boston MA
- Nonprofit Finance Fund, New York NY
- Nonprofits Assistance Fund, Minneapolis M
- North Carolina PIRG
- Northside Community Development Fund, Pittsburgh PA
- Ohio Capital Corporation for Housing, Columbus OH
- Ohio PIRG
- OligarchyUSA
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance, Charlottesville VA
- Michigan PIRG
- Rocky Mountain Peace and Justice Center, CO
- Rhode Island PIRG
- Rural Community Assistance Corporation, West Sacramento CA
- Rural Organizing Project OR
- San Francisco Municipal Transportation Authority
- Seattle Economic Development Fund
- Community Capital Development
- TexPIRG
- The Fair Housing Council of Central New York
- The Loan Fund, Albuquerque NM
- Third Reconstruction Institute NC
- Vermont PIRG
- Village Capital Corporation, Cleveland OH
- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty - Florida
- WashPIRG
- Westchester Residential Opportunities Inc.
- Wigamig Owners Loan Fund, Inc., Lac du Flambeau WI
- WISPIRG

Small Businesses

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Environmental Planning
- Hayden & Craig, PLLC
- Mid City Animal Hospital, Pheonix AZ
- UNET