WHO IS TOO BIG TO FAIL? GAO'S ASSESSMENT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL AND THE OFFICE OF FINANCIAL RESEARCH

HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

MARCH 14, 2013

Printed for the use of the Committee on Financial Services

Serial No. 113–7

U.S. GOVERNMENT PRINTING OFFICE

80–873 PDF WASHINGTON : 2013

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

HOUSE COMMITTEE ON FINANCIAL SERVICES

JEB HENSARLING, Texas, *Chairman*

GARY G. MILLER, California, *Vice Chairman*
SPENCER BACHUS, Alabama, *Chairman Emeritus*
PETER T. KING, New York
EDWARD R. ROYCE, California
FRANK D. LUCAS, Oklahoma
SHELLEY MOORE CAPITO, West Virginia
SCOTT GARRETT, New Jersey
RANDY NEUGEBAUER, Texas
PATRICK T. McHENRY, North Carolina
JOHN CAMPBELL, California
MICHELE BACHMANN, Minnesota
KEVIN McCARTHY, California
STEVAN PEARCE, New Mexico
BILL POSEY, Florida
MICHAEL G. FITZPATRICK, Pennsylvania
LYNN A. WESTMORELAND, Georgia
BLAINE LUETKEMEYER, Missouri
BILL HUIZENGA, Michigan
SEAN P. DUFFY, Wisconsin
ROBERT HURT, Virginia
MICHAEL G. GRIMM, New York
STEVE STIVERS, Ohio
STEPHEN LEE FINCHER, Tennessee
MARLIN A. STUTZMAN, Indiana
MICK MULVANEY, South Carolina
RANDY HULTGREN, Illinois
DENNIS A. ROSS, Florida
ROBERT PITTENGER, North Carolina
ANN WAGNER, Missouri
ANDY BARR, Kentucky
TOM COTTON, Arkansas

MAXINE WATERS, California, *Ranking Member*
CAROLYN B. MALONEY, New York
NYDIA M. VELÁZQUEZ, New York
MELVIN L. WATT, North Carolina
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
MICHAEL E. CAPUANO, Massachusetts
RUBÉN HINOJOSA, Texas
WM. LACY CLAY, Missouri
CAROLYN McCARTHY, New York
STEPHEN F. LYNCH, Massachusetts
DAVID SCOTT, Georgia
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
GWEN MOORE, Wisconsin
KEITH ELLISON, Minnesota
ED PERLMUTTER, Colorado
JAMES A. HIMES, Connecticut
GARY C. PETERS, Michigan
JOHN C. CARNEY, Jr., Delaware
TERRI A. SEWELL, Alabama
BILL FOSTER, Illinois
DANIEL T. KILDEE, Michigan
PATRICK MURPHY, Florida
JOHN K. DELANEY, Maryland
KYRSTEN SINEMA, Arizona
JOYCE BEATTY, Ohio
DENNY HECK, Washington

SHANNON McGAHN, *Staff Director*
JAMES H. CLINGER, *Chief Counsel*

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

PATRICK T. MCHENRY, North Carolina, *Chairman*

MICHAEL G. FITZPATRICK, Pennsylvania, *Vice Chairman*
PETER T. KING, New York
MICHELE BACHMANN, Minnesota
SEAN P. DUFFY, Wisconsin
MICHAEL G. GRIMM, New York
STEPHEN LEE FINCHER, Tennessee
RANDY HULTGREN, Illinois
DENNIS A. ROSS, Florida
ANN WAGNER, Missouri
ANDY BARR, Kentucky

AL GREEN, Texas, *Ranking Member*
EMANUEL CLEAVER, Missouri
KEITH ELLISON, Minnesota
ED PERLMUTTER, Colorado
CAROLYN B. MALONEY, New York
JOHN K. DELANEY, Maryland
KYRSTEN SINEMA, Arizona
JOYCE BEATTY, Ohio
DENNY HECK, Washington

CONTENTS

WHO IS TOO BIG TO FAIL? GAO'S ASSESSMENT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL AND THE OFFICE OF FINANCIAL RESEARCH

Thursday, March 14, 2013

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2128, Rayburn House Office Building, Hon. Patrick McHenry [chairman of the subcommittee] presiding.

Members present: Representatives McHenry, Fitzpatrick, Duffy, Grimm, Fincher, Hultgren, Ross, Wagner, Barr; Green, Cleaver, Ellison, Perlmutter, Maloney, Delaney, Sinema, Beatty, and Heck.

Ex officio present: Representatives Bachus and Waters.

Also present: Representative Garrett.

Chairman MCHENRY. The subcommittee will come to order.

Without objection, the Chair is authorized to declare a recess of the committee at any time.

This hearing today of the Subcommittee on Oversight and Investigations is entitled, "Who is Too Big to Fail? GAO's Assessment of the Financial Stability Oversight Council and the Office of Financial Research." It is the first meeting of this subcommittee in this Congress. I want to welcome the new ranking member of this subcommittee, Mr. Green of Texas. We both came in, in the same class, and it is an honor that we have risen together.

Today, we have distinguished witnesses, and after we recognize Members for opening statements, we will introduce the witnesses.

I now recognize myself for 5 minutes for the purpose of an opening statement. With that, you can start the clock.

In the summer of 2009, a year before the passage of the Dodd-Frank Act, President Obama announced his vision of financial regulatory reform. From the East Room of the White House he described a Council that would, "bring together regulators across markets to coordinate and share information, to identify gaps in regulation, and to tackle issues that don't fit neatly into an organizational chart."

He said, "We are going to bring everyone together to take a broader view and a longer view to solve problems in oversight before they become a crisis." This was a moment where the urgency of passing financial regulatory reform and these necessary changes became very urgent in order to prevent another crisis.

Two and a half years after the enactment of Dodd-Frank, however, fewer than half of the mandated rules have been finalized. In fact, significant pieces of Dodd-Frank have yet to be promulgated, such as the Volcker Rule, the over-the-counter-derivatives regulation, the Qualified Residential Mortgage (QRM) rule, and the definition and designation of systemically significant non-bank financial companies.

Granted, Dodd-Frank issued a huge mandate requiring collaboration and consistency across several agencies, but there was a promise made in the creation of the Financial Stability Oversight Council (FSOC). It was a promise of coordination and an effort to thwart a future crisis.

However, after reviewing the GAO audit, the GAO being responsible for overseeing the Executive Branch putting best practices and principles like private enterprises do with hiring consultants, the GAO is our consultant to review that and they do a yeoman's task of that. The GAO audit of the Council and the Office of Financial Research (OFR) indicates that these entities are far from delivering on that promise made by the President over 4 years ago.

First, GAO's examination of the Council's transparency policies and its process to designate non-bank financial institutions for supervision by the Federal Reserve illustrates the fact that it has not provided the marketplace with a clear, rules-based framework within which to work.

Second, by examining FSOC's efforts to coordinate regulatory action among agencies and to identify systemic risks, including OFR's efforts in aid of those functions, it seems that neither of these agencies are presently equipped to discover potential future threats to the financial system and to proactively mitigate them. I find it especially disconcerting that after 2½ years, GAO has found that the Council lacks systemic processes to identify future threats to the financial system in its annual reports; that it fails to distinguish future from current threats; and that it has failed to prioritize those threats that it has identified.

I think it is important to point out that as a part of the GAO review process, the entity under review is given 60 days prior to publication of the report to issue a response letter addressing the GAO's findings. This is what it does with all agencies across the government.

I thought it interesting that after 60 days, the response letter included in this report came from Assistant Secretary of the Treasury Mary Miller, acting on behalf of the Treasury Secretary, and not as an official acting on behalf of the Council itself.

This begs the question: If it is not even possible for the Council, at the Council level, to come to some level of consensus and agreement on a GAO report that is 63 pages long, how exactly do we expect the Council to coordinate actions across these existing regulators, and to act nimbly in anticipating systemic-wide financial threats?

The GAO has offered 10 recommendations in its review of the Financial Stability Oversight Council and the Office of Financial Research. I look forward to hearing from today's witnesses on whether it is possible for the OFR and FSOC to work collaboratively with the institutions that currently exist. It is clear at the outset of reading the report that the FSOC, as currently designed, isn't getting the job done.

So with that, I recognize for 5 minutes the gentleman from Texas, Mr. Green.

Mr. GREEN. Thank you, Mr. Chairman.

And this is my first opportunity to sit as ranking member. I think it appropriate that I take this opportunity to thank the many persons who made it possible for me to have this opportunity, and I want to assure all that I take this opportunity seriously.

And I also want to let those who are consumers know that I understand that consumers have rights, and those who are in the financial services community understand that I am very much aware that members of the financial services community have needs. And it is our responsibility, our duty, to balance the needs and the rights, the rights of consumers and the needs of those in the financial services community. And I am honored to have this opportunity to do so.

I also want to thank the chairman.

Mr. Chairman, thank you so much for the amiable, amicable way that we have been able to work thus far. For those who may be interested, he and I had dinner together. It was most enjoyable, I must tell you. And we plan to have dinner again, assuming that our schedules can match up, and I believe that we can do this.

Chairman MCHENRY. And I certainly appreciate you purchasing the dinner as well.

Mr. GREEN. Thank you.

Chairman MCHENRY. It was very kind of you, and I will buy next time.

Mr. GREEN. This is why we are having dinner again.

I also would like to thank you, Mr. Chairman, for your opening statement, and the sense of while you and I may not agree in our opening statements, you have stayed to the topic that you called to my attention for this hearing today. And I think it is exceedingly important that we do our very best to stay on target, stay on focus.

If we do this, while I am sure this hearing will be exciting to a good many of us, it may be boring to a lot of other people, because it really deals with a report that we have received from GAO, which contains recommendations. And we understand that a newly instituted organization of the magnitude and size of FSOC has to have time to get up to speed so that it can work efficaciously.

The truth be told, if you go back to 1933 and you look at the FDIC, which is probably the forerunner to what we have today, it is a quite similar paradigm. If you go back, you will find that it took years for the FDIC to get up and running to the extent that it was as effective as it ultimately has been. And it has been quite effective.

So today, we have this opportunity to look at FSOC. We will also look at the Office of Financial Research, and we will look at the recommendations that have been made. I am going to ask my colleagues to do as best as we can to pay as much attention to what is being said and to take seriously the recommendations of GAO.

But I am also going to look closely at what FSOC and the Office of Financial Research have by way of responses.

I have had an opportunity to peruse the report and I don't find anything in that report which is exceedingly detrimental. The truth is, they have made some recommendations that we have to take seriously. And I look forward to our working with the two entities and with the other members of this committee to make sure that we find a good way to move forward with an institution that is dearly needed for the benefit of consumers and the financial services community.

With a minute and 28 seconds left, let me just share one final thought. These are not easy times, they are not the worst of times, and they are not the best of times. But these are the times that will enable persons who mean well and who want to work across lines to work together.

I am going to do all that I can to work with the chairman and members across lines so that we can work together for the benefit of the American people. While we may have opinions that will differ, it is my belief that there is so much more that we can agree on and we ought to try to find the things that we agree on and work together.

With that, I will yield back the balance of my time, Mr. Chairman. And thank you very much for convening the hearing.

Chairman MCHENRY. I thank the ranking member.

The Chair will now recognize for 2 minutes the vice chairman of the subcommittee, the gentleman from Pennsylvania, Mr. Fitzpatrick.

Mr. FITZPATRICK. Thank you, Mr. Chairman. And I look forward to the panel discussion here this morning.

I look forward to learning more about the steps that FSOC and the Office Of Financial Research plan to take to increase transparency. Transparency is a pillar of representational government. And the important work of the FSOC should be submitted to vigorous public scrutiny, so we expect to see how we can all improve in that area.

I am also concerned about the FSOC's expansive authority to designate non-bank institutions as systemically important financial institutions (SIFI). A SIFI designation is likely to have affects on the markets and the economy as a whole, but the GAO report states that the FSOC has no plans to examine that impact. I hope that they will quickly correct course and adopt policies and procedures to measure the impact of their designations.

And finally, I plan to ask the witnesses about coordination between the FSOC and its member agencies. Although the GAO report found that collaboration has been lacking, I actually find it troubling that the FSOC appears to be inserting itself into deliberations at the SEC with regards to money market funds. If an agency is continuing to consider a matter and it has the expertise to give it proper contemplation, then I question the need to have yet another agency subvert that process. So I look forward to the testimony in considering the answers to some of these questions. And I yield back.

Chairman MCHENRY. I thank the gentleman.

Mrs. Maloney of New York is recognized for 2 minutes.

Mrs. MALONEY. Thank you, Mr. Chairman, and thank you, Ranking Member Green.

And welcome to the witnesses. I thank you all for your service.

The Financial Stability Oversight Council and the Office Of Financial Research were two key pillars of the Dodd-Frank reforms that we passed and the President signed into law. They are a direct result of the work we did to fill in the gaping holes in regulatory oversight that led to an estimated $22 trillion in losses to the U.S. economy.

They are a response to the realization that our regulators did not have the ability to look across the financial system and to detect financial instability before it ballooned out of total control.

The FSOC is simply a council of regulators who meet and coordinate regulatory and oversight efforts, and it is dependent upon data that it receives from the Office of Financial Research to help them do this job.

The OFR was created to spot trends within the financial services industry through the collection and analysis of near-time financial industry data. Dodd-Frank details specific information that the office is supposed to collect from the financial services institutions. The language was specific in saying, “The office shall collect data using the same protocols the industry does.”

The reasoning behind this was to get the office up and running in the quickest possible fashion so that we can continually assess the overall health of the U.S. financial markets, spot trends, or an oversaturation of a particular financial instrument—we all remember the credit default swaps. And it was supposed to proactively alert and work with the effective brokers in an orderly fashion, proactively dealing with any problems that may arise so that that we don’t experience another run on the markets and near failure, like we had in 2008.

So, I look forward to your testimony and your responses to the GAO report. Thank you.

My time is up.

Chairman MCHENRY. The gentleman from Missouri is recognized for 3 minutes.

Mr. Cleaver?

Mr. CLEAVER. Thank you, Mr. Chairman.

I appreciate you and the ranking member for calling this hearing together.

And I would like to join my colleagues in welcoming the witnesses to this Subcommittee on Oversight and Investigations hearing on the Financial Stability Oversight Council and the Office Of Financial Research today. I look forward to this hearing. I look forward to hearing your comments.

Both FSOC and OFR are a relatively new part of our regulatory framework created by Dodd-Frank. The Council provides, for the first time, comprehensive monitoring to assure the stability of our Nation’s financial system.

Years without accountability for Wall Street and big banks brought us the worst financial crisis since the Great Depression: the loss of 8 million jobs; failed businesses; a drop in housing prices; and wiped-out personal savings.

The process we had in place for previous problems was insufficient, to say the least. The Council is charged with nothing short of seeing the next crisis coming down the road and helping regulators find ways to stop it from arriving at our doorstep.

Together with OFR, the Council identifies threats to the financial stability of the United States, promotes market discipline, and responds to emerging risk to the stability of the United States' financial system.

Today's testimony reminds us that FSOC and OFR can improve and augment the existing efforts. Key FSOC missions—to identify risk and respond to emerging threats to financial stability—are, at a fundamental level, inherently challenging, in part because risks to financial stability do not develop in the same way in successive crises.

The GAO has identified several areas in which these key organizations can better fulfill their mission.

I look forward to hearing more from the GAO, the FSOC, and the OFR today as we work together to ensure fulfilling our mission.

Members of the panel, thank you for your testimony today.

I yield back.

Chairman MCHENRY. The gentleman from Florida, Mr. Ross, is recognized for 3 minutes.

Mr. ROSS. Thank you, Mr. Chairman.

And being from Florida, where sunshine is very important, sunshine and the—arena has to do with transparency. And I note that the GAO report found that the public cannot easily monitor FSOC's progress toward fulfilling its statutory purpose because it does not maintain sufficiently detailed records of its meetings and has not implemented a satisfactory policy to disclose those records.

For example, FSOC's many important committees, which consider policy matters before presenting such matters to FSOC's council of voting and non-voting members, keep neither transcripts of their meetings nor minutes.

The Council also does not transcribe its meetings, though it does keep certain meeting minutes. However, the minutes do not provide meaningful insight into the perspectives and insights shared at Council meetings due to vagueness.

In addition, the Council does not publish a public agenda prior to each meeting, and FSOC's one-and-a-half-page transparency policy is completely silent on the matter of public notice.

Finally, the public generally cannot monitor the Council's activities in person because it has historically conducted approximately two-thirds of its meetings in private in executive session, even though it is required to hold public meetings whenever possible.

The Council's meeting minutes do not provide a basis to determine whether the Council met in executive session consistent with FSOC's transparent policies.

With that, I yield back, Mr. Chairman.

Chairman MCHENRY. I thank the gentleman.

We will now welcome our distinguished set of witnesses for today.

We have, for his first appearance on the House side of the Capitol, the Honorable Richard Berner, the Director of the Office of Financial Research (OFR). Prior to his confirmation as the OFR Director, Dr. Berner served as a Counselor to the Secretary of the Treasury with a responsibility for standing up the OFR. He has held various positions in the public and private sector and on the public sector on the research staff of the Federal Reserve Board.

He has a Ph.D. from the University of Pennsylvania, and has an undergraduate degree from a place called Harvard.

Thank you, Dr. Berner, for being here.

Mr. Amias Gerety is the Deputy Assistant Secretary for the Financial Stability Oversight Council. He previously worked for private consulting firms, as well as a Washington group, the Center for American Progress. He also has an undergraduate degree from Harvard University.

And Ms. Nicole Clowers is the Director of the Financial Markets and Community Investment Division of the Government Accountability Office. She has been with the GAO for 14 years. She has a bachelor's degree from Virginia Tech and a master's in public administration from the University of Georgia—thank you for being the southern representative on the panel—and is a 2009 recipient of the Arthur S. Flemming Award for outstanding public service.

Thank you all for your service to our people and within our government.

Each of you will be recognized for 5 minutes. We have a lighting system that is very similar to what you see on the roads today. I hope you will recognize these lights more than we do those other lights on the public roads. There will be no red light cameras, but we ask you to summarize your statements. And for the record, your opening statements will be included in the record.

And like the roads, green means go, yellow means hurry up, and red means stop, so you will have 1 minute to go when the yellow light comes on.

With that, we will begin with Dr. Berner.

STATEMENT OF THE HONORABLE RICHARD BERNER, DIRECTOR, OFFICE OF FINANCIAL RESEARCH, U.S. DEPARTMENT OF THE TREASURY

Mr. BERNER. Chairman McHenry, Ranking Member Green, and members of the subcommittee, thank you for the opportunity to appear today on behalf of the Office Of Financial Research.

In my remarks this morning, I will provide an overview of the OFR's major accomplishments and priorities. I will also describe actions the OFR has taken in response to a report by the Government Accountability Office in September 2012.

My written testimony provides more details on the significant progress that the OFR has made in fulfilling its primary data and research responsibilities, as well as in enhancing its transparency and accountability.

As you know, Congress created the OFR through the Dodd-Frank Act to improve the quality of financial data available to policymakers, and to develop better tools and analyses to understand the risks in the financial system.

The OFR supports the activities of the Financial Stability Oversight Council—also known as the Council. The OFR, the Council, and Council member organizations have complementary mandates, and our different perspectives are mutually beneficial. They enable us to conduct comprehensive assessment and monitoring of threats to financial stability while avoiding duplication through regular collaboration and coordination.

The OFR has built a new organization from the ground up, assembling a talented workforce and developing a technology infrastructure with the highest level of security. The Office is still a young organization, but it is now delivering on its mission in concrete ways.

For example, the OFR is reporting regularly to the Council through its Systemic Risk Committee on developments in financial markets and activities, on financial stability measures, and on macroeconomic indicators. The OFR is also providing data and analysis to inform the work of the Council's non-bank designation committee, including analysis of the asset management industry.

And the OFR is providing data and staff support for the Council's 2013 annual report. Last July, the OFR published its first annual report, and will release its second one later this year.

Many of the OFR's early accomplishments involve collaboration on research and on data standards. In addition to its mandate to serve the needs of the Council, the OFR is required by statute to cultivate a network of academics, researchers, data scientists, and others to enrich and expand OFR capabilities.

We are collaborating with the research and data communities through our research working paper series, our seminars and conferences, and our financial research advisory committee.

We are also collaborating internationally on data standards which improve the quality of financial data and help reduce the reporting burden for industry. These standards facilitate our analysis of interconnections among financial firms and their counterparties, and help us to understand the transmission and amplification of stress across the financial system. In particular, the OFR has played a central role in the international initiative to establish a global legal entity identifier, a code that uniquely identifies parties to financial transactions and links their basic business card information.

As we pursue the OFR's agenda, we are committed to the highest level of transparency and accountability to the Congress and the public. We strongly support the GAO's important oversight function and appreciate its constructive work in conducting its review.

In response to the GAO report, the OFR has improved its communication with the public, further developed its strategic planning and performance management, and worked with the Council to assure a coordinated approach to achieving our shared mission.

Chairman McHenry and other members of the subcommittee, thank you again for the opportunity to appear today. We welcome the oversight of this subcommittee, and we look forward to working with you and your staff to continue the critical task of promoting the stability of this Nation's financial system.

I would be happy to answer your questions.

[The prepared statement of Dr. Berner can be found on page 58 of the appendix.]

Chairman MCHENRY. Thank you, Dr. Berner.

Mr. Gerety?

STATEMENT OF AMIAS M. GERETY, DEPUTY ASSISTANT SECRETARY, FINANCIAL STABILITY OVERSIGHT COUNCIL, U.S. DEPARTMENT OF THE TREASURY

Mr. GERETY. Thank you.

Chairman McHenry, Ranking Member Green, and members of the subcommittee, thank you for the opportunity to appear here today to discuss the Financial Stability Oversight Council's role in implementing key reforms of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

This month marks the 5-year anniversary of the failure of Bear Stearns and the start of the financial crisis, and the biggest recession our country had experienced since the Great Depression. Those events in turn led to President Obama signing the most comprehensive set of financial reforms in 80 years into law in the summer of 2010.

One of the Dodd-Frank's key reforms was the creation of the Financial Stability Oversight Council, the first Federal entity vested with clear responsibility for comprehensive monitoring of the stability of our Nation's financial system.

The Council's statutory mission is to identify risks to the financial stability of the United States, promote market discipline, and respond to emerging threats to the stability of the U.S. financial system. Since its creation, the Council has worked to fulfill this mission and promote coordination among its members.

To that end, one of the Council's first actions was the development of an organizational structure that fostered open and frank discussion, collaboration, and coordination. Through the creation of standing interagency staff committees, the Council's work draws upon the collective policy and supervisory expertise of its members.

The Council has convened 28 times, has published 2 annual reports and 6 additional studies or reports, and has designated 8 financial market utilities as systemically important.

The Council has also played an active role in coordinating the regulatory response to significant events, such as Superstorm Sandy. The Council is also firmly committed to operating in an open and transparent manner. At its first meeting, the Council adopted a transparency policy which provides that Council meetings will be open to the public whenever possible and not less than twice each year. The Council has had 9 open sessions in its first 2½ years.

The Council's annual report is also a key accountability mechanism that provides transparency to the public and to Congress about the Council's activities over the previous year and its forward-looking assessment of the Council's priorities.

The Council's rulemakings on designations of non-bank financial companies and financial market utilities also demonstrate its commitment to transparency. Although these rules were not statutorily required, the Council believed it was important to provide the public with insight into how the Council intended to evaluate these potential designations.

The Council is now in the final stages of evaluating an initial set of non-bank financial companies for a potential designation which will subject them to enhanced prudential standards and supervision by the Federal reserve, closing an important regulatory gap.

During the past 2½ years, the Council staff has also been pleased to work with a number of teams from the Government Accountability Office as they have conducted multiple reviews of the Council's activities.

The GAO report published in September 2012 highlighted a number of examples of how both the Council and the OFR have demonstrated transparency and accountability while carrying out their respective missions to safeguard the stability of our financial system.

The reports also made a number of recommendations to further enhance the progress that each organization has made in these important areas. The Council and the OFR provided a joint response to Congress and the GAO outlining the actions taken and planned in response to each recommendation, described in more detail in my full written testimony.

The Council remains firmly committed to promoting transparency and accountability in connection with its activities, and takes the GAO's recommendations seriously.

I appreciate the invitation to appear here to provide this update on the Council's responses to the GAO report, and I look forward to your questions.

Thank you.

[The prepared statement of Mr. Gerety can be found on page 89 of the appendix.]

Chairman MCHENRY. Ms. Clowers, you are recognized for 5 minutes.

STATEMENT OF A. NICOLE CLOWERS, DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Ms. CLOWERS. Good morning, Chairman McHenry, Ranking Member Green, and members of the subcommittee. Thank you for the opportunity to be here today to discuss our work on FSOC and OFR.

As you know, the Act established FSOC and OFR to address regulatory weaknesses highlighted by the recent financial crisis, namely the lack of an agency responsible for monitoring risk across the financial system and a shortage of timely information to facilitate that oversight.

Although Congress set up some accountability mechanisms for FSOC and OFR, Members of Congress have questioned whether more needs to be done to ensure FSOC and OFR use their authorities as Congress intended.

In my comments today, I will discuss three issues: first, the challenges that FSOC and OFR face in carrying out their missions; second, the steps the entities have taken to carry out their responsibilities; and third, GAO's recommendations to FSOC and OFR. My comments are based on our September 2012 report.

First, FSOC and OFR face several challenges as they work to achieve their missions, namely the Dodd-Frank Act left most of the fragmented regulatory structure in place. As a result, FSOC's ability to provide a more comprehensive view of the threats to financial stability hinges on the collaboration among its many members, almost all of whom have their own independent regulatory viewpoint.

Second, despite this and other challenges, FSOC and OFR have taken steps to carry out their responsibilities. For example, FSOC established multiple standing committees to carry out the business of the Council. One of the committees, the Systemic Risk Committee, is responsible for monitoring risk for the Council. OFR participates on this committee. OFR is also building capacity to monitor threats to financial stability.

The third and final topic that I would like to discuss today is the recommendations from our September report. We made 10 recommendations to FSOC and OFR, and I would like to briefly highlight a few of those recommendations that are related to the agencies' core missions: transparency; and accountability.

To better position FSOC to achieve its core missions, we recommended that FSOC develop a systematic approach to help identify potential threats to financial stability. While the Systemic Risk Committee may help FSOC analyze known risk, it does not take full advantage of member agency resources to identify new threats.

In addition, we found that FSOC does not have a process for consistently identifying new threats, separating them from well-known threats, or prioritizing them. As a result, policymakers and market participants do not have the information they need to develop effective and timely responses. Therefore, we recommended that FSOC develop more systematic, forward-looking approaches for reporting on emerging threats.

Related to transparency, we recommended, among other things, that FSOC keep detailed records of closed-door meetings. While no specific level of detail is required in FSOC minutes, the limited documentation of the discussions makes it difficult to assess FSOC's performance. For instance, the meeting minutes typically describe agenda items for the meetings, and information on the presenters for each agenda item, but lack additional detail. As a result, the Congress and the public receive limited information on the FSOC's decision-making.

Finally, related to accountability, the Congress intended that the designation of the financial companies for enhanced supervision would lead to greater financial stability. The designations will likely have other significant benefits and costs for the designated companies as well as potentially the Nation's economy.

Given these potential impacts, we recommended that FSOC should comprehensively evaluate whether the designations, once made, are having their intended impact.

In conclusion, Mr. Chairman, although fully addressing our recommendations may take time, doing so will help FSOC and OFR shed more light on their decision-making and allow the Congress to hold them accountable for results.

Furthermore, addressing our recommendations can help FSOC and OFR to enhance collaboration among its FSOC members, which is critical to their ability to achieve their missions.

We will continue to monitor the entities' progress in implementing our recommendations, and we stand ready to assist Congress as it continues its oversight.

Chairman McHenry, Ranking Member Green, and members of the subcommittee, this completes my prepared statement. I would be happy to answer questions at the appropriate time.

Thank you.

[The prepared statement of Ms. Clowers can be found on page 65 of the appendix.]

Chairman MCHENRY. Thank you all for your testimony.

I now recognize myself for 5 minutes.

The GAO report was issued in September of last year. The FSOC has met 8 times since then.

Mr. Gerety, has the GAO report been discussed at the Council level?

Mr. GERETY. Thank you, Mr. Chairman.

The GAO report has been discussed at length among the staff committees, in particular among the deputies' committee, but has not been discussed by the Council members itself, as our minutes suggested. The Council is aware of the oversight, and so we presented on that topic more generally, rather than the specifics of this report.

Chairman MCHENRY. At the subcommittee level. How many subcommittees are there?

Mr. GERETY. In particular, the deputies' committee has discussed this topic as it has discussed a significant number of topics before this.

Chairman MCHENRY. Is there a transcript I could find of those discussions?

Mr. GERETY. The Council does not keep transcripts of staff meetings.

Chairman MCHENRY. Is there an agenda of those staff meetings that I could find?

Mr. GERETY. Congressman, the Council endeavors to—

Chairman MCHENRY. Is the answer no?

Mr. GERETY. We do not publish agendas of staff meetings.

Chairman MCHENRY. Okay. Now, at the full FSOC committee, there are 10 recommendations from the GAO on a very important agency. Two and a half years after Dodd-Frank was passed, we still don't have the ability, we have the minutes that are typically two to five pages, one is actually a page-and-a-half if you include the number of attendees. Do you have any intention of providing transcripts of the FSOC meeting?

Mr. GERETY. Congressman, I can't speak on behalf of the Council. The Council is actually made up of its members and—

Chairman MCHENRY. Certainly. But you are here on behalf of the Chairman of that Council at the direction of the FSOC.

Mr. GERETY. That is correct. What I can say is with respect to the issue of transparency, and I think that the recommendations that the GAO made are ones that we take seriously, and we have—

Chairman MCHENRY. How do we know that you take them seriously if we have no documentation you have had these discussions?

Mr. GERETY. Sir, for example, in the Council's letter to the Congress and to the GAO, we talk about the steps already taken and additional steps. For example, one of the GAO's recommendations was about the transparency of our Web site. In December of 2012, the Council made a number of steps to improve that Web site to make it more navigable, to provide updates that people can sign up for e-mail updates based on—

Chairman McHENRY. I appreciate that. That is nice. And that is a nice step. To your point about the Mary Miller letter on behalf of the Treasury Secretary, the Assistant Secretary of the Treasury, the response to the GAO report, that 60 days that I acknowledged in my opening statement, I find it peculiar that it was on behalf of the Treasury Secretary. Was there a vote of the FSOC for this response by a Treasury official?

Mr. GERETY. Sir, this response was prepared in consultation with all of the FSOC members.

Chairman McHENRY. Okay. Where can we find documentation of that consultation?

Mr. GERETY. Congressman, the consultation process is consistent with a very collaborative and open framework among the Council members, so the natural process of course is to circulate drafts, collect comments, and then to produce that.

Chairman McHENRY. And this is what the GAO has designated as a problem area within the 10 recommendations, that there is not transparency within FSOC to the public or the regulated communities. This is what is so deeply disturbing about the intention of FSOC to mitigate the next financial crisis when you can't even disclose the meeting minutes, like the Federal Reserve does, the transcripts of your meetings. When the Federal Reserve is a greater discloser of information than you at the FSOC, I think that is a major concern.

Now, Ms. Clowers, is it fairly typical that the regulated agency, when you give a report, actually have consultation on your report?

Ms. CLOWERS. Yes. When we provide a report for comment, typically the agencies will respond within 30 days. And in doing so, they will have consulted with people within their agency.

Chairman McHENRY. Does the fact that a Treasury official has to respond for the FSOC raise some of your concerns within your report?

Ms. CLOWERS. Who signs the report can vary by agency and the topic at hand. So the fact that Ms. Miller signed for the chairperson is not that unusual. But I think that it does reflect some of the issues we raised in the report in terms of the Council and the decision-making, trying to reach consensus on certain issues.

Chairman McHENRY. Okay. Thank you for your testimony.

This highlights the fact that the current FSOC measure of disclosure is simply not working, as the GAO report highlights and as my questions illuminate.

I now recognize the ranking member for 5 minutes.

Mr. GREEN. It is our tradition to recognize the ranking member of the full committee whenever the ranking member is present. So I will yield to the ranking member of the full committee, Ms. Waters.

Ms. WATERS. Thank you very much, Mr. Green.

FSOC and OFR are central to the overarching objectives of Wall Street reform, and I want to have you further expound on the work that your standing committees are undertaking to assist in the Council's goals and objectives.

How do these committees collaborate and facilitate communication between individual member agencies?

Mr. GERETY. Thank you, Congresswoman.

I think this is an important topic, and one of the first actions of the Council was to create an open and collaborate framework through these interagency staff committees. In particular, the FSOC's deputies' committee meets biweekly. It covers a range of topics. Most importantly, it covers topics related to coordination, the Council's agenda, and how to address issues before the Council.

In addition, the deputies' committee helps facilitate the work of the other staff committees that are dedicated to particular topics. The Systemic Risk Committee—which we have already mentioned this morning—meets monthly and creates a framework for all of the supervisory and market expertise of the regulatory members of the FSOC. The non-voting members come together and discuss risks to the financial system, trends in financial markets, and macroeconomic indicators, and use that process to develop and understand potential threats to financial stability. Those processes obviously build into a really important accountability document, which is the FSOC's annual report. The FSOC's annual report is a comprehensive document. It looks at significant financial market developments, significant regulatory developments, and it tries to identify potential emerging threats and to make recommendations.

In addition, each of the members of the Council is required to sign a statement to Congress identifying the recommendations that they believe are necessary to promote our financial stability. And over the past 2 years, each of those members has signed a statement, along with the FSOC's annual report, saying that those recommendations are the most important to promote financial stability.

Ms. WATERS. The GAO expressed concerns with FSOC and OFR's lack of transparency in its decision-making process. While the GAO report makes good recommendations, I am concerned about how FSOC will balance transparency with its responsibility to maintain the confidentiality of market-sensitive information.

Can you discuss how FSOC has attempted to strike the right balance?

Mr. GERETY. Yes, Congresswoman.

I think this is an important issue, which is the balance between the confidentiality of supervisory information, the confidentiality of market sensitive analysis, and the importance of being transparent and accountable. I think the GAO has recommended a number of areas where we can improve that transparency and accountability.

I think we have already taken some steps, and I think on the basis of this conversation and the continuing dialogue with the GAO, there are certainly more steps that we can consider over time and revisit that transparency and policy over time to make sure that balance is struck correctly.

However, I would also note that on a number of the topics that have been discussed here today, there has been tremendous pressure on the other direction. For instance, in the non-bank financial company designations process, the companies have expressed, and market participants have expressed deep concern about the nature of confidential information and the nature of those deliberations.

And so in striking that balance the Council has always tried to strive to protect confidential supervisory information so that we have an open dialogue within the regulatory community, while also publishing and getting public input on decisions made by the Council through a notice and comment process, which we have done in significant studies in the past.

Ms. WATERS. Thank you very much.

In testimony before the Senate, Fed Governor Dan Tarullo expressed concerns with areas of systemic risk that remain a challenge for the Fed on financial stability. Can you discuss OFR's research and analysis of the tri-party repo market, as well as current proposals to address the clearing of banks' significant exposure to credit risk?

Mr. BERNER. Thank you, Congresswoman.

That is an important issue, our work on the tri-party repo market and on short-term funding markets in general are extremely important for the analysis of financial stability. Those issues have been discussed at length in both FSOC annual reports and in our OFR annual report that was published in July of last year.

We continue to do work on those issues. As you know, steps have already been taken to mitigate some of the risks in the tri-party market. In the United States, however, there are three parts to the repo market. And the other two parts—namely the bilateral or so-called DVP market, and the GTF market—are less widely discussed, but they may contain their own risks.

In seeking to analyze and to measure the risks in those markets, we are working with other Council member agencies, in this case specifically the Federal Reserve, to improve the quality and scope of data on those markets, to analyze the data that are available, which as far as we know have not yet been analyzed. And—

Chairman MCHENRY. The gentlelady's time has expired.

If you can summarize?

Mr. BERNER. Sure. And we plan to do further work in that area for the benefit of the Council and for the Fed.

Ms. WATERS. Thank you very much, Mr. Chairman. I yield back.

Chairman MCHENRY. Let the record reflect that the time was not appropriately recognized. This was the gentlelady's time, not the ranking member of the subcommittee's time. I just want that to be reflected, and without objection, that is so ordered.

We will now recognize the chairman emeritus of the full committee, the gentleman from Alabama, Mr. Bachus.

Mr. BACHUS. Thank you.

Director Clowers, coordinating or facilitating coordination between the agencies for rulemaking and supervision enforcement actions and reporting requirements as part of FSOC's explicit duties, if you were to assess FSOC's ability to coordinate agency rulemaking as of the time you completed your recent study, what would your assessment be?

Ms. CLOWERS. This was related to one of the recommendations that we did make for FSOC, that we have seen steps that they have taken to promote collaboration and coordination, including development of the road map and the consultation framework. But we thought more could be done.

And in fact, in 2011 we recommended that FSOC develop a formal policy that would outline when coordination should take place, who should be involved, and what to do when you have conflicting views.

We think that there is a greater role for FSOC to play in coordinating the many Dodd-Frank rulemakings. FSOC has told us that they lack the authority to force members to coordinate. The regulators have also expressed some concerns about maintaining their independence.

But we think that the balance can be struck in both maintaining a regulator's independence and still have FSOC play a greater role in this area.

Mr. BACHUS. All right.

Deputy Secretary, could you write to the committee and tell us what you think your lack of authority is? Because I think you will agree that coordinating between the agencies is—if you don't, you are going to have a fragmented market. And you are also going to have migration of certain activities to unregulated areas, like you had in 2006, 2007, and 2008.

Would you do that?

Mr. GERETY. Congressman, I would be glad to respond in more detail.

However, I would note that there is a distinction between the responsibilities that the Council has, which are to collaborate and coordinate across its member agencies, and the authority that it may have—

Mr. BACHUS. Yes, and I am just saying, lay out in your letter what you think your duties are, what you think you lack, and what you say that the Director has said that some of the agencies have expressed a pushback against you. We would like to know the specifics.

Mr. GERETY. Importantly, the Dodd-Frank Act, when creating the Council, did not change the fundamental statutory independence of the regulatory agencies that make up the Council's membership.

Mr. BACHUS. Yes, but you were actually designated by statute to coordinate that rulemaking. So just tell us what your limitations are, what you need, or why you can't.

A follow up to that is if they fail to coordinate rulemaking, both internally with domestic regulators and with foreign regulators, and I know the E.U. has expressed some real concerns in this regard, could that lead to disruptions in the U.S. economy? Director Clowers, for instance, with the CFTC rulemaking on derivatives, I think it has already, according to The Wall Street Journal and others, led to some fragmentation.

Ms. CLOWERS. Right. We have done a series of reports looking at the importance of coordination among agencies, both in their normal activities as well as rulemaking. And when agencies aren't appropriately coordinating, it can lead to conflicting rules, duplication, or even potential gaps.

Mr. BACHUS. Thank you.

Do you agree with that, Deputy Secretary?

Mr. GERETY. Congressman, I think the importance of coordination across the implementation of Dodd-Frank is crucially important.

I would note on the issue that you raised, it was an issue the Council takes seriously and was discussed by the Council members in December of last year.

Mr. BACHUS. Sure. And issuing no-action letters is not a solution. You understand that?

Mr. GERETY. Congressman, I think what you are referring to are actions by the CFTC.

Mr. BACHUS. Yes. But you would agree that is not what is intended?

Mr. GERETY. Congressman, I don't think I can comment on the specific regulatory actions by the CFTC. But I think the important points that you raised about the importance of regulatory coordination, both domestically and internationally, are central to the Council and to the Treasury as well.

Mr. BACHUS. Yes. Would you be willing to sit down with the subcommittee chair, Chairman McHenry, and staff and our committee Chair, and tell us what you believe we can do, or if there are failures in the Act or the statute, let us know what those are?

Mr. GERETY. Congressman, we would be glad to work with you or with your staff to talk about challenges in implementation of the Act. I think that there is a lot of good work being done and most importantly, I think there is a lot of evidence that regulators are working through the issues that you are raising.

Mr. BACHUS. Thank you.

Chairman MCHENRY. I thank the former chairman of the full committee, and I will now recognize the ranking member of the subcommittee, Mr. Green.

Mr. GREEN. Thank you, Mr. Chairman.

Let me start with our representative from GAO. You have indicated that some things "can lead to," but you did not say "have led to," nor have you said they "will lead to." And I want to use this moment to clarify, because this coordination issue is something that is important, but it is not something that has led to anything that is negative. Is this a correct statement?

Ms. CLOWERS. I would give one example of where better coordination in terms of the sequencing and timing could have been improved. Specifically, FSOC put out its rule on designating non-bank financial companies before the Federal Reserve had defined what it means to be predominantly engaged in financial activities.

And so, that is an example of where we heard from the industry this isn't helpful in terms of the sequencing.

Mr. GREEN. I understand.

But the point is that nothing has been done that has led to an adverse impact on the economy. That was what the question had to do with when you addressed it. Is this a fair statement?

Ms. CLOWERS. This is a fair statement.

Mr. GREEN. Okay.

And you have also indicated that some good things have been done with FSOC. Reiterate, if you would, some of the good things that have been done.

Ms. CLOWERS. Certainly. One example, as Mr. Gerety has talked about already, is the committee structure that FSOC set up in terms of interagency makeup of those committees and the work that gets done at the committee level.

In addition, FSOC has met all its mandated study requirements and issued two annual reports that are comprehensive and contain information for the public.

OFR has been working to stand up an agency while fulfilling its mission, which is a challenge, and they have been working to hire and retain top talent.

In addition, OFR has developed a working paper series to examine critical issues facing the Nation.

Mr. GREEN. And while you have some recommendations, is it fair to say that you did not and your report does not connote or denote any fatal flaws?

Ms. CLOWERS. We identified a number of areas where we think improvements could be made—

Mr. GREEN. I understand improvements, but you haven't identified any fatal flaws.

What I am trying to do is make the record clear as to your—you have recommendations, but you have not concluded that there are fatal flaws in this process and that they will take some time to work out the recommendations that you have called to our attention. Is this a fair statement?

Ms. CLOWERS. Yes.

Mr. GREEN. Thank you. And the truth is that with new startups the size of FSOC and OFR, it takes some time to develop systems and techniques and methodology. Is this true?

Ms. CLOWERS. Yes.

Mr. GREEN. And is it true that while you have given your recommendations, you also understand that as time progresses, they will have greater opportunities to do greater things. And when you re-examine, conceivably these things can be remedied. Is that a fair statement?

Ms. CLOWERS. We believe all the recommendations we have made could be implemented and would improve both agencies.

Mr. GREEN. Now, let me go quickly to the representative from FSOC.

You indicated that you have issued two annual reports. You have designated two entities as significantly important. And you have had nine open session meetings. Is that correct?

Mr. GERETY. That is correct.

Mr. GREEN. Can you just elaborate a little bit on how you work with the various entities to produce the work product that you have called to our attention?

Mr. GERETY. Thank you, Congressman. I think that the work products process that we have established, as Ms. Clowers identified, is primarily through interagency standing committees.

The Council has 15 members—10 voting members, 8 of whom are independent regulatory agencies, plus the Treasury Secretary and an independent member with insurance expertise. In addition, there are three members from the State regulatory community, as well as Dr. Berner and the Director of the Federal Insurance Office.

So we have a very wide diversity of views and we have benefited greatly from an open and collaborative process that runs through committees that allow all 15 members of the Council to engage, even on topics that are a little bit outside of their natural expertise.

And we think that is very important, because one of the key lessons of the crisis is that sometimes things that are happening in one area of the financial system could have impacts in other areas of the financial system.

One of the great examples of this, in terms of the Council's recent history, is in Superstorm Sandy. And what you saw is that the Council met at the principal-level 2 times in 2 days.

And what we really saw in that instance was the benefit of having Federal regulators, both securities and banking, on the same phone call together, and also the benefit of State regulators, so we were able to get the State banking commissioner perspective on the operational challenges in New York, New Jersey, and other affected areas, as well as preliminary loss estimates, both at the Federal and State levels.

I think we have seen that this open and collaborative approach allows that vast expertise of the membership of the Council to really contribute on a range of issues that come before the financial system.

Chairman MCHENRY. The gentleman's time has expired.

Mr. GREEN. Thank you, Mr. Chairman.

Chairman MCHENRY. I thank the ranking member.

Now, we will recognize the vice chairman of the subcommittee, Mr. Fitzpatrick, for 5 minutes.

Mr. FITZPATRICK. Thank you, Mr. Chairman.

As I indicated in my opening statement, the FSOC is currently considering subverting at least one lawful deliberative decision that the Security and Exchange Commission is making or is in the process of making regarding rulemaking and money market funds.

So my question is to you, Mr. Gerety—and I would ask that any of the panelists consider responding if you agree or disagree—do you believe that an FSOC designation of money market funds for enhanced Fed supervision is an appropriate and adequate alternative to the SEC changing the rules that apply to these funds?

Mr. GERETY. Congressman, I think that you raised an important issue, which the Council has discussed on a number of occasions and in its annual report, which is the question of further reforms to address structural vulnerabilities in money market funds.

I think the points that you make are important, for the following reasons: One—and the Council has recognized this repeatedly, the SEC has clear statutory and regulatory authority to address money market funds.

The second thing that I think I would highlight in the Council's actions is that the Council has worked very closely with the SEC staff and SEC Chairman Schapiro and now Chairman Walter on the consideration of these reforms.

Moreover, what the Council did last fall was not an action that would subvert the process of the SEC but rather encourage a public dialogue on the reforms that the SEC has considered and is considering.

We thought that by putting forward public recommendations consistent with Section 120 of the Dodd-Frank Act about an issue that relates specifically to money market funds from a regulatory perspective, but could have broader impacts on the financial system, we were able to get public comment, public input, and also create a more public dialogue about these reforms under consideration.

Obviously, the first choice is for the SEC to take action. That is something that the Council has made clear.

Mr. FITZPATRICK. The SEC process at this point, would you call it deliberative, the process that agency is engaged in?

Mr. GERETY. As I understand it from the conversations with SEC staff, and with Chairman Walter and Chairman Schapiro, they are engaged in collaborative and a deliberative process within the SEC.

Mr. FITZPATRICK. Certainly, it is lawful, correct?

Mr. GERETY. That is my understanding—

Mr. FITZPATRICK. And it is currently in process, isn't that right?

Mr. GERETY. That is correct.

Mr. FITZPATRICK. So is it appropriate to recommend that an agency take a particular action under Section 120 of Dodd-Frank in cases where the agency is still considering the matter and is still in deliberation?

Mr. GERETY. Under the authority in Dodd-Frank, the recommendation authority under Section 120 authorizes the Council to make recommendations to an agency when it feels that there is an issue that could pose a threat to financial stability. The proposed recommendation that the Council put out is precisely to make a proposed recommendation and to engage in a public dialogue and get public comment on that issue of concern.

Mr. FITZPATRICK. Does the FSOC have greater expertise in an area regarding SEC's deliberation more so than that latter agency?

Mr. GERETY. Congressman, as I mentioned earlier, the Council staff both at the Treasury and in other member agencies worked closely with SEC staff and with Chairman Schapiro to have the benefit of their expertise. But this issue, while directly related a particular matter of money market funds, also has broader implications for short-term funding markets and the stability of the financial system.

Mr. FITZPATRICK. Nothing further. I yield back.

Chairman MCHENRY. If the gentleman would yield?

I certainly appreciate the gentleman yielding.

So it is an intention of FSOC to make regulations that sometimes get bottled up in other regulatory—independent regulatory agencies?

Mr. GERETY. Mr. Chairman, if I may, the Council's action was to make recommendations not regulations.

Chairman MCHENRY. Okay.

So you made recommendations on money market funds. FSOC made recommendations on money market funds because the SEC could not come to what the FSOC thought was an appropriate conclusion.

Mr. GERETY. The Council's action was to make a proposed recommendation. It is an issue that has been highlighted in two previous annual reports and an issue that on which we have consulted closely with SEC staff and with Chairman Schapiro.

Chairman MCHENRY. Is this interference by the FSOC?

Mr. GERETY. The authority that I think you are referring to is a Section 120 authority. It was created by the Dodd-Frank Act. And what the essence of the authority says is that where there are issues that relate to financial stability, the Financial Stability Oversight Council should go through a public dialogue to make—

Chairman McHENRY. Is this an example of FSOC using the SIFI designation as a threat?

Mr. GERETY. Mr. Chairman, I think it is important to distinguish between two different things. One is the Section 120 authority, which the Council has done, has made a proposed recommendation, engaged in a public dialogue about further reforms to money market funds. The second thing that you are referring to is a question about how the Council may use its non-bank designation authority.

Certainly, the Council has the authority to designate any non-bank financial company whose material financial distress would pose a threat to financial stability. The Council has not decided whether to use that authority in that instance. The Council has not decided whether to use that authority in any instance at this point.

We have laid out a rulemaking process and guidance on that. And I would further say that the statute makes clear that any non-bank designations must be firm-specific rather than to the industry as a whole.

Chairman McHENRY. All right, but those two powers wouldn't be mixed? No one would mix two powers?

We will just yield to the gentleman from Missouri for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman.

Let's stay on the non-banks. I want to actually—all three of your comments, but maybe Mr. Gerety and Mr. Berner more so.

Do you believe that non-banks should be declared systemically important financial institutions, Mr. Berner?

Mr. BERNER. Congressman, thanks for your question.

It is really up to the Council to decide on this process, as Mr. Gerety indicated. That is firmly embedded in the rulemaking process for the Council.

Mr. CLEAVER. Okay. Maybe the question is—maybe we have to go back to go forward. I am thinking AIG, which is a non-bank. We sat on this committee after the failures began with Lehman Brothers and we—whether we had a lot of time to think about it or not is irrelevant at this point. I am thinking about what we did, because we thought that this was the end of the world coming when George Bush sent over his Secretary of the Treasury, Fed Chairman Bernanke, and SEC Chairman Cox, sitting right there at that table telling us what they saw coming.

So it important, at least to me, to find out whether you think there was a contagious run or whether there was a connectivity that could have rippled and continued to do devastation to the economy.

Mr. GERETY. Congressman, I think the issue that you are raising is really central to one of the authorities that was given to the Council in Dodd-Frank. I think there are three really important points to make about the non-bank designations.

First, we generally believed that the institution that posed the largest risk should be subject to the toughest standards.

Second, we have to understand that the institutions that posed such risk may or may not be structured in a way that they would be prudentially regulated. They may or may not be banks or bank holding companies.

And third, we have to recognize that the financial system is naturally going to change over time. When you put those three things together, what you realize is that—and what, I think, is embedded in Dodd-Frank, is a perspective that the Council must have the authority to regulate firms based on the risk that they pose and not the corporate form that they choose.

So when going through the non-bank designations process, what the Council is deliberating on is which firms pose significant risk, and therefore should be subject to tougher liquidity, tougher capital, and tougher supervision by the Federal Reserve. And that is the nature of the designation. It is not some sign one way or another. But what it says is that firms which pose a significant risk should be subject to tough standards.

Mr. CLEAVER. Thank you.

Ms. Clowers?

Ms. CLOWERS. GAO has recognized that risk can come from all sectors of the financial system, including non-banks.

Mr. CLEAVER. Thank you.

With my little time remaining, I am concerned because, unfortunately, there is a lot of bashing of Federal employees that goes on. You can always get an "attaboy" if you say something negative about Federal employees. And I would like to know from you, Mr. Gerety, whether or not you think that you have the capacity to go out and compete with the private sector to get the very best people possible to work with the Federal Government, realizing that they could make much, much more in the private sector?

And do you think that when we disparage the workers in the public sector, and then constantly say you can't get any pay increases, that is in any way helpful to the country or to your operation, Mr. Gerety?

Mr. GERETY. Congressman, we have had success attracting very talented people, but I agree that the payscale of Federal Government employees is lower than what comparably talented people would achieve in the private sector.

But the passion that people bring to public service is something from which we benefit.

Mr. CLEAVER. That is exactly what I expected you to say. And it is also something that is troublesome to me.

Just continuing to see what you didn't address, and I understand why you didn't do it, the kind of battering that you take.

Thank you, Mr. Chairman.

Chairman MCHENRY. Thank you.

And we will now go to Mr. Ross, of Florida.

Mr. ROSS. Thank you, Mr. Chairman.

Mr. Gerety, I want to address an area of non-bank financial companies with you, specifically with regard to insurance companies. Even though they are regulated by State pursuant to the McCarran-Ferguson Act, it is your understanding and, of course, FSOC's appreciation that they are systemically important financial institutions, correct?

Mr. GERETY. Congressman, I wouldn't say the Council has made that determination.

Mr. ROSS. But it is true in your example that you just had there that you coordinated it with Hurricane Sandy in dealing with the solvency, I guess, of these institutions, being able to meet their risk when they had the issues in the Northeast with the catastrophe of Hurricane Sandy.

Now, my concern is that you probably have at least two companies, insurance companies, that may be considered SIFIs, is that true?

Mr. GERETY. Congressman, the Council has made a decision not to comment on specific companies until final determination.

Mr. ROSS. Do you think that insurance companies at all are considered systemically important financial institutions?

Mr. GERETY. Congressman, I think that, as I mentioned a moment ago, the issue is not whether the—

Mr. ROSS. Wait a second now—but you also talked about risk. And there is a different element of risk with regard to insurance companies. They base on risk-based capital in terms of what their long-term risk is going to be as opposed to just statutory accounting principles that apply to most financial institutions.

So my question to you is, if you have insurance people on the Council, is it your testimony today that insurance companies are not going to be considered systemically important financial institutions?

Mr. GERETY. I would make a distinction between the importance of insurance in the financial system, which is undeniable—

Mr. ROSS. Would that be why the GAO report, then, explains that there is insufficient staff support for these insurance people who are on the committee?

Mr. GERETY. The Council has three members with insurance expertise—

Mr. ROSS. But you agree that the GAO report indicated that they have insufficient staff support? Is that true?

Mr. GERETY. So—

Mr. ROSS. Ms. Clowers, is it true that your report indicates that?

Ms. CLOWERS. Right—in our report we note that the insurance representative, for example, doesn't have the entire agency as the other member agencies would have to draw on those resources.

Mr. ROSS. Mr. Gerety, has the Council gone out to the National Association of Insurance Commissioners to ask for advice and guidance as recommended by Dodd-Frank?

Mr. GERETY. The Council has on its membership, as you know, three—

Mr. ROSS. I know it has the membership, but has it gone out? Has it reached out to the public? Has it reached out to any associations with expertise for guidance in terms of trying to determine whether insurance companies are going to be systemically important financial institutions?

Mr. GERETY. Congressman, it has reached out, both to the public and to insurance experts—

Mr. ROSS. Are there any records of that?

Mr. GERETY. Yes, sir, absolutely. The—

Mr. ROSS. Are there just minutes or are there records?

Mr. GERETY. The non-bank designations process took—made an affirmative decision to go through a rulemaking and get public comment, not just on an ANPR, an advanced notice of proposed rulemaking, but on two separate proposed rulemakings.

And in addition, we have started, with the help of Director Huff, who sits on the Council, to create information-sharing agreements—

Mr. ROSS. So this is—most likely, they are going to be SIFIs. But let me move on to another issue, and that is the Volcker Rule. I firmly agree that banks should not be involved in proprietary trading when they are using insured deposits. There is no question about that. When we are talking about making markets, it gets a little bit more difficult. But where we are running into real difficulty is the diversity of opinions from agencies as to what and when the Volcker Rule will apply.

And I direct your attention to a letter of December 20th from the Bipartisan Policy Center—and I believe you may have a copy of this—but their concern is that the adoption of the Volcker Rule should be consistent among all agencies. Would you not agree?

Mr. GERETY. Congressman, I think that is an important point, and the Treasury has a statutory coordination rule on the Volcker Rule. I think one thing that is key to note in the experience that we have seen so far—although the statute doesn't require substantively identical rules—

Mr. ROSS. But the impact of not having a consistent rule is going to be devastating on the financial industry. Would you not agree? There has to be some consistency, in not only interpretation, but also the application of the Volcker Rule. And I think that is what this letter requests.

But more importantly, I understand that just the other day, Mary Miller indicated that she thought it would be best if there was a joint rule delivered. Would you not agree that a joint rule of all the agencies, the SEC, everybody involved on the Volcker Rule be given?

Mr. GERETY. We agree that a consistent Volcker Rule would be very important.

Mr. ROSS. Would you commit the FSOC to making sure that a joint rule is issued with regard to the Volcker Rule?

Mr. GERETY. I can't commit on behalf of the Council, and more importantly, I can't—there are statutorily independent agencies that are given the authority to write rules.

However, I would note that in the proposed rule stage, all five of those agencies, notwithstanding their statutory independence, did deliver substantively identical proposed rules. So there is, I believe, evidence of a commitment to the point that you make about a consistent Volcker Rule.

Mr. ROSS. And do you believe that there will be a joint rule then?

Mr. GERETY. I can't predict the future.

Mr. ROSS. Mr. Chairman, I will yield back my time.

Chairman MCHENRY. On that note of not being able to predict the future, we now recognize the gentleman from Colorado, Mr. Perlmutter, who I predict will have a good series of questions.

[laughter]

Mr. PERLMUTTER. I am not sure your prediction will come true, Mr. Chairman, but I thank you for the time.

And I appreciate Mr. Ross' questions. To the panel, it is like you are in a deposition. We are going to say, "Isn't it true that," "Wouldn't you agree that."

So, Ms. Clowers, I will start with you.

Isn't it true that Section 112(c)(5) requires that much of what the FSOC does has to remain confidential?

Ms. CLOWERS. Correct.

Mr. PERLMUTTER. Okay. So just going back to your transparency piece, your transparency recommendation is more on general principles and not so much in the regulatory arena where they are saying to an institution or to a group of institutions, "We have trouble here," but it is more, "We think these might be emerging threats," or, "We are worried about a bubble over here."

Where do you think the transparency needs to be more—where does it need to be clearer? Where do their records need to be clearer?

Ms. CLOWERS. We think the records could be improved at the principals level, for example. Again, the minutes taken at those meetings are very limited. Often, it will just provide information on who presented, what the agenda item is, and then it will say, "The agenda—the issues were discussed and questions were"—

Mr. PERLMUTTER. But in the accounting arena—and I appreciate the desire for more information.

Ms. CLOWERS. Yes.

Mr. PERLMUTTER. But you would admit that they have to balance between confidentiality of the information they might receive from an institution or a group of institutions versus making that open and declaring it to the world.

Ms. CLOWERS. Yes, and anyone dealing in the financial markets arena—any of the regulators recognize the importance of maintaining confidential information and the impact that releasing certain information could have on the markets. And we recognize that in our report, as well.

We think there is a balance that could be struck, and we point out the other entities such as the Federal Reserve, the Federal Open Market Committee. The way they release information could be a model for FSOC.

Mr. PERLMUTTER. Okay, thank you.

Mr. Gerety, just sort of going back to basics, before the crash of 2008, when, in my opinion, the Bush Administration allowed the regulators to turn a blind eye to a number of bubbles that were appearing in the economy, the different regulators sort of operated in silos, and weren't really speaking to one another or collaborating, as is described in the statute, or you have described in your testimony.

How many meetings—you said there have been eight meetings since the September report of FSOC?

Mr. GERETY. I believe that is correct. I don't have the exact number at the top of my head.

Mr. PERLMUTTER. About how many meetings overall have they held since the passage of Dodd-Frank?

Mr. GERETY. The Council has met 28 times at the level of the principals.

Mr. PERLMUTTER. Okay. So that alone, in my opinion, having sat through the testimony and the trauma of the crash of 2008, is a huge step in the right direction so that these agencies are speaking to one another so that they can, Ms. Clowers, determine from their conversations whether a bubble is developing, whether a threat is emerging.

So to you two, I would ask, what would you suggest they do differently to pinpoint emerging threats?

And maybe, Ms. Clowers, I will start with you.

Ms. CLOWERS. In the report, we describe the current processes that FSOC uses, which is through the Systemic Risk Committee in which the agency members come together and identify potential issues and pass them up through the deputies and to the principals.

What we had recommended is they take a more systematic and comprehensive approach using both quantitative and qualitative tools to look across all the sectors. Because again, going to your point, that is what was missing before the crisis—that we were too siloed. The current process that they use at the committee level could result in the silos again if agency members bring only what they identify as risk and then discuss amongst themselves.

We want them to be more horizontal in their reviews.

Mr. PERLMUTTER. Okay.

Mr. Gerety, do you have any comment on what she just said?

Mr. GERETY. Sir, I think what Ms. Clowers has just described is actually consistent with the processes that the Council has adopted. And certainly on the basis of that recommendation, things that we strive to do more and more so.

I think in response to the question of how do we make sure we have a horizontal review, that is actually one of the great benefits of the Systemic Risk Committee. We have a member from the National Credit Union Administration. We have a member from the FDIC. We have staff coming from the insurance and other sectors to make sure they are sharing a perspective from any group, and also comparing across.

And in addition, one of the things we work closely with the Office of Financial Research on is to develop some more systematic sharing of financial stability and other macro economic factors—

Mr. PERLMUTTER. Thank you, Mr. Chairman.

And I thank the witnesses for your testimony.

Chairman MCHENRY. The gentlelady from Missouri, Mrs. Wagner, is recognized for 5 minutes.

Mrs. WAGNER. Thank you, Mr. Chairman.

And thank you to our witnesses for coming here.

I am not an attorney, I am just married to one, so I will be very direct.

Mr. Gerety, would you agree that uncoordinated action by multiple regulatory agencies imposes a cost on the financial system of the United States?

Mr. GERETY. Congresswoman, I think what's important is that agencies coordinate as they implement their independent statutory duties.

Mrs. WAGNER. I was interested in Ms. Clowers' testimony and some of the recommendations that were given in your GAO report that talked about meeting a cost-benefit analysis.

Could you comment on that?

Mr. GERETY. I think that the issue raised is the question of how do we make sure that the implementation of Dodd-Frank is effective, but also needs to be considered in the context of the financial crisis that we just experienced and the tremendous costs it imposed on the economy.

Mrs. WAGNER. Have you studied—FSOC, OFR—what the potential costs of non-coordination are, sir? And if so, how much would that be?

Mr. GERETY. I think the issue of coordination is very important, but as we go through the implementation of Dodd-Frank, I think there is plenty of evidence of very significant coordination among the financial regulatory community, and the importance that they value making sure that the rules are consistent.

Mrs. WAGNER. But you have not looked at the costs regarding this?

Mr. GERETY. We accept that the importance of coordination is very high and that is why we are very focused on making sure that—

Mrs. WAGNER. Is the answer yes or no on the cost-benefit analysis?

Mr. GERETY. Congresswoman, I think what you are asking about is the importance of coordination. We think it is very important, and we are working to promote that coordination between agencies.

Mrs. WAGNER. Let me go back to a comment that you made earlier, then, sir. I believe your testimony was that you could not comment on the actions of other regulatory agencies, like the CFTC. Sir, wasn't that why you were created?

Mr. GERETY. Congresswoman, I was speaking for myself. I can't speak to the specific decisions made by the CFTC in terms of how they promote their international regulatory approach.

Mrs. WAGNER. I will move on.

Ms. Clowers, how has FSOC coordinated agency rulemaking to this point in time?

Ms. CLOWERS. We had made a recommendation in 2011 that we thought FSOC could play a greater role in coordinating the rulemaking process. We recommended that they develop a formal policy that would indicate when coordination should take place, who should be involved, and how to reconcile conflicting views. We think there is a role for FSOC to play as a traffic cop, so to speak.

Mrs. WAGNER. How did FSOC fulfill its very specific statutory duty to facilitate coordination during the process that led to the proposal of the Volcker Rule in 2011?

Ms. Clowers?

Ms. CLOWERS. In working through our audit on FSOC, we saw that a lot of the coordination takes place at the committee level in terms of working through specific issues. I don't have an answer on the specifics on the Volcker Rule, but I can get back to you.

Mrs. WAGNER. I would appreciate that. And I believe that the report indicated that there was significant room for improvement. Is that correct, ma'am?

Ms. CLOWERS. That is correct.

Mrs. WAGNER. Okay, thank you.

Next, Dr. Berner, and then Mr. Gerety, can you describe to what extent FSOC and OFR have developed comprehensive and systematic mechanisms for identifying and monitoring systemic risk?

Mr. BERNER. Thank you, Congresswoman.

We are working hard in the OFR, in collaboration with the Council and its member agencies, in order to do just exactly that. As Mr. Gerety mentioned, we work through the Systemic Risk Committee to develop risk hypotheses to try to identify emerging risks, not just those risks that have occurred in the past. And we try to do that by looking at structural vulnerabilities in the financial system, such as the ones that have been discussed here today.

It was referred earlier to risks in the tri-party repo market and short-term funding markets generally, in money funds and other areas, as well as cyclical risks that may emerge, such as the build-up of leverage or maturity transformation in the financial system.

Mrs. WAGNER. Thank you, sir.

Mr. Gerety, could you answer that question, please?

Mr. GERETY. The Council has developed a number of processes to make sure that we have very strong interagency collaboration and identification of issues. In addition, the Council's annual report is a comprehensive document that looks systematically across the financial sector, both in terms of significant financial market developments, financial regulatory developments, and then also uses that as a basis to develop hypotheses about potential recommendations—

Mrs. WAGNER. If I may interject here, I believe that the GAO report indicated, however, that in fact FSOC lacked a systematic process to identify future threats. And that perhaps it had failed to distinguish future from current threats.

If you could respond to that?

Mr. GERETY. Congresswoman, the approach that we have taken in the annual report is to identify developments, to identify vulnerabilities, and to identify potential shocks that could interact with those vulnerabilities and create threats. In that sense, I think we have a very systematic approach to identifying issues that the financial regulatory community and market participants need to address.

Mrs. WAGNER. I think my time has expired. I appreciate the Chair's indulgence.

Chairman MCHENRY. Ms. Clowers, did you have a response to that?

Ms. CLOWERS. Yes. We did report in our September report that we thought FSOC could do a better job in identifying and reporting on both current and emerging threats in its annual report. At times, it is commingled together, so it is difficult to determine what is a current threat versus an emerging threat. An example would be the eurozone crisis that was talked about in the annual report as an emerging threat, when in general most market participants have known about eurozone issues for a number of years.

Mrs. WAGNER. And the prioritization of those threats.

Ms. CLOWERS. Absolutely. They have identified a number of threats each year, and we believe prioritizing those threats could help better focus policymakers as well as market participants on the key issues. But when everything is a priority, nothing is.

Mrs. WAGNER. Correct.

Chairman MCHENRY. Mr. Ellison, from Minnesota, is recognized for 5 minutes.

Mr. ELLISON. Thank you, Mr. Chairman, and Ranking Member Green. I appreciate you calling this hearing.

Sometimes when we discuss these issues about Dodd-Frank and the legislation that came as a result of it, including FSOC, the discussion sort of makes me think that there wasn't a financial crisis, that we didn't see 4 million foreclosures, that we didn't see leading financial institutions either collapse or have to be consolidated. All of these crises didn't happen. It almost feels like we are pretending Congress just passed a bunch of regulations for no good reason.

Anyway, we have had the GAO report which made some recommendations and observations. And I guess my question is for Mr. Berner and Mr. Gerety.

Mr. Gerety, your organization was fully staffed just this past year. Mr. Berner, you were just confirmed in January, and according to your office, your staff is only half of what it will be in the coming year. I think that you are doing okay.

Where would you say you are in terms of building the infrastructure you need and the tools that you need to carry out your mandate? And does the sort of embryonic nature of the work you are doing explain part of the analysis that GAO may have done?

Mr. BERNER. Congressman, thank you for your question.

We are well along in the standing up of our office. As you indicate, however, it is a challenge both to build an organization from scratch, as well as to fulfill the mandates with which we are charged. We hope that we are doing a good job on both of those.

I indicated in my written testimony some dimensions of both of those things. And in response to the report, which we very much appreciate, and appreciate the engagement with the GAO, we are taking steps to implement many of the recommendations that the GAO has given us.

I would point to my written testimony, for example, to set a performance metric that we have developed in response to that need. We are committed to transparency and accountability in the performance of our obligations.

Moreover, I would say that we are really starting to deliver on our mandate. For example, just last night we published the 6th working paper in our working paper series that deals with issues that go across the financial system, not just focused on one part of it. But as Mr. Gerety indicated, and I indicated earlier, that kind of horizontal approach to look across the financial system is extremely important for carrying out our mandate.

Mr. ELLISON. Thank you.

Mr. Gerety?

Mr. GERETY. Congressman, I would add that the points you make are important, and I think the engagement that we have been able to have with the GAO has been very helpful. In the example of the Council's annual report, we certainly are learning as we go, becoming more effective in considering a wide range of reports, and providing even more transparency and accountability into our analysis of that.

We are working through and drafting this year's report as we speak. And so, I think the GAO's recommendations in that area are going to be something we take very seriously as we work to improve that product.

Mr. ELLISON. Thank you.

Would you like to respond, Ms. Clowers?

Ms. CLOWERS. Certainly. I would agree with you that the agencies face challenges. And as we recognized in our report, for the OFR in particular, trying stand up an organization while carrying out their mission is challenging. FSOC is tasked with an inherently difficult job of identifying and monitoring risks. And so, we recognize those challenges. And the recommendations that we make are designed to improve these important institutions.

Mr. ELLISON. Thank you.

I think it is just important to point out that your recommendations are not indictments; they are designed to help.

Ms. CLOWERS. Correct.

Mr. ELLISON. Yes. And with the short time I have remaining, could you all identify what challenges you think the sequester might present to you carrying out your mission?

Mr. BERNER. Congressman, I would just respond by saying that the Financial Research Fund, which funds both the FSOC and the OFR, is subject, according to OMB, to the sequester. And so, that has resulted in some cut in our ability to fulfill our mission—to spend money to fulfill our mission.

Mr. GERETY. We are working with OMB to develop a plan for how to operate consistent with the sequester. It certainly will affect us, and we are developing a plan to make sure that we are as effective as we can be, given the loss.

Mr. ELLISON. It might be helpful to us to know how it is going to affect you. If you all can just communicate with the committee and my office on problems such as: we are going to have reduce this number of staff; what it is going to actually mean in terms of your ability to deliver on the mandate.Thank you.

I yield back, Mr. Chairman.

Chairman MCHENRY. The gentleman's time has expired.

And if I might concur with the gentleman, we would certainly appreciate your response to the committee on those effects from OFR and from FSOC as well.

Mr. Berner, in particular, I know you operate through an industry assessment that funds your operations in large part. It is a different funding mechanism so you have slightly different processes on getting your budget, and so to detail that would be helpful as well, and the challenges associated with that.

With that, we now recognize a new member of the committee, Mr. Barr of Kentucky.

Mr. BARR. Good morning.

And thank you, Dr. Berner, Mr. Gerety, and Ms. Clowers for your testimony here today and for your efforts in providing oversight and contributing, hopefully, to the financial stability of our financial system.

Mr. Gerety, in February, or last month of this year, the Bipartisan Policy Center issued a report on housing reform which specifically requested the President to work with the Secretary of the Treasury to appoint an adviser to force coordination of the rules related to mortgages.

I know forcing coordination is inconsistent with Secretary Geithner's analysis of the authorities of the Council. But given the fact that this Bipartisan Policy Center issued a report advocating for more coordination on rules related to mortgages, and given the fact that facilitating coordination is one of the statutory duties of the Council, will you commit to coordinating the release of new mortgage regulations?

And will you use Dr. Berner's organization, the OFR, to help evaluate the impact of the flurry of mortgage rules emerging from Dodd-Frank, including but not limited to the Qualified Mortgage rulemaking coming out of the CFPB?

Mr. GERETY. Congressman, I can't commit on behalf of the Council. Obviously, that is up to the Council members.

But I can say that the importance of housing-related rules, mortgage-related rules is a topic that has been very important and central to the Council's work in its analysis of the financial system and in its thinking about the implementation of rules under the Dodd-Frank Act. This has actually been a topic that the Council has discussed a number of times and has made public recommendations about the importance of in the Council's annual report.

I think that the points you make are things that are already very central to the Council in terms of focusing on reforms to the housing market in a way that work together and that work effectively to promote the safety and soundness of that market.

Mr. BARR. Ms. Clowers, can you respond to Mr. Gerety's testimony a little bit, specifically on what benefits could we anticipate and what unintended consequences could be avoided if these rulemakings on mortgages were better coordinated?

Ms. CLOWERS. We have done a body of work on the importance of coordination among agencies, not only in looking at coordination at the FSOC level, but also at particular Dodd-Frank rulemaking.

And what we have found is that although the regulators are coordinating, especially when Dodd-Frank requires that they coordinate on certain rules, much of the coordination is ad hoc and informal.

And while that could be sufficient in some circumstances, we recommended that the agencies develop formal policies for coordination, because in the press of business, if things are just ad hoc or informal, that is when coordination can break down. Or if there are conflicting views, that is when coordination can break down if it is ad hoc and informal.

Thus, we recommended more formal policies to guide this coordination.

Mr. BARR. Mr. Gerety, I hope that you take seriously the GAO's concerns regarding the ad hoc nature of the coordination.

But let me ask you another question, Mr. Gerety, really quickly. Does the Council internally prioritize the significance of current and emerging threats to the economy which are listed in its annual report?

And does the Council devote staff and budgetary resources accordingly to that important effort of prioritization?

Mr. GERETY. The Council's annual report is a record of the issues and recommendations that the Council members feel are necessary to promote financial stability. That is the language of the statute and that is the threshold by which the Council prioritizes. So I think what we see in this is there is a large membership among the Council. They each have statutory responsibilities and capabilities to address issues.

And so, while the number of recommendations and the number of issues is large, it reflects the importance and the dynamics within the financial system.

And I think that is how the Council thinks about this problem, is to make sure that across the regulatory community, issues are identified and that agencies and market participants work to address them.

Mr. BARR. I am not sure I heard an answer in that to the specific question of how does the Council prioritize the emerging threats.

It seems to me your answer was, we identify emerging threats. The question was, how does or does the Council at all prioritize those emerging threats that you do identify?

Mr. GERETY. Congressman, the language of the statute—and when you think about threats in the financial system, it is not always possible to identify which threat is likely to emerge sooner rather than later.

We have seen over the course of the last few years, at certain times global growth has been a larger concern. At certain times, issues in Europe have been larger concerns.

So in that sense, what the Council aims to do and what the statute suggests the Council needs to do is to identify the broad range of threats that could pose a threat to financial stability and then to work to address them.

And I think that is the standard by which the Council operates.

Chairman MCHENRY. The gentleman's time has expired.

Mrs. Maloney, from New York, is recognized for 5 minutes.

Mrs. MALONEY. Thank you, Mr. Chairman.

And I thank all of the panelists.

Dr. Berner, the Dodd-Frank statute requires you to develop tools for risk management and monitoring. So, what criteria are you using to identify systemic risk?

Mr. BERNER. Thank you, Congresswoman.

We are using a variety of criteria to identify threats to financial stability. As I indicated earlier, we are working in the context of the Systemic Risk Committee of the Council to develop a product and several products that will look at those various measures of risk.

Some of them are well-known. Some of them are, for example—

Mrs. MALONEY. But what are they? Can you list them?

Mr. BERNER. Some of them are reflective of indicators that we listed in our annual report. There were 31 there. Measures such as the so-called CoVaR, which illustrates the joint contribution of a financial institution's contribution to a threat to financial stability. Others that have been developed in the academic community which are known variously as MES or SCS.

Mrs. MALONEY. But can you tell me what they are? I don't know what MES is or SCS.

Mr. BERNER. Sure.

Mrs. MALONEY. What, specifically, is it? What are the systemic risk indicators that you are looking at, in plain English?

Mr. BERNER. Sure. These indicators attempt to measure empirically what the shortfalls might be, and the losses that might be accumulated by an institution under stress and how that might spread across the financial system.

These are—

Mrs. MALONEY. Such as? Are you going to identify these risks to see how they go over the financial system? What are they? Is it capital? What, specifically, are you looking at to identify systemic risk?

Mr. BERNER. Congresswoman, capital might be a remedy for some of those risks, but the metrics that we use attempt to identify whether there is excessive leverage in the system, whether there is a buildup of maturity transformation, whether low volatility is leading to the buildup of those two things in the financial system or in the part of a group of financial companies, wherever they might be located in the financial system—

Mrs. MALONEY. If you could get to the committee the list of the 31 and more specifics in this area, I would like to study it more.

But I want to know if the technology that you are developing, will it allow or does it allow for adjusting this criteria to reflect the changes in the market over time or incorporate best practices or lessons learned as the project matures?

Because one of the criticisms during a financial crisis is that regulation did not keep up with innovation and with the new—will you be flexible in changing this in the technology that you are developing?

Mr. BERNER. That is a really important question that you raise, Congresswoman. The evolution of the financial system and financial innovation means that the system is ever-changing. It means that the metrics can't be considered as always reliable from the past as they might be in the future.

Mrs. MALONEY. So are you incorporating technology to adjust?

Mr. BERNER. We are constantly looking at innovations in financial markets and financial institutions to try to take account of whether or not these indicators are reliable.

Mrs. MALONEY. The statute also asks for you to collect the data that then goes to FSOC for them to look at. And I have asked for this before, maybe it came into my office, but I don't recall seeing it. What specific data elements are you collecting? And could you get it to the committee, so we can all look at it?

And how many have you already collected, are you giving to FSOC? What is the list that you would like to get? And very importantly, where are you getting it from? Are you getting it from other agencies? Are you getting it from a financial institutions? Where are you getting it?

That is an in-depth, longer question, but I do want to talk about the Legal Entity Identifier (LEI) project, which some have described—one of my constituents described it as the "black hole project" that will never be completed.

So I want to know, what is the projected timeline for the implementation of the Legal Entity Identifier within the financial industry?

Mr. BERNER. Congresswoman, the Legal Entity Identifier project is very important because it uniquely helps us to identify parties to financial transactions. That is an important part of standardizing data in the global financial system.

Mrs. MALONEY. But my question was, what is the timeline for implementation and completion?

Mr. BERNER. That timeline actually involves a launch of the system this month. There are some issues to wrap up before—

Mrs. MALONEY. You mean the project is completed then? You are going to launch it? It is completed?

Mr. BERNER. I would describe the process as a process. The implementation and diffusion through the financial system has begun. The CFTC, for example, has—

Mrs. MALONEY. My time is almost up. What is the estimated—

Chairman MCHENRY. The gentlelady's time is—

Mrs. MALONEY. Could you get that to the committee, the estimated cost of the project?

Thank you.

My time is up.

Chairman MCHENRY. As I pledged to the witnesses, you do have time to answer—I will give you time to answer the question.

Dr. Berner, what is the estimated time of completion of the LEI? Is there a date?

Mrs. MALONEY. And, Mr. Chairman, also the cost to both government and the private sector.

Chairman MCHENRY. That was not what the gentlelady asked, but we will be happy—is there a date you have for completion?

Mr. BERNER. Congressman, we don't have a specific date for completion—

Chairman MCHENRY. Do you have a year?

Mr. BERNER. This is an ongoing—

Chairman MCHENRY. Do you have a year?

Mr. BERNER. This is an ongoing process. The project is well—

Chairman MCHENRY. Do you have a hope for a date of completion?

Mr. BERNER. I wouldn't describe, Congressman, that there is a specific date for completion—

Chairman MCHENRY. Okay, thank you. And that suffices.

I will be following up, and I pledge to follow up with my colleague from New York on this question of—

Mrs. MALONEY. Thank you, Mr. Chairman.

Chairman MCHENRY. With that, I will now recognize the gentleman from Tennessee, Mr. Fincher.

Mr. FINCHER. Thank you, Mr. Chairman.

Dr. Berner, these questions are going to be geared, I guess, toward you.

With transparency being consistent, the OFR has been asked by FSOC to conduct a comprehensive study on the asset management industry and analyze if these firms could pose systemic risk. Can you tell us the process that OFR is using to examine asset managers?

Mr. BERNER. Yes, Congressman. Thank you for your question.

We are taking a comprehensive look at the asset management industry and its activities. The process involves engagement with the industry to learn about its practices and business models and the mix of businesses in that industry.

The process also involves looking at data on that industry to try to understand empirically both the size and scope of those activities in the industry.

And last, the process involves full engagement with Council member agencies to get their views on how the asset management industry and its activities, from their perspective, might be analyzed.

So this is a great example of coordination across the Council.

Mr. FINCHER. Can you tell me specifically who you have met with and what you have learned from the meetings so far?

Mr. BERNER. We have met with a number of asset managers, Congressman. I can get you the list of—

Mr. FINCHER. Would you please do that?

Mr. BERNER. But I just want to say, Congressman, if I may, that in the process of engagement with the industry, we have welcomed the opportunity to engage with any and all who want to meet with us. So we have engaged both with industry groups as well as with specific firms.

Mr. FINCHER. Are there specific activities that you are looking for engaged by the asset managers that you are really concerned about that may pose systemic risk?

Mr. BERNER. Congressman, the analysis is not yet complete, but in looking at activities, we look back to the fundamental services in the financial system and where there might be evidence of a build-up of risk in those activities, specifically a build-up of maturity transformation, connectedness across the financial system so that we look at those activities not just as the origin of any threat to financial stability but for the possibility that it might transmit or amplify a threat to financial stability.

Among those would include reliance on short-term funding, along with a portfolio of longer-term assets. Among those would be other evidence of those kinds of activities that might pose a threat.

Mr. FINCHER. How long is it going to take to complete the study?

Mr. BERNER. Congressman, we don't have a specific date to complete the study because it is, in the work that we are doing to study the industry, the process is well under way, and it is being discussed within the committee.

Mr. FINCHER. General framework—how long has the process been?

Mr. BERNER. The process has been ongoing, Congressman, for about a year, and we hope to complete it in the next few months.

Mr. FINCHER. But before the end of the year?

Mr. BERNER. Before the end of the year.

Mr. FINCHER. Okay. Good deal.

I yield back the balance of my time.

Thank you, Mr. Chairman.

Chairman MCHENRY. Will the gentleman yield?

Mr. FINCHER. I will yield.

Chairman MCHENRY. To follow up with Dr. Berner on the question my colleague from New York had on the cost of the LEI, that process, do you have any analysis you could give us, any estimate?

Mr. BERNER. Congressman, we don't have a specific estimate of the cost of the LEI project at this point in time. But what I would say is that the benefits to industry and to regulators, in my judgment, far exceed the cost. And I think the evidence for that is—

Chairman MCHENRY. How do you know that the benefit will exceed the cost if you do not yet know the cost?

Mr. BERNER. The industry has told us that the benefits are likely to exceed the cost.

Chairman MCHENRY. And what if the industry said that everything is fine and hunky-dory, do you even need to collect data if they just tell you that?

You understand the question arising out of this? How do you know how much to request from the industry to fund your office on a program for which you don't know the cost.

Mr. BERNER. Congressman, the project is a global project. We have full global engagement around the world with global regulators under the auspices of the Financial Stability Board. And so the cost have been spread across all those agencies and—

Chairman MCHENRY. Do you know the cost for your agency?

Mr. BERNER. Congressman, I can get back to you and tell you the resources that we have used in prosecution of the—

Chairman MCHENRY. And would you also disclose your anticipated resources that you will need for the remainder of this year and next year?

Mr. BERNER. Congressman, I can do that.

Chairman MCHENRY. Thank you.

With that, I now recognize Mr. Delaney of Maryland.

Mr. DELANEY. Thank you, Mr. Chairman.

I have two questions. My first relates to data and information that you are tracking to determine whether institutions that are designated as systemically important are actually getting benefits in the market for that designation from a cost of capital or access to capital perspective.

So I am not sure who would be the best to—either Mr. Gerety or—

Mr. GERETY. Congressman, I think the question that you are asking is a question about perception, how do market participants think about risks of firms?

Mr. DELANEY. Yes.

Mr. GERETY. What I can say is from the perspective of Dodd-Frank and the actions taken in Dodd-Frank, that perception that the government will prevent the failure of any firm is incorrect, and Dodd-Frank is very clear that no taxpayer losses shall be incurred in the use of the Orderly Liquidation Authority (OLA) and that no financial firm, no matter how large or complex, will be prevented from failure—

Mr. DELANEY. But firms which have that designation have emergency funding available to them should there be a crisis, is that correct?

Mr. GERETY. That is not correct, sir. The designation of a nonbank financial company does not give that company access to any emergency funding. In fact, what it does is it imposes significant capital liquidity and enhanced supervision on that company.

Mr. DELANEY. What about a bank that is designated systemically important?

Mr. GERETY. The Council doesn't designate any banks or bank holding companies as systemically important. The Dodd-Frank Act in its terms on the statute imposes heightened standards on any bank holding company with a larger than $50 billion balance sheet.

Mr. DELANEY. And so, there is no emergency funding available to financial institutions which are designated systemically important to manage their liquidation?

Mr. GERETY. Congressman, I think we have to separate—

Mr. DELANEY. Right.

Mr. GERETY. —two distinct authorities. The question that you are asking, I think, is related to the Council's authority to designate a non-bank financial company.

Mr. DELANEY. Yes.

Mr. GERETY. The action of that designation is simply the imposition of enhanced supervision by the Federal Reserve.

Now, separately, Dodd-Frank created an Orderly Liquidation Authority for financial companies, both non-bank financial companies and bank holding companies. The designation is actually not required for the use of that Title II authority.

Mr. DELANEY. Right.

Mr. GERETY. So there is no direct statutory link between designation and the use of Title II.

Importantly, what the statute makes very clear is that taxpayers cannot bear losses and that liquidation cannot be prevented through the use of government funds.

Mr. DELANEY. Right. But do you track any data to determine if the market perception is actually becoming reality, and firms have enhanced access to capital either at lower rates or just greater depth of market because of various designations?

Mr. GERETY. Congressman, I think the question is an important one. There is actually a lively academic debate about how to measure what that looks like, and where it is going. I think the evidence is in some ways mixed.

Importantly, if you just look at the simple measures of risk before the crisis and post-crisis, what you see is that the market is pricing much more significant risk and that is reflected in a number of metrics in the financial system.

Mr. DELANEY. But I am talking about relative; I am not talking about absolute risk. Obviously, they are pricing risk differently than they did before the crisis. But on a relative basis, do you track firms which receive various designations within the government and their access to capital versus similarly situated firms which do not to see if there is any reinforcing market perception based on designations?

Mr. GERETY. The most important thing from the perspective of the Council is that that perception as it exists is incorrect, and that the action of Dodd-Frank is to prevent any firm from having a—

Mr. DELANEY. Whether they are making it correctly, because to some extent, if the market assumes that, it becomes reality. So putting aside how they should interpret the actions, do you track whether they do actually interpret the actions the way the academics think they should determine the actions?

Mr. GERETY. Congressman, there is a very wide range of academic opinion and other studies on this matter. We are certainly aware of that debate. But the thing that I think is important to note is that the action of Dodd-Frank does not allow that perception to become reality. The action of Dodd-Frank is to prohibit in law the use of any taxpayer losses to prevent the liquidation of any firm.

So whether that perception exists or not in the market, it is incorrect.

Mr. DELANEY. But doesn't it also by law require the industry to set aside funds to be available for institutions during their orderly liquidation?

Mr. GERETY. Congressman, I think what you are asking about is whether firms themselves need to plan for their liquidation, and that is true both in terms of capital and liquidity standards and in terms of the creation of what are commonly called "living wills."

Mr. DELANEY. Right

Mr. GERETY. So firms being required to plan for their resolution in bankruptcy is the standard Dodd-Frank imposes on that.

Mr. DELANEY. But industry-wide, funded by industry financing that is available through a liquidation, you are saying does not exist?

Mr. GERETY. Dodd-Frank does not create an industry assessment to fund liquidation.

Chairman MCHENRY. The gentleman's time has expired.

It is done through the FDIC. And if the FDIC runs out of funds, it can tap the Treasury.

Mr. DELANEY. No, I am not talking about—

Chairman MCHENRY. On a technical basis, the gentleman is correct in his answer. But I understand the point, and I would love to have further conversations with the Member.

And now, we will recognize the gentleman from Wisconsin, Mr. Duffy.

Mr. DUFFY. Thank you, Mr. Chairman.

Mr. DUFFY. Per Dodd-Frank, a non-bank SIFI designation must meet the definition of "predominantly engaged in a financial activity." That definition in Dodd-Frank was set forth in Section 4(k) of the Bank Holding Company Act.

That was also the Pryor-Vitter amendment in the Senate that came forward.

Now, the Fed has come out with a proposed rule that potentially expands the definition of "predominantly engaged in financial activities," expanding that definition of Section 4(k), as it was set forth in Dodd-Frank. My concern is that the Fed's definition of "predominantly engaged in financial activity" is going to cast potentially a far wider net and grab, maybe, large manufacturers and retailers in the country.

FSOC is in the final stages of evaluating an initial set of non-bank SIFI designations. Is it possible, Mr. Gerety, that those designations can take place before the Fed submits its rule and definition?

Mr. GERETY. I don't believe the statute requires that rule to be complete before designations. However, we are working very closely with the Federal Reserve. They have consulted with the Council on that rule. And we expect them to finalize that.

Mr. DUFFY. My question: Is it possible that FSOC will come out with its non-bank SIFI designations before the Fed submits its final rule and definition?

Mr. GERETY. Congressman, I can't speak for the Council's timing in its decision, but—

Mr. DUFFY. Is it possible?

Mr. GERETY. —there is no statutory—

Mr. DUFFY. But is it possible?

Mr. GERETY. There is no statutory—

Mr. DUFFY. I know. But is it possible? You are the representative of Treasury. Is it possible that those designations may come out before the Fed's rule?

Mr. GERETY. The definitions require a two-thirds majority vote of the Council. I can't speak for two-thirds of the Council.

Mr. DUFFY. Okay. So let's talk about it maybe in a little different way. Are you committed that if FSOC comes out with these non-bank SIFI designations—are they committed to using the rule as set forth in 4(k) for Dodd-Frank? Or are they potentially going to use the rule that might be expanded from the Fed?

Mr. GERETY. The Fed has the authority to interpret the definition of "predominantly engaged in financial activity" as you have identified. Section 4(k), which you are referring to, is in the Bank Holding Company Act—

Mr. DUFFY. That is right.

Mr. GERETY. The Federal Reserve has the statutory authority to interpret that section of the Bank Holding Company Act as it relates to the definition of "predominantly engaged in financial activity."

Mr. DUFFY. I don't know if you have seen the letter that was sent by Senators Vitter and Pryor, basically setting forth that it was quite clear what the intent of their amendment was, which was to strictly follow Section 4(k).

And now, the Fed is going to potentially expand that rule. Are you saying that FSOC is not going to follow the will of Congress, but potentially an expanded interpretation by the Fed?

Mr. GERETY. Congressman, the Federal Reserve has the authority to interpret the Bank Holding Company Act. It is given the rulemaking authority under Dodd-Frank. And so, I anticipate that we would follow the Federal Reserve's rule as it interprets the statute.

Mr. DUFFY. So when there is a conflict between what the directive of Congress was and then its interpretation by the Fed, FSOC will go forward with the interpretation of the Fed, as opposed to what Congress has specifically delineated in Dodd-Frank.

Mr. GERETY. Congressman, I can't speak to the—a commitment that I think you are asking on behalf of the Council. But I can say that my understanding is the Federal Reserve has the authority to interpret the Bank Holding Company Act and write rules in that, as given by Dodd-Frank.

Mr. DUFFY. Let's try another way. Can you assure Congress that FSOC will not designate any non-bank an SIFI that doesn't meet the definition as set forth in Section 4(k)?

Mr. GERETY. Congressman, as I understand it, you are asking if the FSOC will consider the statutory standard, which is that any company needs to be a non-bank financial company predominantly engaged in financial activity, and we intend to follow that standard in our designation.

Mr. DUFFY. You understand the concern? Congress was very focused and very concerned about an expansion of this law to encompass companies that have nothing to do with the financial sector. There are retailers and manufacturers. And if you expand it, basically FSOC can have some impact on all of these large companies across the country. And that was our concern.

And now we see this—the Fed expanding the rule that can go far beyond the intent of Congress. That is our concern.

Mr. GERETY. Congressman, if I can just respond briefly, two points. First, the statutory standard is at 85 percent of revenue—

Mr. DUFFY. That is right.

Mr. GERETY. —or 85 percent of assets are financial in nature, as defined as we have just been discussing.

And second, that is only the limit of what the Council can do. The Council has set up a very robust process to assure that any non-bank financial company designated by the Council is one that poses risk to the financial markets.

Mr. DUFFY. My point is that Congress was clear in what we wanted. And it is being expanded. I want to know that FSOC will follow the directive of Congress, not an expanded definition by the Fed.

Chairman MCHENRY. The gentleman's time has expired.

We will now recognize Mrs. Beatty for 5 minutes.

Mrs. BEATTY. Thank you so much, Mr. Chairman, and Mr. Ranking Member.

Let me first thank you for being here today, and for taking the time to go over how you operate and also in such a short period of time being able to respond to the many things that not only we have put on you, but what have come up in the report.

As I have listened to the dialogue today, as we talk about whether it is strategic planning or whether we are talking about how you meet all of the standards, I guess many of the things I was going to ask have been addressed.

So let me pose this question to you. When we look at the FSOC and the OFR, they are central to the overarching objectives of the Wall Street Reform. And they must—I believe you must also be given the opportunity to redefine—the research we talked about, the rulemaking, and certainly a deliberative process. Can you share with the committee what you have done so far to establish a working relationship with some of your foreign counterparts, or can you talk about any of the metrics established in your new roles with what you are doing with FSOC or the OFR as you employ or monitor measures of systemic risk?

Mr. GERETY. Congresswoman, let me address the international coordination issue first. The statute gives the Council the responsibility to coordinate domestically and suggests that the Treasury Secretary should coordinate on behalf of the Council internationally.

The Council has been very active in discussing amongst itself the international developments, whether they be on derivatives regulation, whether they be through the Federal Insurance Office and in collaboration between Treasury and the State insurance commissioners on progress in the international dialogue on insurance.

So those are the types of topics that the Council has really made sure that it uses its domestic conversation to be coordinated with the international activities of U.S. regulators, whether they be the market regulators, the insurance community or the banking regulators.

So I think we have been very active in using the Council to facilitate a dialogue about the importance of and the progress of international coordination on regulatory issues.

Mrs. BEATTY. Thank you. I appreciate that.

Mr. BERNER. Congresswoman, thanks for your question. As I mentioned in my testimony, we are taking steps to coordinate internationally.

First, data standards is one area where I talked about that. The coordination globally on the data standards is extremely important. The standard would not be a standard without global coordination in the Legal Entity Identifier and other related projects.

Second, we do regularly coordinate with our counterparts globally under the aegis of the Council, in order to exchange information and the way that we approach looking at information and filling gaps in data. That is extremely important for all of us, because some of those gaps exist on a global basis.

So we regularly compare our work with that of other central banks and with other macro prudential, if I can use that term, agencies in Europe and Asia and around the world.

That is an important part of our work. It has only begun, and we have a lot more to do in that area.

Mrs. BEATTY. Let me ask one other thing. My colleagues have asked you a lot of questions about how you will respond to whether it is an administrative rule or how you will respond to Congress. Is there anything that you have not shared with us that you would like to add that would let us know how you will notify Congress and the public about potential threats to the financial system and to the economy?

Mr. GERETY. Congresswoman, I think that the issue you raised is an important one. Although there are some regular ways for the Council required in Dodd-Frank to report to Congress on its activities, and to publicly state its view about both its activities and its priorities with respect to risk, we also have to recognize that risks may not arise on a natural calendar-year cycle.

I think in light of that, what you have seen in the work of both the Council and the OFR is a determined effort to address risks as they arise, to meet on those risks, and if necessary, to make public recommendations or public proposals for recommendations, as you saw last fall with money market funds.

Mrs. BEATTY. Okay. Thank you.

Chairman MCHENRY. I thank the gentlelady, for her promptness, especially.

Thank you.

We will now recognize Mr. Grimm of New York for 5 minutes.

Mr. GRIMM. Thank you, Mr. Chairman.

And I want to thank you all for testifying today. I appreciate your time.

Just to follow up, Mr. Gerety, you were just mentioning derivatives regulations and the coordination internationally and how important it was and how you had been very active, the Council has been very active.

So, given that the FSOC's role to promote this international competitiveness, I wanted to ask about Basel III. The Basel III implementation specifically related to derivatives, since you mentioned that.

It is my understanding that the international Basel III agreement introduced a new derivatives capital requirement, the credit valuation adjustment (CVA), which is intended to minimize counterparty exposure for uncleared swaps.

But it is also my understanding that the E.U. recently proposed in its implementation to Basel III, I think that is CRD IV, that based on that proposal it would create an exemption to CVA capital—the capital mandate for European banks transacting with corporates, sovereigns, pension funds.

So, obviously, U.S. proposals reflecting Basel III that include CVA, it looks like the E.U. wants to exempt a lot of that. So the question is, has the FSOC done any analysis on the impact of this inconsistency? Would both U.S. firms at home and abroad, and U.S. businesses that use derivatives be at a disadvantage, and has the FSOC looked at that?

Mr. GERETY. Congressman, I am not specifically aware of the particular exemptions that you are talking about in the E.U. proposals, but I think the general point is an important one, which is Basel III, as you know, is not binding in its agreement itself. It is promulgated through rules in the United States, and then in rules around the world.

Therefore, the question about how that agreement is interpreted and implemented in a consistent way is very important, both to the competitiveness issues that you talked about, but also to the financial stability issues, which is, if the aim of these international agreements is to assure a level playing field, both on risk and on competition, then it is very important that the financial system is adequately protected in each area.

Mr. GRIMM. I have limited time. You are basically just regurgitating the purposes. We all get that. My question is—and if you don't have it with you, if you could please submit it to the committee—has the FSOC specifically looked at it? The E.U. has come out with their proposals and said, "We are carving out an exemption." And I think I listed pension funds is one example. Sovereigns, another. Corporates, another.

That would certainly put U.S. entities at a big competitive disadvantage, so I would ask that you submit that to us to see if FSOC is—if they haven't looked at it, if they intend on looking at it, what analysis—the impact that it would have.

If U.S. financial firms have a mandated capital charge that is separate from margin. I want to be clear about that. It is the new CVA—effectively impacting the pricing that they can extend clients. Would you agree that if the E.U. does this exemption, it would limit the competition in services for U.S. businesses in an undesirable way?

Is that something you would agree with?

Mr. GERETY. Congressman, I don't want to comment on a specific exemption. I am not totally familiar with the point that you raise. However, I do think the general point of the consistency, both in terms of risk and in terms of competition, is something we value.

Mr. GRIMM. You don't need to know the exact exemption, but would you at least say that if the rules are not consistent, that it is certainly going to put U.S. institutions at a disadvantage? Is that fair to say, which is what the FSOC is trying to avoid? Isn't that your whole purpose?

Mr. GERETY. To the issue of consistent rules, it is certainly something that we take very seriously. And I think working across a whole range of issues, not just the specifics that you are raising, consistency has been something that the Council has discussed. How is Basel III implementation going and what is going to be the impact, both domestically and internationally.

Mr. GRIMM. Okay. So, I would like for you to submit to the committee some type of analysis of the impact that, if the E.U. is, in fact, going to exempt—have a major exemption to CVA, that impact on the U.S. institutions. Can you do that?

Mr. GERETY. Congressman, I am glad to get back to you and your staff with more on this issue.

Mr. GRIMM. Is that a "yes?"

Mr. GERETY. I am glad to get back to you on this issue.

Mr. GRIMM. You hate the words "yes" and "no?" Okay.

I yield back.

Chairman MCHENRY. The gentleman from Washington, Mr. Heck, is recognized for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman.

I just want to make an observation about Reverend Cleaver's question and concern earlier about, have recent congressional actions, with respect to Federal employee compensation, deterred or harmed our ability to attract and retain a sufficient caliber of talent in order to undertake this very important task. I share that concern, but based on your respective presentations here today, I am sleeping better tonight, and I thank you for your public service.

Mr. Gerety, I have had the great privilege to spend a great deal of my career in both the public sector and the private sector, and I find that the public sector elevates certain process values pretty consistently. And the GAO report, frankly, is exhibit A: transparency; accountability; and collaboration.

In the private sector, we elevate certain other values: clarity; and the value of time. And in that spirit, I kind of went looking for some indication of when FSOC would designate non-bank financial institutions—SIFIs. I couldn't find it, so can you either disabuse me of it, or alternatively, indicate as specifically as you can when that might happen?

Or, lastly, if you cannot do that, at least give us a range, or an estimate as to when that designation will occur. Because it matters.

Mr. GERETY. Personally, I think it is an important question. While I can't speak on behalf of the Council, as I mentioned earlier, the designation standard is that a two-thirds majority vote of a Council vote, I can say that we expect those proposed designations to happen in the next few months.

Mr. HECK. Thank you.

My second and last question—I am fascinated by this question of living wills. And I guess we have the experience of the first tranche of that over on the big, big, big, big banks. I am wondering if you have had any feedback or input or questions or conversations with potential non-bank financial institutions about that requirement, which, I believe, would be associated with their designation as an SIFI, and what kinds of concerns you are hearing, and what particular challenges you would anticipate for them in that regard, especially given that the business models of the non-banks is so fundamentally different in many cases than bank financial institutions.

What are you hearing? What wisdom can you share with us? And, lastly, just how long is it going to be before you think we are at the point where we have really good living wills that make sense and fulfill the statutory objective?

Mr. GERETY. Congressman, on the question of how non-bank financial companies have thought about the living will requirements specifically, I think that actually has been less of a significant area of concern. One of the best public records of this is the comment processes that we have gone through in the non-bank financial companies.

We did an Advance Notice of Proposed Rulemaking, our first proposed rule. We actually, based on that comment, did a second proposed rule, and then finally, finalized the rule.

So we did get a very wide range of input from industry academics and others on how non-bank financial companies were thinking about designation. In particular, they were very focused, as you note, on the differences in business model and making sure that when the Fed applies enhanced credential standards, it does so in a manner that respects and reflects those different business models.

I think within that, the living will requirement is a significant requirement, but it asks the firms to design on the basis of their operation how they would go through an orderly liquidation in bankruptcy, and therefore, I think that requirement can be applied to a very wide range of business models. So we haven't heard a significant concern about that requirement, but rather, more on the general imposition of enhanced prudential standards and making sure they respect and reflect the differences in business models across the wide range of non-bank financial companies.

Mr. HECK. Thank you. I yield back the balance of my time.

Chairman MCHENRY. We will now recognize Mr. Hultgren of Illinois for 5 minutes.

Mr. HULTGREN. Thank you, Mr. Chairman.

I want to return to FSOC's responsibility under Section 112 to enhance the competitiveness of U.S. financial markets and to "facilitate information-sharing and coordination" between member agencies. Despite repeated assurances of coordination, we are beginning to see regular breakdowns in joint rulemakings, guidances, and definitions between the CFTC and the SEC—the Volcker Rule, what is a U.S. person, extraterritoriality rules, swap execution facilities.

Mr. Gerety, what steps is FSOC taking to ensure these agencies are properly coordinating their Dodd-Frank rulemakings, specifically with SEFs?

Will the FSOC commit to ensure that the SEC's and CFTC's proposals are substantially similar and released at the same time?

Mr. GERETY. Congressman, I think the Council has been very active in coordinating with the SEC and the CFTC and discussing their progress on on rulemakings as well as rulemakings more generally.

Mr. HULTGREN. So do you think they will—is there a commitment that those will be released at the same time and be substantially similar?

Mr. GERETY. Congressman, when it comes to the SEC or the CFTC, which are independent agencies, the Council cannot determine their rulemaking processes or their rulemaking timeline, so I can't make that commitment.

But I can say that there is lots of evidence of the SEC and the CFTC working very closely together, and we think that coordination is very important.

Mr. HULTGREN. Ms. Clowers, I wonder if you could follow up on this? Are you concerned that regulatory uncertainty and undue complexity will result if the FSOC fails to coordinate important rulemaking, like the SEF rules?

Ms. CLOWERS. In our report, we discuss the importance of coordination. And certainly, those are potential outcomes if rules are not properly coordinated.

Mr. HULTGREN. So, you have some concern on that?

Mr. Gerety, Federal Reserve Chairman Bernanke has warned that the U.S. derivatives regulation has to be coordinated internationally or we risk "a significant competitive disadvantage."

The CFTC and the SEC were instructed to coordinate internationally, but I heard testimony from foreign regulators in the Agriculture Committee that concerned me.

What steps has the FSOC taken to ensure that none of its member agencies issue regulations that run counter to the "establishment of consistent international standards?"

Mr. GERETY. Congressman, I think the importance of coordination and consistent rules is one that the Council has spent energy on. However—

Mr. HULTGREN. What steps have they taken? I recognize it is important to them. What steps have been taken?

Mr. GERETY. The Council has discussed this issue on a number of occasions. At the staff level, we are in very frequent conversation, both with the SEC and the CFTC and together. And I know that those agencies themselves are in near constant contact on the coordination of those rulemakings.

Mr. HULTGREN. So the steps would be just really the contact that has happened? There is nothing beyond that?

Mr. GERETY. With respect to coordination, I think what you can expect from regulatory agencies pursuing their independent statutory authorities is that they work very, very closely together to try and promulgate consistent rules.

Mr. HULTGREN. Do you agree that substantive differences in rulemaking and interpretation between the SEC and the CFTC could increase compliance costs and hurt U.S. competitiveness?

Mr. GERETY. I think, Congressman, this is an area that is quite complex, but, nonetheless, I think the importance of substantively consistent rules, consistent also with the statute, is something that we would think is very important.

Mr. HULTGREN. So you would say yes?

Mr. GERETY. Congressman, I think—

Mr. HULTGREN. Substantial differences in rulemaking and interpretations could increase compliance costs. Yes, it could, or no, it couldn't?

Mr. GERETY. Congressman, I think we have to look at compliance cost in relation to the statutory language. And both the SEC and the CFTC are working very hard to coordinate with each other—

Mr. HULTGREN. The reason they would be coordinating is because they would see compliance costs hurting U.S. competitiveness if they don't coordinate. Is that right?

Mr. GERETY. I think not just competitiveness, but also from a risk perspective, we want rules to be consistent. That is something that the regulatory community has been very straightforward on, which is an important value.

Mr. HULTGREN. My time is winding down. You clearly have both a coordination and a competitiveness mandate. Do you or do you not acknowledge that this disruption which really is right before our eyes—certainly it is reported in The Wall Street Journal—Republican and Democratic Commissioners at the CFTC and the SEC have raised concerns, and foreign regulators came to Congress to cry foul and warn about the impact to U.S. institutions.

Again, I wonder if you could comment on this, then, what—if you can't comment on this, what specifically is your role?

Mr. GERETY. The role of the Council I think, as you identified, is a broad role of coordination, information-sharing, and to facilitate that among regulators.

What I think you are asking about is the Council's role with respect to specific regulatory priorities of the SEC and the CFTC in the specific conduct of those rulemakings.

I would note I think in the issues that you have raised, these are not final. And so, my understanding is that the regulators are working very closely together to take in these comments and to try to work—

Mr. HULTGREN. My time is up. But just to clarify, my concern is the confusion and lack of coordination is leading to hurting U.S. competitiveness and leading to uncertainty. And I think that is a real problem.

My time has expired. I yield back, Mr. Chairman.

Chairman MCHENRY. And, without objection, Mr. Garrett is recognized for 5 minutes for the purpose of asking questions.

Mr. GARRETT. I thank the chairman.

I was going to go down one road, but Mr. Hultgren's questions lead me to follow up with Mr. Gerety on the—so, you believe that there has been substantial coordination between the SEC and the CFTC on the promulgation of the rules?

Mr. GERETY. Congressman, I do believe that the Council—that the Commission staff both at the SEC and the CFTC have been in very frequent, near constant contact on the coordination of these rulemakings.

Mr. GARRETT. Does constant contact also mean that they are actually running on the same timeline?

Mr. GERETY. Congressman, I can't speak to the rulemaking timelines of the CFTC or the SEC.

Mr. GARRETT. So it would not be—in order to have coordination, wouldn't one have to come out not before the other? Why has one agency come out today and then the other one comes out a year from now and say that we have done so in a coordinated manner? How can the market respond to that?

How can that be called coordinated?

Mr. GERETY. Congressman, I think what you are identifying is an issue between the nature of the process—is it a coordinated process, are people working together—

Mr. GARRETT. And when it is not coming out at the same time, would you say that is—I would say that is uncoordinated. Wouldn't you?

Mr. GERETY. I think what we can recognize in the process we have seen to date is staff working together, the Commissions having joint public roundtables, the Commissions working together, the Council helping to facilitate dialogue in this area and information-sharing in this area.

Mr. GARRETT. So what you are saying is that you are looking at the process, but not at the end result. And so, as long as there is process that is going in the right direction, in other words everybody is having a meeting once a week or talking every so often, that is satisfactory. But if the end result is an uncoordinated timeline or an uncoordinated result, that is something you don't care about. Is that what you are telling me?

Mr. GERETY. I think that the Council and the Treasury believe very firmly that it is important for the rules to be consistent at the level of substance as well.

Mr. GERETY. However, I would note that the SEC and the CFTC are independent regulatory agencies. Each of those Commissions needs to make decisions about their rulemaking.

Mr. GARRETT. And so in this area, you are saying that your authority—the Council's authority is limited.

Mr. GERETY. The Council's authority is limited. It cannot determine the rulemaking decisions of independent regulatory agencies.

Mr. GARRETT. Absolutely no authority in that area.

Mr. GERETY. The Council I think—I wouldn't say—I think the question that you may be referring to is the Council does have authority to make recommendations in that area. And I think we have taken that and used that authority in some instances.

But with respect to changing the independence of the SEC or the CFTC, the Council does not have authority.

Mr. GARRETT. So do you look at it from a risk basis, that if they operate on a different timeframe and end up with different—end up with basically different rules, that you could have arbitrage as far as which way companies will go, based on different rules?

Mr. GERETY. Certainly, Congressman, the issue of consistency, both in terms of timing and of substance, is one that we think is important.

Mr. GARRETT. And if that was the case, and if you found that regulatory arbitrage was going to potentially be the State, because they are coming out on an inconsistent basis and they are coming out on an inconsistent timeline, wouldn't that give you authority to act in that case?

Mr. GERETY. Congressman, I think we need to make a distinction between what the Council's actions can be. The Council, as you know, is made up of its members. The SEC Chair and the CFTC Chair sit on the Council, so we work very closely with them on the progress of Dodd-Frank implementation generally.

And also, in terms of the Council's authority, the Council has authority to make recommendations to independent regulatory agencies with respect to issues that could relate to financial stability.

Mr. GARRETT. So, in other words, the timeframe is really not a factor for you, as far as trying to assess the risk assessment of the matter. As long as they come out with a final product that is satisfactory, then it is okay.

Mr. GERETY. Congressman, I think the timeframe may be important. We certainly are working closely with the regulating community—

Mr. GARRETT. Does that explain why you became involved with the SEC in the money market fund situation, that you were not satisfied with the timeframe there, and you decided to insert your influence in that area, but you decide, where there could not be any regulatory arbitrage, but here is an area where you could have regulatory arbitrage, and some would suggest that you would already see it, as industry begins to, in anticipation of the rules, with one agency moving at a breakneck speed, and another agency moving at a more thoughtful manner, that you could see the arbitrage occurring now.

Does that explain why you take two different approaches to this? Or why do you take two different approaches to it?

Mr. GERETY. I think with the issue that you identify in money market funds, what the Council saw is the SEC not being able to take an action to have a public dialogue about the risks and structural vulnerabilities in money market funds.

And the Council saw that as an issue and decided to put out for proposed recommendation a number of possible reforms to the—

Mr. GARRETT. Wait a second. Isn't that what you just said was the role of the regulator, that you are not—you don't have the authority to get into there?

Isn't that what the SEC had said that they wanted to do as a regulator? Isn't that the SEC who wanted to do a study?

And all of a sudden, you decided, as a Council, to interfere in that area by moving forward?

But in this other area, much more—very complex other area that really is ripe for consistency, you decided to have a hands-off approach. I see that as being inconsistent from your perspective, and they are potentially causing risk to the market.

But, with that, I believe my—

Chairman McHENRY. Yes, your time has expired. I appreciate the chairman of the Capital Markets Subcommittee.

I will now recognize the vice chair of the subcommittee, Mr. Fitzpatrick, for 5 minutes.

Mr. FITZPATRICK. Thank you, Mr. Chairman.

Mr. Gerety, does your transparency policy include any requirements about giving public notice of your Council meetings?

Mr. GERETY. Congressman, I don't think that our transparency policy speaks specifically to the public notice of Council meetings.

However, I would note that the Council has established a process whereby when possible, the Council notices public meetings 7 days in advance.

Mr. FITZPATRICK. What does that mean, "when possible?"

Mr. GERETY. For example, there were a number of instances when the Council has had conference calls in relation to specific market events or other concerns, and those meetings had not even been scheduled 7 days in advance, so it wasn't possible to notice those meetings 7 days in advance. In that instance, such as during Superstorm Sandy or in response to the downgrade of U.S. debt in August of 2011, the Council, obviously, did not provide public notice 7 days in advance. But the general practice that we have tried to adopt as we become more mature is to provide a week's notice for meetings.

Mr. FITZPATRICK. Were there instances where you had public meetings but you didn't provide public notice of it during the superstorm?

Mr. GERETY. During the course of the Council's development, I can't recall off the top of my head when we started this practice of noticing meetings 7 days in advance, but I can tell you that the general practice we have adopted is to—and I think we will continue going forward—is to notice meetings 7 days in advance.

Mr. FITZPATRICK. And what is the rationale for explicitly excluding any reference to a requirement for noticing public meetings in advance in the policy?

Mr. GERETY. Congressman, I can't speak specifically to that rationale. I think at the time, the transparency policy was trying to address the transparency of the Council's operation.

As we have gone through the 2½ years of the Council's existence, as we have had dialogue with both public market participants, and others like the GAO, we have looked for ways to improve our transparency and our accountability, and I think this is one of the steps that we have taken to try and improve our processes and be more transparent in noticing public meetings on a regular basis.

Mr. FITZPATRICK. So under the policy as currently drafted and as it is being followed, are there any circumstances in which FSOC is actually required to give public notice of a meeting?

Mr. GERETY. Congressman, I don't think the policy speaks to public notices, but I can tell you what the practice is. We have adopted the practice of—and I think our records show that we are following that practice of noticing meetings 7 days in advance.

Mr. FITZPATRICK. Why doesn't FSOC transcribe the minutes of the meetings, the specifics other than what was referenced earlier in the hearing here? That you might have a public meeting and the entire minutes are a page-and-a-half, including the attendees. Why don't you transcribe them?

Mr. GERETY. Congressman, I can't speak to the Council's decision about how to record and whether to transcribe minutes. I can say that we have heard that recommendation from the GAO and we are looking broadly at ways to continue to improve transparency and accountability, and we will consider that as go forward.

Mr. FITZPATRICK. Wouldn't you agree that a transcription of a meeting is a much better record of the meeting rather than a very sparse page-and-a-half of minutes?

Mr. GERETY. Congressman, I think the question that you are raising is a question about how to balance the goals of keeping confidential information, market sensitive discussions confidential while also providing sufficient transparency and accountability to the public. And I think that is a balance that the Council is working to strike.

Mr. FITZPATRICK. Director Clowers, in your audit did FSOC articulate a reason that justifies its failure to transcribe the minutes in the meetings?

Ms. CLOWERS. It was similar to what Mr. Gerety has offered in terms of protecting confidential information and looking to strike the right balance in providing the information and that transparency in protecting information.

But, again, we have noted the importance of transparency in all the decision-making, and we point to the Federal Reserve, Federal Open Markets Committee, which provides more information. Even 3 weeks after the meeting, they will provide more detailed minutes and then later will release transcripts.

Mr. FITZPATRICK. So this is how FSOC compares to the Federal Reserve? You are saying the Federal Reserve is much more transparent, provides more information, including a transcription?

Ms. CLOWERS. Correct.

Mr. FITZPATRICK. Director Clowers, is FSOC subject to the Sunshine Act?

Ms. CLOWERS. This is a question that I have talked to our attorneys about, and it is my understanding that it goes to the definition of "agency." And we haven't been able to find any type of definitive court rulings about whether FSOC would be defined as an agency. But it is my understanding that they would not.

Mr. FITZPATRICK. Mr. Gerety, can you agree that the Council would subject itself to the Sunshine Act?

Mr. GERETY. Congressman, I can't commit on behalf of the Council—

Mr. FITZPATRICK. Would you agree that it would be a good thing to be subject to the Sunshine Act? Would you agree that it would be a good thing for the Council to be subject to the provisions of the Sunshine Act?

Mr. GERETY. Congressman, the Council operates consistent with law. The Sunshine Act is a law. And I think the way that we have operated is consistent with the spirit. Certainly, in terms of public notices, we have adopted that practice, as we just discussed. But I can't speak to or commit to the Council's decisions.

Mr. FITZPATRICK. Thank you.

Chairman MCHENRY. I appreciate that.

And I want to announce as a procedural piece here, in consultation with the ranking member, there was agreement to go into a second round, to not exceed 10 minutes per side. It was a failure of the Chair to not announce that.

And by unanimous consent, that is so ordered.

So with that, I will recognize myself for 5 minutes.

Ms. Clowers, is the Attorney General a member of the FSOC?

Ms. CLOWERS. The Attorney General? No.

Chairman MCHENRY. The Attorney General is not.

The Attorney General said in December, "The impact on the stability of the financial markets around the world is something we take into consideration. We reach out to experts outside of the Justice Department to talks about what are the consequences of actions that we might take," meaning Justice, "that would be—and what would be the impact of those actions. We want to make particular prosecutive decisions or determinations with regard to particular institutions."

Mr. Gerety, has the FSOC been consulted by the Justice Department as it relates to financial institutions?

Mr. GERETY. My understanding is that the Justice Department reached out to Treasury but not to the Council as a whole.

Chairman MCHENRY. To the Treasury Secretary?

Mr. GERETY. I am not personally aware of the officials within the Treasury who engaged with the Department of Justice on this question. I can say that my understanding is that the Treasury was not able to offer a meaningful assessment of the impact.

However, I think the issue that you raise—

Chairman MCHENRY. Were you directly or indirectly contacted by the Justice Department in regard to this matter?

Mr. GERETY. Personally, I was not engaged in those conversations, but I—

Chairman MCHENRY. Mr. Berner, were you?

Mr. BERNER. No, sir.

Chairman MCHENRY. Were any members of your staff?

Mr. BERNER. No, sir.

Chairman MCHENRY. Mr. Gerety, are you the designated staff person within Treasury as it pertains to the FSOC?

Mr. GERETY. There are—

Chairman MCHENRY. It is not a trick question. It is simply yes or no.

Mr. GERETY. I do run an office within Treasury that supports the Council's activity.

Chairman MCHENRY. And your title is what?

Mr. GERETY. I am the Deputy Assistant Secretary for the Financial Stability Oversight Council.

Chairman MCHENRY. All right, I am not trying to be tricky with you.

And you were not contacted by the Justice Department or any individuals within the Justice Department about potential prosecutions against institutions or individuals within financial institutions?

Mr. GERETY. I was not personally contacted.

Chairman MCHENRY. Okay.

Dr. Berner, has OFR done any analysis about what the impact would be of a prosecution of an individual or a financial institution?

Mr. BERNER. No, the OFR has not done any such analysis.

Chairman MCHENRY. Is the OFR planning any such data collection and analysis?

Mr. BERNER. The OFR is not planning any such analysis. However, if the Council directed us to look at any question related to financial stability, that would be the way in which we would undertake any analysis.

Chairman MCHENRY. Okay.

The Attorney General testified on March 6th before the Senate Judiciary Committee and said, "I am concerned that the size of some of these institutions becomes so large that it becomes difficult for us to prosecute them when we are hit with indications that if you do prosecute, if you do bring a criminal charge, it will have a negative impact on the national economy, perhaps even the world economy. And I think that is a function of the fact that some of these institutions have become too large, and I think it has an inhibiting influence and impact on our ability to bring resolutions that I think would be appropriate."

Let me ask once again. Dr. Berner, have you provided any data or information to the Justice Department about potential impacts of prosecutions of individuals and financial firms or financial firms?

Mr. BERNER. No, we have not.

Chairman MCHENRY. Okay. Ms. Clowers, I know you are not a Justice Department official, but you are a financial services expert.

Is this capacity within the Justice Department?

Ms. CLOWERS. We have not examined the Justice Department to make this type of determination.

Chairman MCHENRY. Do you examine institutions that have financial services expertise within government?

Ms. CLOWERS. Yes, we do.

Chairman MCHENRY. And you have not done any analysis within the Justice Department?

Ms. CLOWERS. That is correct.

Chairman MCHENRY. Not to say the Justice Department lacks that authority or expertise, but you are simply not aware of that expertise?

Ms. CLOWERS. I am not aware of that expertise, correct.

Chairman MCHENRY. Okay.

Mr. Gerety, is there any intention by your office and your staff to do this analysis that I have asked Dr. Berner about?

Mr. GERETY. Congressman, I think the question you are asking is, would the—

Chairman MCHENRY. The question, I will repeat, is, do you have any plans to conduct an analysis at this moment? Do you have any plans?

Mr. GERETY. The Council is not taking up this matter specifically. However, I think the broader issue about how to deal with the risks of large, complex financial institutions is addressed comprehensively in the Dodd-Frank Act.

Chairman MCHENRY. Okay. And, therefore, the Attorney General is wrong in his analysis?

Mr. GERETY. I think the Attorney General is speaking to prosecutorial decisions. Those are his decisions to make. And more generally, I think the point that bears repeating is that no firm—no institution is above the law.

Chairman MCHENRY. Thank you. My time has expired.

Mr. Green?

Mr. GREEN. Thank you, Mr. Chairman.

Let me start with our GAO representative.

Does your report in any way contain any information related to the subject matter that was just called to your attention?

Ms. CLOWERS. Did the issue of—

Mr. GREEN. Did you audit in any way the Attorney General or any of the concerns raised by the Attorney General?

Ms. CLOWERS. No.

Mr. GREEN. And what is the style of this hearing today, as you understand it?

Ms. CLOWERS. I am sorry, the style?

Mr. GREEN. The style—the topic—the title?

Ms. CLOWERS. The title—the focus was on our report on FSOC and OFR.

Mr. GREEN. And did you come prepared today to talk about the Attorney General and inquiries that he may have made to certain agencies?

Ms. CLOWERS. No.

Mr. GREEN. Is this something that is totally unexpected as it relates to you and your purpose for being here today?

Ms. CLOWERS. Certainly over the past few months, we have seen this in the press, in addition to talking about it.

Mr. GREEN. But I am talking about as it relates to your report, is this something that is totally unexpected as it relates to your report?

Ms. CLOWERS. Correct.

Mr. GREEN. Are you afraid to say this is something that is totally unexpected—

Ms. CLOWERS. Oh, it is not related—

Mr. GREEN. —as it relates to your report?

Ms. CLOWERS. —to our report.

Mr. GREEN. All right. So this is beyond the scope of your report?

Ms. CLOWERS. Yes, it is outside of our scope.

Mr. GREEN. You say this without hesitation, reservation, or equivocation?

Ms. CLOWERS. Yes.

Mr. GREEN. Now, let's talk to our representative from FSOC.

Do you have a mandate that requires you to supervise in some way—well, do this. Give us the entities that come under the purview of your jurisdiction.

Mr. GERETY. Congressman, the Council is created among its members to address a broad range of risk related to financial stability that is embodied within the non-bank designation—

Mr. GREEN. Can you pull the microphone a bit closer, please?

Mr. GERETY. —Sure—that is embodied within the non-bank designations authority within a variety of recommendation authorities. So in that sense, the Council has a broad mandate to facilitate information-sharing and coordination on issues in the financial system that could relate to financial stability.

Mr. GREEN. And as it relates to the Attorney General, do you have any supervisory authority over the Attorney General?

Mr. GERETY. The Attorney General is not a member of the FSOC and the Attorney General's decisions on prosecutorial matters are up to the Attorney General and the Department of Justice.

Mr. GREEN. What did you come prepared to talk about today?

Mr. GERETY. Congressman, I was prepared to speak to the GAO report, and also to broad matters that are before the Council.

Mr. GREEN. Let's talk to our member from the Office of Financial Research.

What were you prepared to talk about today, sir?

Mr. BERNER. Congressman, I came here prepared to talk about the role of the Office in serving the needs of the Council, as well as the recommendations from the GAO with respect to our mandate.

Mr. GREEN. And finally, do this for me. Clarify, if you would, liquidity versus solvency. There was some information accorded, and I don't think clarity was provided. Can you make it as transpicuously clear as possible, please, in terms of liquidity versus solvency? Include clawback in there, if you would, such that people will understand that taxpayers have no money that will be at risk in the final analyses.

Mr. GERETY. Congressman, I think the most important statements in the Dodd-Frank Act with respect to solvency and the actions taken in a crisis are really in Title II, which bears on the Orderly Liquidation Authority. And Title II makes it very clear that no taxpayer funds shall be used to prevent the liquidation of any financial company under the title.

What that means is that no financial firm will be protected from its own mistakes by actions of government or the use of taxpayer funds.

There is, I think, more broadly in the financial system, an understanding that in certain instances, like the discount window, the Federal Reserve is able to provide a lender of last resort function to banks.

But the important action of Dodd-Frank is to make clear that taxpayers can bear no losses in the liquidation of any firm, and that the government cannot prevent the liquidation of any financial firm, no matter how large or complex.

Mr. GREEN. Mr. Chairman, I believe that pursuant to our agreement, the time has expired. And if this isn't true—the agreement that we have—I would ask that you move to sound the gavel and call this meeting adjourned.

Chairman MCHENRY. I certainly appreciate the ranking member, and I certainly appreciate the testimony of the witnesses today.

Mr. GARRETT. Mr. Chairman, even though I am not a member of the committee, I will seek unanimous consent for an additional 5 minutes.

Mr. GREEN. Mr. Garrett knows that I love him dearly, but unfortunately, I have an appointment with the President of the United States of America. We have a meeting with him. You have already had yours, so I am going to have to step away and respectfully decline the—

Mr. GARRETT. Would it be of any assistance if I told you we had a 2-hour meeting and not very much came out of it so that—

[laughter]

Mr. GREEN. Well, not everybody who looks at Mount Rushmore sees Presidents. So it depends on your perspective, I suppose.

Mr. GARRETT. I understand that, thank you. I yield back.

Chairman MCHENRY. The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, I do want to close by thanking the witnesses for their service in our government. Thank you for answering the questions, and we certainly appreciate your willingness to respond to the written questions that we will certainly have as a follow-up.

Thanks so much. And without objection, this hearing is adjourned.

[Whereupon, at 12:43 p.m., the hearing was adjourned.]

A P P E N D I X

March 14, 2013

Testimony of Richard Berner, Director of the Office of Financial Research, U.S. Department of the Treasury
House Financial Services Subcommittee on Oversight and Investigations
Hearing on "Who is Too Big to Fail? GAO's Assessment of the Financial Stability Oversight Council and the Office of Financial Research"

March 14, 2013

The views expressed in this testimony are those of Richard Berner, Director of the Office of Financial Research, and do not necessarily represent the views of the President.

Introduction

Chairman McHenry, Ranking Member Green, and other members of the subcommittee, thank you for the opportunity to discuss the role of the Office of Financial Research (OFR) in supporting the Financial Stability Oversight Council (Council) and its member organizations. As we work to fulfill the mission of the OFR, we are fully committed to being transparent and accountable to the Congress and the public.

As we discussed when I last testified before this subcommittee, Congress created the OFR through the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) to improve the quality of financial data available to policymakers, and to develop better tools and analysis to understand the risks in the financial system.

The OFR's independent data-and-research work supports the activities of the Council, which is responsible for identifying risks to the financial stability of the United States, promoting market discipline, and responding to emerging threats. The complementary mandates of the OFR, the Council, and its member organizations enable us comprehensively to assess and monitor the stability of the financial system. The OFR's regular collaboration and coordination with them enables us to work toward achieving our shared mission, while avoiding duplication.

The OFR is committed to the highest level of transparency and accountability in pursuing our agenda. We publish the results of our work on our website, in our Annual Report, in six published working papers, and in press releases and blogs documenting important developments. We have hosted two conferences jointly with the Council, and numerous workshops and seminars to exchange ideas with other researchers and data scientists. We have created the Financial Research Advisory Committee to advise the OFR and, as required under the Federal Advisory Committee Act, the Committee holds open meetings and makes public its recommendations. With speeches and participation in panels, OFR officials regularly engage in public events and meetings with stakeholders in industry, and the research, data, and global regulatory communities.

The Office reports regularly to Congress and others charged with oversight. In December, as required under the Dodd-Frank Act, the Office issued its 2012 Annual Report to Congress on

Human Capital Planning, the second in the series. The Office routinely communicates with Congressional offices and committees, and OFR officials have testified before this and other committees. The Office also engages regularly in audits with inspectors general and the Government Accountability Office (GAO).

In my testimony today, I will describe the OFR's major accomplishments and key priorities. As you requested, I will also describe actions the OFR has taken in response to a report by the GAO in September 2012 entitled, "New Council and Research Office Should Strengthen the Accountability and Transparency of Their Decisions."

OFR Accomplishments

The OFR has made significant progress in fulfilling its primary data-and-research responsibilities.

Data and Analysis to Support the Council: The OFR has been active in providing key data and analysis that have informed the Council's work. These activities have included and will continue to include:

- Supplying data and analysis for the work of the Council's nonbank designation committee, including analysis of the asset management industry;
- Providing data and staff support for producing the Council's 2013 Annual Report;
- Acquiring, managing, protecting, and securely making available to the Council and to its own researchers the data needed for assessing and monitoring threats to financial stability;
- Supporting the Council's Systemic Risk Committee by reporting regularly on developments in financial markets and activities, in financial stability measures, and in macroeconomic indicators; and
- Conducting research and analysis, and monitoring risks related to short-term funding markets, money market funds, hedge funds, credit default swaps, and other areas.

Legal Entity Identifier: To improve the quality of financial data, the OFR is working to establish standards for data collection and usage. Standards enable us to aggregate and compare data on an apples-to-apples basis. Standards also facilitate our analysis of interconnections among financial firms and their counterparties, and help us to understand the transmission and amplification of stress across the financial system.

For industry, these standards also have benefits, enabling firms to report the same data to regulators as they use to manage risks and to run their management information systems, thereby reducing reporting burdens. Standards also reduce industry costs for collecting, cleaning, and aggregating data.

The OFR has played a central role in the international data-standards initiative to establish a global Legal Entity Identifier (LEI), a code that uniquely identifies parties to financial transactions and links to their basic "business card" information. The OFR's Chief Counsel was recently selected as the first Chair of the Regulatory Oversight Committee, which was formed to lead and direct the LEI implementation under a mandate from the Group of 20 leading global economies.

We plan to extend our collaborative work on data standards by developing best practices for the hierarchies that map the relationships among entities or products. For example, legal entity hierarchies define the relationships, such as ownership and control, among legal entities engaged in financial transactions.

Organizational Build-Out: To accomplish its mission, the OFR needs a talented workforce and a world-class and secure technology infrastructure.

Workforce – The OFR employs 140 staff—an increase of 27 percent since the GAO report was issued. That number is expected to roughly double to 275-300 by FY2014-2015, when we plan to reach a steady-state staffing level. The OFR has also filled seven of its nine senior management positions at the Director, Deputy Director, and Chief levels, and in December issued its 2012 Annual Report to Congress on Human Capital Planning.

The OFR has created a Fellowship Program, through which experts from academia, state regulatory agencies, non-profit organizations, and other federal agencies may spend up to two years at the OFR performing research and conducting advanced training of OFR employees. The Fellowship Program facilitates the sharing of new methods and approaches to identifying and analyzing threats to financial stability. The OFR's first Executive Fellow is a Professor of Economics at Johns Hopkins University.

Technology Infrastructure – The Office has put in place a short-term analytical environment for its researchers, as well as agreed-on processes and a collaboration environment for the secure exchange of data with other Council member organizations. To log, track, and follow-up on responses to requests to the OFR for data and services, the OFR is establishing an online service desk. The Office is currently building upon its foundational infrastructure to create a long-term secure analytical environment, leveraging advances in current technologies related to data management.

No OFR goals are more important than safely and securely collecting data and safeguarding the data we hold. The Office is governed by Treasury information security standards, and our Chief Information Security Officer works closely with his Treasury counterpart to assure that our policies and procedures meet or exceed the standards of the Treasury Department, as well as the standards of Council member organizations. As required by the Federal Information Security Management Act, the Office has established an information security program policy and data handling procedures for proper safekeeping of information at the highest level of the Federal Information Processing Standards.

First Annual Report: The OFR's first Annual Report, released on July 20, 2012, included a framework for evaluating threats to financial stability, a comprehensive exploration and identification of current risks, and thorough discussions of OFR's activities. The report also described the OFR's agenda related to data and research, and the types and sources of data that the OFR will need to fill data gaps and fulfill its mission. In addition, the report contained a selection of OFR research and a primer on data standards. The report is on the OFR's website at http://www.treasury.gov/ofr.

Working Paper Series: The OFR has released six working papers, including four new papers published this year, focusing on topics such as systemic risk analytics, best practices in risk management, agent-based modeling, and hedge fund contagion. The Working Paper Series makes accessible the OFR's in-depth work to analyze and measure threats to financial stability. These papers, some developed in partnership with national experts, are intended to promote discussion among researchers and subsequent feedback that helps the OFR fine-tune its research. The papers are all available on the OFR's website at http://www.treasury.gov/ofr. The OFR plans to continue to increase its output of important, timely, and innovative research on financial stability topics as its research staff continues to grow and its network of partnerships with outside researchers and academics continues to mature and expand.

Seminars and Conferences: The OFR has hosted a number of conferences, workshops, and seminars to engage with experts from academia, industry, and elsewhere in government on questions related to financial stability. Specifically:

- Since 2011, the OFR has hosted more than 60 seminars as part of its Research Seminar Series, a forum in which OFR staff can exchange ideas with thought leaders in economics, finance, and other fields.
- The OFR and the Council have co-sponsored two conferences: "The Macroprudential Toolkit: Measurement and Analysis" in early December 2011 and "Assessing Financial Intermediation: Measurement and Analysis" in early December 2012.
- The OFR convened a workshop in August 2012 for academic researchers, financial market participants, and financial policymakers to evaluate stress-testing approaches and future research.
- Last month, the OFR co-hosted with other Council member organizations the third annual Regulatory Data Workshop. Experts from federal regulatory agencies discussed advances and challenges in financial data management and technologies, and identified areas for collaboration. It is notable that the first Regulatory Data Workshop helped launch initial U.S. work on the LEI.

Financial Research Advisory Committee: In November 2012, the OFR announced the membership of the Financial Research Advisory Committee, a group of 30 distinguished professionals in economics, finance, financial services, data management, risk management, and information technology. These experts provide advice to the OFR on best practices for data management, data standards, and research methodologies. The Committee first met in December 2012; minutes of that meeting are posted on the OFR website. At their next meeting, members will review the work of the panel's subcommittees, which are focused on research, data and technology, and financial services and risk management.

OFR Actions in Response to the GAO Report

The subcommittee's invitation letter asked me to address a September 2012 GAO report that reviewed the progress of the Council and the OFR in achieving their missions. The report concluded that the Council and the OFR have made progress in establishing their operations and approaches for monitoring threats to financial stability, developing mechanisms for accountability and transparency, and enhancing collaboration among Council member organizations. The report also recommended steps to improve communication with the public, to develop the OFR's strategic planning and performance management system, and to clarify responsibilities between the Council and the OFR.

The Office strongly supports GAO's important oversight function and appreciates its constructive work in conducting its review. We have been pleased to work with Nicole Clowers and her team. Their willingness to engage with us and their valuable suggestions are helping us improve our effectiveness, transparency, and accountability.

In the following three sections, I will describe the progress the OFR has made in responding to GAO's recommendations.

Improving Communication with the Public: The OFR has greatly improved its ability to provide information on its work to the public since the issuance of the GAO report. The OFR has redesigned its website (www.treasury.gov/ofr) to make it more user friendly, timely, and proactive. Launched in November 2012, the new website design and enhanced OFR capabilities offer several improvements:

- Easier navigation and better organization of Web content.
- Significantly expanded online content. For example, we routinely post on the OFR website our reports, research papers, assessment information, data standards updates, research papers, conference materials, news releases, Congressional testimony, and other information.
- Increased transparency including through a home page "slideshow" that highlights key new content and links to it.
- E-mail update alerts that flag new content; currently more than 2,000 subscribers receive the notifications.
- Analytical tools to monitor the number and timing of website visits and page views.
- Ability to update our own Web content through the site's content management system for more timely information.

To foster enhanced communication and outreach, the OFR will further enhance the website and has created a new position for a Chief of External Relations, who will lead a team responsible for communications, Congressional affairs, and outreach with industry and academia.

The OFR has also sought to demonstrate transparency and accountability in its communications by:

- Testifying at Congressional hearings and responding to Congressional inquiries;
- Providing briefings and attending meetings with members of Congress, their staffs, and the staffs of Congressional committees;
- Making routine notifications to key Congressional offices and committees about significant OFR activities and initiatives;

- Publishing the OFR Annual Report and Annual Report to Congress on Human Capital Planning; and
- Engaging in, and responding to, audits conducted by GAO, inspectors general, and others.

Further Developing Strategic Planning and Performance Management: The OFR's Strategic Framework, published in March 2012, described the OFR's long-term strategic goals, objectives, and implementation priorities for FY 2012-FY 2014. The framework also detailed the OFR's organization, workforce plan, governance, transparency, and oversight. The GAO report called the framework an important step but recommended that the Office further develop its strategic planning and performance management system by linking OFR activities to its goals, and using publicly-available performance measures to monitor its progress.

In response, the OFR has finalized a set of performance measures for each of its strategic goals (see Table 1). These measures will be included in the FY 2014 budget submission to Congress, along with specific targets for FY2013 and FY2014.

Table 1 - OFR Foundational Performance Measures

Goal	Performance Measures
Council Support	• Percent of responses to Council data and research requests that meet delivery targets • Percent of project milestones met for establishment of an interagency data inventory program
Data Standards	• Percent of milestones met in information standards strategy
Center of Excellence for Research	• Number of research products published • Number of research products coauthored or pursued in collaboration with outside researchers, government agencies, or others
Public Information	• Percent increase in the number of OFR Web page visitors
Building the OFR	• Percent of OFR implementation priorities completed • Cost of the OFR relative to total assessed assets, per $billion assessed • Total staff hired compared to targets

OFR goals and objectives continue to drive its budget and its strategies for planning, project management, and human capital. This work is reflected in documents that the OFR uses to manage its day-to-day work, as well as in congressionally-mandated reports. The forthcoming President's Budget will provide additional details on the budget projections of the OFR.

Clarifying Council-OFR Responsibilities: The GAO report acknowledged that there does not appear to be overlap in the work of the OFR and the Council, which have complementary mandates, or among the work of the Council member organizations. However, the report recommended that, to ensure comprehensive identification and analysis of threats to the financial system and to minimize duplication, the Council and the OFR clarify their respective responsibilities for monitoring threats to financial stability, as well as the roles of Council member organizations.

The OFR and the Council have strengthened steps to assure a coordinated approach to achieving their shared mission and to minimize duplication. By drawing on the collective expertise of its member organizations and the OFR, the Council and its committees facilitate comprehensive monitoring and analysis of trends and emerging risks to the U.S. financial system. The Deputies Committee of the Council serves as a coordinating entity to monitor any overlap among Council member organizations. Additionally, senior leaders of the OFR meet weekly with the Council staff to coordinate ongoing activities and to prevent duplication of effort.

The OFR and the Council also take great care not to duplicate the work of federal financial regulators, which continue to collect the data they need to monitor the financial institutions they supervise. To provide the connective tissue between the efforts of other Council member organizations and to complement their work, the OFR collaborates with them to identify and fill gaps in data and knowledge about the financial system. To that end, the OFR has conducted an inventory of data held by those organizations. By statute, the OFR must consult closely with them before collecting data from any firm, and works to collaborate on any data gathering activities beyond simple procurements.

The OFR is also fostering Council-wide collaboration on data issues through the Council's Data Committee. The Committee coordinates among Council member organizations on matters pertaining to data standards and collection. The Committee has formed working groups to address topics, such as establishing protocols for sharing data among Council member organizations and identifying data hierarchies needed for analysis.

Conclusion

Chairman McHenry, Ranking Member Green, and other members of the subcommittee, thank you again for the opportunity to appear before you today. We welcome the oversight of this subcommittee in helping to ensure that, in carrying out its mission, the OFR is fully transparent and accountable to the Congress and the public. We look forward to working with you and your staff to continue the critical task of promoting the stability of this nation's financial system.

I would be happy to answer your questions.

United States Government Accountability Office

GAO

Testimony
Before the Subcommittee on Oversight and Investigations, Committee on Financial Services, House of Representatives

For Release on Delivery
Expected at 10:00 a.m. EDT
March 14, 2013

FINANCIAL STABILITY

Continued Actions Needed to Strengthen New Council and Research Office

Statement of A. Nicole Clowers, Director
Financial Markets and Community Investment

GAO
Accountability * Integrity * Reliability

GAO-13-467T

GAO
Accountability * Integrity * Reliability

Highlights

Highlights of GAO-13-467T, a testimony before the Subcommittee on Oversight and Investigations, Committee on Financial Services, House of Representatives

March 14, 2013

FINANCIAL STABILITY

Continued Actions Needed to Strengthen New Council and Research Office

Why GAO Did This Study

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act created FSOC to identify and address threats to financial stability and OFR to support FSOC and Congress by providing financial research and data. This testimony primarily discusses findings from a September 2012 GAO report and addresses four topics (1) challenges FSOC and OFR face in carrying out their missions, (2) FSOC's and OFR's efforts to establish management mechanisms, (3) FSOC's and OFR's activities for supporting collaboration among their members and external stakeholders, and (4) FSOC's rules for designating nonbank financial firms that pose threats to financial stability.

For this testimony, GAO updated some information on the entities' response to the recommendations in its September 2012 report.

What GAO Recommends

In its September 2012 report, GAO made 10 recommendations to FSOC and OFR, which among other things, recommends ways to improve the transparency and accountability of their decisions. In response to GAO's report, Treasury said, as Chairperson, that the council and OFR had considered the recommendations. In March 2013 Treasury and OFR officials described steps that each entity was considering or taking to address some of them.

View GAO-13-467T. For more information, contact A. Nicole Clowers at (202) 512-8678 or clowersa@gao.gov

What GAO Found

The Financial Stability Oversight Council (FSOC) and Office of Financial Research (OFR) face challenges in achieving their missions. For example, collaboration among FSOC members can be challenging, as almost all members represent independent agencies that retain existing authorities. Additionally, OFR faces the challenge of building a world-class research organization while meeting shorter-term responsibilities.

FSOC and OFR have developed some management structures to carry out their missions and taken steps to promote collaboration among their members and stakeholders. For example, FSOC established several standing committees composed of members' and member agencies' staffs to support the council in carrying out its business. FSOC also issued rules on the process for designating nonbank financial firms for additional oversight. However, GAO reported in September 2012 that these efforts could be strengthened to conform to key standards and practices and made 10 recommendations.

- FSOC should develop a systematic approach to help identify potential threats to financial stability that includes collecting and sharing key financial risk indicators. FSOC's Systemic Risk Committee, which is responsible for identifying risks to financial stability, has procedures to facilitate risk analysis but does not have a systematic approach or comprehensive information. FSOC member agencies on their own may not be well positioned to judge which potential threats will benefit from interagency discussions.
- FSOC should develop more systematic approaches that are forward looking and help prioritize threats to the financial system in its annual reports. To date, FSOC's annual reports have not reflected a forward-looking process for identifying emerging threats.
- To improve transparency, (1) FSOC should keep detailed records of closed-door sessions and (2) both FSOC and OFR should develop a communication strategy to improve communications with the public. Currently, public information on FSOC's and OFR's decision making and activities is limited.
- OFR needs to further develop its strategic planning and performance management system to include some leading practices. OFR issued a strategic framework in March 2012 that did not, among other things, link activities to strategic goals and performance measurement systems.
- FSOC should identify an agency or agencies to monitor or implement each recommendation from its annual reports within specified time frames. FSOC's annual reports have not consistently identified which entities should monitor or implement the identified recommendations.
- FSOC should (1) develop policies to clarify when formal collaboration or coordination should occur, (2) more fully incorporate key practices for successful collaboration, and (3) clarify with OFR responsibility for implementing requirements to monitor risks to the financial system.
- FSOC should develop a comprehensive framework for assessing the impact of its designation decisions. For example, FSOC has issued rules on processes for designating nonbank financial entities for additional oversight, but it has not developed plans to comprehensively evaluate whether the designations are having their intended impact.

GAO
Accountability * Integrity * Reliability
United States Government Accountability Office
Washington, DC 20548

Chairman McHenry, Ranking Member Green, and Members of the Subcommittee:

Thank you for the opportunity to be here today to discuss the Financial Stability Oversight Council (FSOC) and the Office of Financial Research (OFR). As you know, the 2007-2009 financial crisis focused attention on weaknesses in the U.S. regulatory structure, including the lack of an agency or mechanism responsible for monitoring and addressing risks across the financial system and a shortage of timely information to facilitate that oversight. In response to the crisis, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) in July 2010, which provided for a broad range of regulatory reforms.[1] Among other things, the act established FSOC to monitor the stability of the U.S. financial system and take actions to mitigate risks that might destabilize the system.[2] The Dodd-Frank Act also created OFR to support FSOC and Congress by providing financial research and data.[3] Congress gave FSOC a number of significant authorities to help it execute its broad mission, including to designate nonbank financial companies for heightened supervision by the Board of Governors of the Federal Reserve System (Federal Reserve) and to require financial companies to provide data to OFR. Although Congress set up some specific accountability mechanisms for FSOC and OFR, some members of Congress have questioned whether more needs to be done to help ensure that FSOC and OFR use their authorities as Congress intended.

My testimony today will address four topics: (1) the challenges FSOC and OFR face in fulfilling their missions; (2) FSOC's and OFR's efforts to establish management structures and mechanisms to carry out their missions and attain their goals; (3) FSOC's and OFR's activities supporting collaboration among members and external stakeholders, including international bodies and regulators; and (4) FSOC's rules for

[1]Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[2]The provisions of the Dodd-Frank Act dealing with FSOC are contained primarily in subtitle A of title I, §§ 111-123, codified at 12 U.S.C. §§ 5321-5333, and title VIII, codified at 12 U.S.C. §§ 5461-5472. The following sections of this testimony describe FSOC's specific functions in detail.

[3]The provisions dealing with OFR are contained primarily in subtitle B of title I, §§ 151-156, codified at 12 U.S.C. §§ 5341-5346.

designating nonbank financial companies that pose threats to financial stability.

My remarks are primarily based on our September 2012 report on FSOC and OFR.[4] For that report, we reviewed our prior reports on financial reform and the 2007-2009 financial crisis, statements by government officials and academic experts, and agency documents, including information on the entities' budgeting, staffing, and planning. In addition, we analyzed FSOC policies, procedures, and products to determine whether and how their collaboration practices compared with key elements of effective collaboration we have previously identified and to determine processes FSOC used to issue products.[5] We also interviewed FSOC and OFR staff; officials from FSOC's member agencies; and external stakeholders, including foreign officials, industry trade groups, and academics. In March 2013, we interviewed Treasury and OFR officials to obtain updates on the progress FSOC and OFR had made in implementing our recommendations. The work on which this statement is based was conducted from November 2011 through September 2012 and in March 2013 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

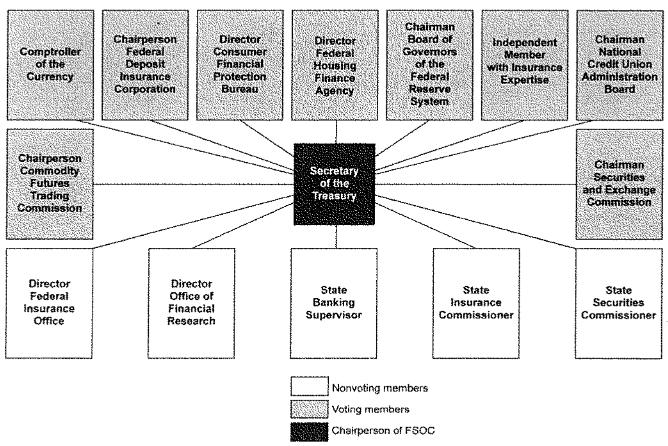
FSOC consists of 10 voting members and 5 nonvoting members (fig. 1). The 10 voting members include 9 federal regulators and an independent insurance expert. The 5 nonvoting members include state-level representatives from bank, securities, and insurance regulators and directors of OFR and the Federal Insurance Office. As the chairperson of FSOC, the Secretary of the Treasury has certain powers and responsibilities related to FSOC's meetings, rulemakings, recommendations, and reports and testimony to Congress. The

[4]GAO, *Financial Stability: New Council and Research Office Should Strengthen the Accountability and Transparency of Their Decisions*, GAO-12-886 (Washington D.C.: Sept. 11, 2012).

[5]GAO, *Results-Oriented Government: Practices That Can Help Enhance and Sustain Collaboration among Federal Agencies*, GAO-06-15 (Washington, D.C.: Oct. 21, 2005).

Secretary, in consultation with the other FSOC members, is also responsible for regular consultation with the financial regulatory entities and other appropriate organizations of foreign governments or international organizations. FSOC has established seven standing committees that are generally composed of staff of FSOC members and member agencies to help carry out the council's business.[6]

Figure 1: FSOC Membership



Source: GAO analysis of Dodd-Frank Act.

The Dodd-Frank Act established OFR to serve FSOC and its member agencies by improving the quality, transparency, and accessibility of financial data and information; conducting and sponsoring research related to financial stability; and promoting best practices in risk

[6]The committees are the Deputies Committee, Systemic Risk Committee, Designation of Nonbank Financial Companies Committee, Designation of Financial Market Utilities Committee, Heightened Prudential Standards Committee, Orderly Liquidation Committee, and Data Committee.

management. The act requires OFR to set up a data center and a research and analysis center to, among other things,

- collect and provide data to FSOC and member agencies;
- standardize the types and formats of data reported and collected;
- perform applied and essential long-term research;
- develop tools for risk measurement and monitoring; and
- make the results of its activities available to financial regulatory agencies.

FSOC and OFR Face Challenges Achieving Their Missions

FSOC and OFR face several challenges as they work to carry out their responsibilities and achieve their missions. First, FSOC's missions—to identify risks to U.S. financial stability and respond to emerging threats to stability—are inherently challenging, for several reasons. Identifying risks to financial stability is challenging because (1) key indicators, such as market prices, often do not reflect threats to financial stability; (2) such threats do not develop in precisely the same way in successive crises; (3) financial innovations are not well understood; and (4) according to experts, effectively monitoring and mitigating systemic risk is both vast and procedurally complex. In addition, actions to preemptively mitigate emerging threats may appear unnecessary or too costly at the time they are proposed or taken.

Second, although the Dodd-Frank Act created FSOC to provide for a more comprehensive view of threats to U.S. financial stability, it left most of the fragmented and complex arrangement of independent federal and state regulators in place and generally preserved their statutory responsibilities. As a result, FSOC's effectiveness in providing for a more comprehensive view of threats to U.S. financial stability hinges to a large extent on collaboration among its many members, almost all of whom have their own independent regulatory responsibilities. In testifying on the coordination of Dodd-Frank rulemakings assigned to specific FSOC members before the U.S. House Financial Services Committee in October 2011, the chairperson of FSOC recognized this challenge. However, he also noted that certain agencies were working much more closely together than before FSOC's creation. The federal financial regulators have also emphasized the importance of maintaining their independence while serving as members of FSOC. For example, several member agencies noted in our prior work on Dodd-Frank rulemakings that any effort to coordinate rulemakings assigned to specific agencies through FSOC would need to be balanced against the statutory requirements of the independent agencies involved.[7] Regulators have also pointed to their differing statutory requirements to explain why they have differing views on policy issues. During the Basel II deliberations prior to the financial crisis, for instance, U.S. bank regulators—the Federal Deposit Insurance Corporation (FDIC), Federal Reserve, and the Office of the Comptroller of the Currency (OCC)—each had a different view of various aspects of those requirements.[8] The regulators traced their differences back to their specific statutory responsibilities.

Third, OFR faces the challenge of trying to build a world-class research organization from the ground up, including acquiring staff with the needed skills, while meeting its short-term responsibility to support FSOC. The researchers who supported the creation of OFR suggested that it would take many years for the new entity to provide the insights that would ultimately be expected of it. Though OFR now has a confirmed director, these researchers had also noted that the long absence of a director for the organization had slowed this process.

FSOC and OFR Could Strengthen Mechanisms to Fully Ensure Accountability and Transparency

FSOC and OFR have taken steps toward meeting the challenges they face. For example, they have taken steps to build mechanisms to identify potential threats to financial stability, provide information to the public about their activities and progress, and establish management and planning structures. However, additional actions could strengthen the accountability and transparency of these efforts. As we have reported in the past, agencies can manage or mitigate many of the challenges of

[7] GAO, *Dodd-Frank Act Regulations: Implementation Could Benefit from Additional Analyses and Coordination*, GAO-12-151 (Washington, D.C.: Nov. 10, 2011).

[8] Basel II is a risk-based capital framework for banks that is based on an international accord. For more information on Basel II adoption in the United States, see GAO, *Risk-Based Capital: Bank Regulators Need to Improve Transparency and Overcome Impediments to Finalizing the Proposed Basel II Framework*, GAO-07-253 (Washington, D.C.: Feb. 15, 2007) and *Risk-Based Capital: New Basel II Rules Reduced Certain Competitive Concerns, but Bank Regulators Should Address Remaining Uncertainties*, GAO-08-953 (Washington, D.C.: Sept. 12, 2008).

setting up new organizations by developing strong management structures and control mechanisms.[9]

Identifying Potential Risks and Emerging Threats to Financial Stability

FSOC has taken steps to meet its statutory responsibilities related to identifying risks and potential emerging threats to U.S. financial stability but has not yet developed comprehensive and systematic mechanisms to realize these goals. These steps include setting up the Systemic Risk Committee—one of the seven standing FSOC committees—that is responsible for systemic risk monitoring and plays a key role in reviewing sources of systemic risk. The committee is operating under draft procedures, with member agency staff suggesting risks or threats that, in their view, may benefit from interagency coordination.[10] According to FSOC policy staff, if there is agreement that an issue warrants further examination, an agency is assigned to develop it, including identifying vulnerabilities in the financial system. When the committee determines that the issue is sufficiently developed, it presents the issue to the Deputies Committee. According to the draft procedures, if issues are elevated beyond the Deputies Committee to FSOC members, agencies may respond with a variety of actions, including enhanced monitoring, additional analysis, the development of potential policy responses, or the implementation of a particular policy response. Potential threats to financial stability are also discussed at FSOC meetings; for example,

[9]GAO, *Millennium Challenge Corporation: Progress Made on Key Challenges in First Year of Operations,* GAO-05-625T (Washington, D.C.: Apr. 27, 2005) and *Troubled Asset Relief Program: Additional Actions Needed to Better Ensure Integrity, Accountability, and Transparency,* GAO-09-161 (Washington, D.C.: Dec. 2, 2008). Such mechanisms include: GAO, *Internal Control: Standards for Internal Control in the Federal Government,* GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999); and *Internal Control Standards: Internal Control Management and Evaluation Tool,* GAO-01-1008G (Washington, D.C.: August 2001). For the importance of objectives and performance measures in determining accountability and efficiency, see, for example, GAO, *Results-Oriented Government: GPRA Has Established a Solid Foundation for Achieving Greater Results,* GAO-04-38 (Washington, D.C.: Mar. 10, 2004) and *Government Performance: GPRA Modernization Act Provides Opportunities to Help Address Fiscal, Performance, and Management Challenges,* GAO-11-466T (Washington, D.C.: Mar. 16, 2011).

[10]FSOC officials noted that the procedures were marked "draft" because the process was new and the committee expected to change the procedures based on its initial experience.

FSOC officials noted that a teleconference was convened to discuss MF Global's bankruptcy.[11]

OFR participates in the Systemic Risk Committee and is building capacity to monitor the financial system for threats to financial stability. OFR has developed the Financial Stability Monitor, a collection of metrics and indicators related to financial stability that is to be continuously updated, according to OFR and Treasury officials. According to these officials, OFR began sharing the Financial Stability Monitor with the Systemic Risk Committee and FSOC member agency staff in February 2012. OFR is also assessing options for analyzing risks to financial stability and produced a working paper in collaboration with outside researchers, published in January 2012 to survey existing approaches.[12] In addition, OFR and FSOC sponsored conferences in December 2011 and December 2012 to discuss a range of issues related to risks to financial stability.[13] OFR staff said that they were evaluating a range of metrics and methods for measuring and analyzing financial markets and systems and were in the early stages of developing network maps and other tools to assess financial stability. For example, OFR evaluated 11 measures against a series of crises over time and reported on some of these efforts in its 2012 Annual Report.[14]

However, FSOC and OFR have not developed a comprehensive, systemic approach to identifying and addressing threats to the financial system. Without a more systematic approach and comprehensive information, FSOC member agencies on their own may not be well

[11]In October 2011, MF Global, the third largest independent broker dealer in the United States, filed for bankruptcy. MF Global Holdings Ltd. and MF Global Finance USA Inc. filed on a consolidated basis for relief under Chapter 11 bankruptcy protection. The jointly registered broker-dealer and futures commission merchant, operating as MF Global Inc., entered liquidation proceedings under the Securities Investor Protection Act. A series of events, including increased exposure to European sovereign debt securities, preceded the bankruptcy filing.

[12]Dimitrios Bisias, Mark Flood, Andrew W. Lo, and Stavros Valavanis, *A Survey of Systemic Risk Analytics,* Office of Financial Research Working Paper #0001 (Washington, D.C.: Jan. 15, 2012).

[13]The Macroprudential Toolkit: Measurement and Analysis. Conference held in Washington, DC, December 1-2, 2011, and Assessing Financial Intermediation: Measurement and Analysis. Conference held in Washington, DC, December 6, 2012.

[14]Office of Financial Research, *2012 Annual Report* (Washington, D.C.: July 2012).

positioned to judge which potential threats will benefit from interagency discussions. FSOC and OFR could improve their efforts to identify risks and threats by collecting and sharing a common set of financial indicators.[15] Systematic collection, analysis, and sharing of financial indicators of key risk factors such as leverage, liquidity, concentrations, underwriting standards, collateral quality, and delinquencies should provide insight into vulnerabilities affecting particular types of financial intermediaries or reveal patterns occurring across the financial system. OFR, through a mechanism such as the Financial Stability Monitor, could play a role in collecting, analyzing, and reporting on these indicators. To improve FSOC's approaches for monitoring threats to financial stability, we recommended that FSOC develop an approach that included systematic sharing of key financial risk indicators across FSOC members and member agencies to assist in identifying potential threats for further monitoring or analysis.

In addition, FSOC does not have sufficient processes for identifying or prioritizing potential emerging threats to U.S. financial stability for its annual reports. FSOC's annual reporting process is an ongoing responsibility which, in the absence of a strategic plan, functions as its major strategic planning document and method for communicating with Congress and the public, especially regarding potential emerging threats to U.S. financial stability. FSOC's 2011 and 2012 annual reports generally addressed the subjects mandated by the Dodd-Frank Act. These reports also provided extensive information about the current economy and complex issues, such as high-frequency trading and the MF Global bankruptcy. In addition, the reports contained extensive discussions of current known threats, such as those associated with money market funds and the European sovereign-debt crisis, and made some recommendations to address them. However, FSOC has not developed a structure that supports having a systematic or comprehensive process for identifying potential emerging threats. In particular, FSOC does not have processes for consistently identifying such threats, separating them from more current threats, or prioritizing them. For instance, certain potential threats related to U.S. debt are not in the 2011 Annual Report. However, the 2012 Annual Report identifies the U.S. debt as a potential threat but does not explain what has changed since the 2011 report. Similarly, the

[15]Such a data-sharing exercise is akin to what the International Monetary Fund proposes with its Financial Soundness Indicators. See International Monetary Fund, *Financial Soundness Indicators: Compilation Guide* (Washington, D.C.: March 2006).

2011 or 2012 annual reports identify risks, such as those associated with the European sovereign debt crisis or money market funds, which are ongoing or have previously been identified as potentially emerging. Further, FSOC identifies a large number of threats without explicitly prioritizing them. In contrast, other entities, such as the International Monetary Fund and European Central Bank, issue reports that explicitly prioritize potentially significant threats. Treasury and FSOC officials and staff noted that FSOC's annual reports have a different purpose and implicitly prioritize the threats in the recommendations sections of the reports. As a result of FSOC's limited processes for identifying and prioritizing potential emerging threats to financial stability in its annual reports, policymakers and market participants do not have the information they need to develop effective and timely responses to those threats. We recommended that FSOC develop more systematic approaches for identifying emerging threats to financial stability that are forward-looking and help prioritize such threats in annual reports.

Transparency

Although FSOC and OFR have adopted communication methods to provide information on their activities to the public and Congress, some of their methods could be strengthened. For example, both entities have web pages on Treasury's website. FSOC's web pages include minutes of the council's meetings, annual reports, frequently asked questions, and information on FSOC rulemakings. OFR has also posted key documents on its web pages, including its annual report, strategic framework, and updates on recent developments, such as the status of the legal entity identifier.

However, FSOC does not keep detailed records of deliberations or discussions that take place at the council's meetings or at the committee level. While no specific level of detail is required for FSOC minutes, the limited documentation of their discussions makes it difficult to assess FSOC's performance. For instance, the minutes typically describe agenda items for the meetings and information on the presenters for each agenda item but lack additional detail even when the information being discussed is not likely to be market sensitive or limit the quality of deliberations. As a result, the public receives little information about FSOC's activities and deliberations, limiting its understanding of these activities.

FSOC policy officials recognized the need for transparency but also noted that certain information was protected from disclosure under various statutes and could not be released. FSOC staff also noted the need to balance the desire for transparency with the need to provide an environment that allows for open discussion and deliberation of issues and policy options. However, similar bodies, such as the Federal Open Market Committee, publish minutes that provide greater detail, and the Federal Open Market Committee voluntarily releases transcriptions of its meetings 5 years after a meeting occurs. As we have previously reported, transparency is a key feature of accountability even when there is a need to safeguard certain sensitive information to protect the marketplace. We recommended that FSOC keep detailed records of closed door sessions of key meetings.[16] According to Treasury officials, the Deputies Committee has reviewed FSOC's existing transparency policy in light of this recommendation and may be positioned to make a recommendation to the Council on addressing our recommendation in the coming weeks.

In our September 2012 report, we also recommended that both entities develop a communication strategy to improve communications with the public, which could include more fully developing their websites. According to Treasury and OFR officials, both entities have taken steps to improve their websites. In November 2012, a Treasury official noted that OFR was actively engaged in redesigning its website but had still not posted some information that would show the progress the agency was making in standing up its operations. While the updated website includes a copy of OFR's organizational chart, that chart does not include the names of its top managers or indicate which positions are filled, as we noted in our report. In comparison, the Consumer Finance Protection Bureau, which was also created by the Dodd-Frank Act, has for some time had its own domain name, an easily identifiable website that includes a detailed organizational chart, and online services that provide regular updates to interested parties.

Management Structures and Strategic Planning

FSOC's management structures include a dedicated policy office within Treasury's Office of Domestic Finance and an executive director.[17] FSOC has also implemented bylaws, a transparency policy, and a consultation framework, and members have signed a memorandum of understanding

[16]See, GAO *Troubled Asset Relief Program: Continued Stewardship Needed as Treasury Develops Strategies for Monitoring and Divesting Financial Interests in Chrysler and GM,* GAO-10-151 (Washington, D.C.: Nov. 2, 2009).

[17]FSOC's policy office within Treasury's Office of Domestic Finance has been led by a Deputy Assistant Secretary. More recently, on December 13, 2012, the Council also approved the appointment of an executive director.

(MOU) on sharing confidential information to govern FSOC activities and promote accountability and transparency. OFR has also taken steps to set up needed management structures. It has developed an organizational structure that is built around a Data Center and a Research and Analysis Center—the two programmatic units established by the Dodd-Frank Act.

FSOC is subject to the Government Performance and Results Act of 1993 (GPRA), as amended, which requires agencies to periodically produce strategic plans, annual performance plans, and performance updates. FSOC has begun planning how it can satisfy these requirements but may request an exemption from some. Treasury's strategic plan for fiscal year 2012-2015 does not include information on FSOC's goals or describe how it will measure FSOC's progress in achieving them.

OFR, which is not independently subject to GPRA, received limited discussion in Treasury's 2012-2015 strategic plan and has begun its own strategic planning process. OFR issued a strategic framework in March 2012 to cover fiscal years 2012-2014 that lists five strategic goals, including:

- supporting FSOC through the secure provision of high-quality financial data and conducting the analyses needed to monitor threats to financial stability;
- developing and promoting data-related standards and best practices;
- establishing a center of excellence for research on financial stability and promoting best practices for financial risk management;
- providing the public with key data and analyses while protecting sensitive information; and
- establishing OFR as an efficient organization and world-class workplace.

OFR's framework also highlights a number of objectives under those goals and lays out implementation priorities for fiscal year 2012.[18] However, OFR acknowledges that it has not yet put other key elements of

[18] The framework also notes the importance of transparency and indicates that OFR is subject to oversight from the Treasury Office of the Inspector General (OIG) and GAO, which have both exercised that authority during OFR's first 2 years, and that the Dodd-Frank Act requires that the OFR Director testify before Congress annually on OFR's activities.

performance management in place, including linking programmatic, human resources, and budgetary decision making to its strategic goals and developing a performance measurement system. To support the growth of OFR into a viable and sustainable entity, we recommended that OFR build on its strategic framework by further developing its strategic planning and performance management system so that it linked its activities to its goals and used publicly available performance measures to measure its progress. OFR officials said that they had developed performance measures and planned to describe these in their fiscal year 2014 budget submission.[19]

In the absence of a strategic plan, FSOC's annual reports serve as a key accountability document. FSOC staff noted that its annual reports provided Congress and the public with a description of FSOC's activities, its views on potential emerging threats to U.S. financial stability, and recommendations to enhance the integrity, efficiency, competitiveness, and stability of U.S. financial markets. They added that the chairperson was required to testify annually before Congress on the report, an activity that served as another accountability mechanism.

When discussing accountability, FSOC members have noted the importance of the statement contained in the front of the reports (and signed by each member) that FSOC is taking reasonable steps to ensure financial stability and mitigate systemic risk. FSOC members have also acknowledged the need to follow up on the report's recommendations, and FSOC staff noted that recommendations would be monitored by FSOC as a whole. However, the annual reports do not specify how FSOC will conduct this monitoring. For example, they do not consistently designate an FSOC member or members to monitor or implement the recommendations or establish time frames for certain actions, such as reporting to the council on the status of recommendations. Treasury officials noted that the Dodd-Frank Act did not give the chairperson or council authority to require that independent regulators take action or impose time frames on member agencies. However, they noted that some recommendations in the 2012 Annual Report were made to specific agencies and put greater stress on more immediate action than others. For example, the 2012 report emphasized the importance of a

[19]OFR's budget submission will be included as part of the President's fiscal year 2014 budget submission.

recommendation to the Securities and Exchange Commission (SEC) to take action to address money market fund risks by noting that wholesale short-term funding markets were a critical component of a well-functioning financial system. FSOC continues to be focused on structural vulnerabilities in money market funds that could disrupt these markets and has proposed specific recommendations for addressing these. However, SEC has not taken further action, and FSOC does not have the authority to require that its proposals be implemented.

To improve FSOC's accountability, we recommended in September 2012 that FSOC should make recommendations in the annual report more specific by identifying which FSOC member agency or agencies, as appropriate, were recommended to monitor or implement such actions within specified time frames. In March 2013, Treasury officials told us that FSOC had begun the development process for the 2013 annual report and that our recommendations about the annual reports were provided to the team assigned to pull together this year's annual report for their consideration.

FSOC and OFR Have Taken Steps to Collaborate but Could Enhance Their Efforts

Title I of the Dodd-Frank Act directs FSOC to facilitate information sharing and coordination among its member agencies and other federal and state agencies regarding domestic financial services policy development, rulemaking, examinations, reporting requirements, and enforcement actions.[20] The Dodd-Frank Act encourages collaboration between FSOC and external stakeholders, especially state regulators and international entities. It also specifies a number of duties for OFR that require collaboration with FSOC members and others. In particular, OFR must collect data on behalf of FSOC, provide the data to FSOC and member agencies, and standardize data collection among the agencies.[21] These activities require collaboration not only with FSOC member agencies but also with commercial data providers, publicly available data sources, and the financial industry.

[20] 12 U.S.C. § 5322(a)(2)(E).

[21] The Dodd-Frank Act provides that member agencies, in consultation with OFR, must implement regulations promulgated by OFR to standardize the types and formats of data reported and collected on behalf of FSOC. However, it also explicitly notes that this provision does not supersede or interfere with the independent authority of a member agency under other laws to collect data in the format that the agency requires.

FSOC and OFR have taken steps to enhance collaboration among FSOC members. Members' staffs told us that FSOC's organizational and committee structures helped support collaboration among FSOC members both on a formal and informal basis. In addition, FSOC is working to standardize data reporting systems among FSOC member agencies. OFR officials noted that the agency had begun a three-stage process to assemble an inventory of data collected by FSOC member agencies as a first step toward standardizing data, reducing duplication, and eventually lowering costs for industry and regulators.

FSOC and OFR have taken some actions to collaborate by leveraging the expertise of external stakeholders and coordinating U.S. activities internationally. In particular, FSOC and OFR held joint conferences in December 2011 and 2012 to discuss a range of issues related to risks to financial stability. OFR has also initiated a working paper series in which OFR researchers have collaborated with outside academics to catalog systemic risk monitoring systems and ways to improve risk management at financial institutions. In addition, OFR created the Financial Research Advisory Committee in November 2012 to solicit advice, recommendations, analysis, and information from academics, researchers, industry leaders, government officials, and experts in the fields of data and technology. Moreover, OFR is working with industry, foreign government entities, and international bodies to create a legal entity identifier, which OFR describes as an emerging global standard that will enable regulators and companies around the world to quickly and accurately identify parties to financial transactions.

However, FSOC could do more to promote collaboration and coordination and apply key practices for successful collaboration that we have previously identified, such as leveraging resources, agreeing on roles and responsibilities, and establishing mutually reinforcing or joint strategies. For example, FSOC has not taken advantage of opportunities to leverage resources through its authority to appoint technical and professional advisory committees. Industry representatives have commented on the benefits of having industry input through such committees, but to date FSOC has not established such committees. Moreover, while FSOC members from federal regulatory agencies are able to draw on staff from across their agencies, the independent insurance member and state representatives have limited support structures—a shortcoming that could be remedied by having other state regulators participate through advisory councils.

In addition, FSOC and OFR have not defined their roles and responsibilities for monitoring risks to the financial system. As noted earlier, FSOC is tasked with monitoring the financial services marketplace to identify potential threats to U.S. financial stability, and OFR must develop and maintain metrics and reporting systems for risks to U.S. financial stability as well as monitor, investigate, and report on changes in systemwide risk levels. These responsibilities overlap somewhat, but this overlap is not unexpected given OFR's primary mission of supporting FSOC. The Dodd-Frank Act defines certain responsibilities for FSOC and OFR, but the lack of clear responsibility for implementation can lead to duplication, confusion, and gaps in their efforts. This risk is further compounded by the fact that many FSOC member agencies have risk analysis and data collection functions associated with their supervisory responsibilities. Some of these functions are explicitly focused on risks to financial stability, and some member agencies have created their own programs to examine them. To the extent that these programs provide unique information to FSOC, they will be contributing to the overall effort. However, if not properly coordinated, these separate efforts could be duplicative, resulting in wasted time and resources. We recommended that FSOC and OFR clarify responsibility for implementing requirements to monitor threats to financial stability across FSOC and OFR, including among FSOC members and member agencies.

Further, although FSOC has taken action to better coordinate members' rulemakings, additional action is needed. In October 2010 it issued an integrated implementation road map for the Dodd-Frank Act that included a list of the rules regulators were required to promulgate, provided a time line for those rulemakings, and identified the agencies responsible for each one. FSOC has also developed a consultation framework for the agencies involved in rulemakings. In a November 2011 report, we noted that although FSOC's road map and consultation framework were a positive development in facilitating coordination, they had limited usefulness.[22] For example, the consultation framework does not provide, nor according to FSOC staff is it intended to provide, any specifics about staff responsibilities or processes to facilitate coordination. It also does not describe when interagency coordination is required or what happens when rules conflict with or duplicate each other. We recommended that FSOC work with federal financial regulators to (1) develop formal

[22]GAO-12-151.

coordination policies that would clarify issues such as the timing of coordination, the process for soliciting and addressing comments, and FSOC's role in facilitating coordination and (2) more fully incorporate the key practices for successful collaboration that we have previously identified.

FSOC Has Not Yet Designated Nonbank Financial Companies for Enhanced Supervision

The Dodd-Frank Act gave FSOC the authority to designate financial market utilities (FMUs) as systemically important if FSOC determines that the failure of an FMU or a disruption in its functioning could threaten U.S. financial stability. Similarly, the Dodd-Frank Act provided FSOC with the authority to designate nonbank financial companies for supervision by the Federal Reserve under its enhanced prudential standards.[23] The act stipulates that FSOC may designate these companies if material financial distress at that company, or the nature, scope, size, scale, concentration, interconnectedness, or mix of the activities of the company could pose a threat to U.S. financial stability. While individual designations are not made through rulemakings, in an effort to be more transparent FSOC has issued rulemakings for designating FMUs as systematically important and designating nonbank firms for Federal Reserve supervision. FSOC issued final rules, which explain the processes and criteria FSOC intends to use in making the individual designations, in July 2011 and April 2012, respectively.

Each rule, with any accompanying interpretive guidance, outlines a multistage process that FSOC intends to follow in designating these entities. For example, the interpretive guidance that accompanies the rule for designating nonbank financial companies for Federal Reserve supervision includes a number of thresholds that a firm must meet to move beyond the first stage of the process. Financial companies must meet a size threshold of $50 billion in assets and one of five other thresholds, including measures of leverage and debt. In its 2012 Annual Report, FSOC reported that it had designated eight FMUs as systemically important. However, FSOC is still engaged in its process for designating

[23]The Dodd-Frank Act also subjects large bank holding companies with total consolidated assets of $50 billion or more to enhanced supervision and prudential standards. No FSOC designation is required for these bank holding companies to be subjected to enhanced supervision and standards. In addition, some potential nonbank holding companies that may be designated are already subject to some Federal Reserve oversight because they are thrift holding companies. The Dodd-Frank Act transferred the oversight of these companies from the Office of Thrift Supervision to the Federal Reserve.

nonbank financial companies, and therefore no company has yet been designated.

FSOC is subject to laws and executive orders that require certain regulatory analyses as part of its rulemaking processes, including the Paperwork Reduction Act and the Regulatory Flexibility Act, as well as Executive Orders 12866 and 13563.[24] However, FSOC was required to consider costs and benefits of its FMU and nonbank financial company rules only as they related to the Paperwork Reduction Act. FSOC did not conduct a benefit-cost analysis for the rules designating FMUs or nonbank financial companies because the Office of Management and Budget determined that these rules were not economically significant. Treasury officials noted that the rule did not impose substantive requirements on specific entities but only laid out the process by which they could become subject to other rules and regulations. In addition, FSOC member staff noted that the costs and benefits of the designation were not among the factors that the Dodd-Frank Act directed FSOC to consider when making a designation.

Nonetheless, the designations were intended to address certain risks to financial stability posed by these entities and have the potential to confer other benefits and costs on the wider economy as well as on the individual entities designated. For example, some research has shown that certain large, interconnected financial institutions considered too big to fail may have lower borrowing costs than would otherwise be warranted. But being designated would impose a significant regulatory burden on the designated companies according to some of those who commented on the nonbank financial company rule during the rulemaking process. FSOC has some limited processes in place to review its designations of nonbank financial companies, including an annual review of material changes for a designated company and a review of the stage one thresholds stated in dollar terms at least every 5 years. However, it has not set up processes to conduct a comprehensive assessment of the overall impact of the designations and to determine whether they are achieving the intended result.

[24]A regulatory action is determined to be "economically significant" if the Office of Management and Budget determines that it is likely to have an annual effect on the economy of $100 million or more or to adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local, or tribal governments or communities.

Doing a comprehensive analysis to assess whether designations are having their intended impact of providing greater financial stability and the extent of any other impacts will be challenging, but FSOC is uniquely positioned to address that challenge. Establishing a baseline from which to evaluate the overall impact of various rules will likely be complex because the impact of being designated will depend on the application of a number of rules being written by multiple independent regulatory agencies—Commodity Futures Trading Commission (CFTC), FDIC, the Federal Reserve, and SEC—and issued over a span of time.[25] For example, the Federal Reserve has not issued final rules on the enhanced prudential standards that designated nonbank financial companies will be subject to, but other final rules that will apply to these entities have been issued. These rules include one on resolution plans or "living wills" that was jointly issued by the Federal Reserve and FDIC and that will require designated nonbank financial companies to prepare resolution plans. Treasury has also issued a rule that establishes an assessment schedule for the Financial Research Fund, which finances OFR and FSOC under the Dodd-Frank Act.[26] Moreover, not all of these agencies are required to conduct cost-benefit analyses that might be useful in establishing a baseline. Finally, while some regulatory agencies may conduct periodic retrospective reviews of their rules, these reviews tend to focus only on the rules issued by their agency.

Because FSOC is responsible for designating FMUs and nonbank financial companies and its member agencies are responsible for writing the rules that will impact these designated entities, it has certain advantages in conducting a comprehensive analysis. Moreover, FSOC can rely on OFR for some data collection and analysis. However, FSOC

[25]In GAO-12-151 we note the importance of setting up baselines early to support later retrospective reviews of individual rules. In addition, we reported that in light of its various statutory requirements, FSOC plans to assess the future impact of significant Dodd-Frank rules. Given these plans, we previously recommended that FSOC direct OFR to begin collecting the necessary data to carry out these analyses.

[26]Other Dodd-Frank provisions impose additional requirements on large bank holding companies and nonbank financial companies designated by FSOC. These include a requirement that the Federal Reserve subject designated nonbank financial companies that engage in proprietary trading to additional capital requirements, the authority of CFTC to impose limitations on the ability of those companies to control derivative clearing organizations and exchanges, and the ability of FDIC to impose risk-based assessments on large bank holding companies and designated nonbank financial companies if necessary to repay any obligations issued by FDIC to Treasury under the orderly liquidation authority.

members would need to collaborate on such an assessment, because FSOC policy and OFR staff, who are Treasury employees, may not have access to all of the needed information. In addition, collaboration is needed because, according to Treasury officials, it would be inappropriate for FSOC staff to review rules drafted by independent agencies unless those agencies agreed to participate in the comprehensive assessment. Without such an assessment, decision makers may not have the information they will need to determine whether designating new entities for enhanced supervision and other requirements and restrictions is addressing a perceived gap in the regulatory system and improving the stability of the financial system or whether policy changes should be considered. To strengthen the accountability of FSOC's decisions, FSOC should establish a collaborative and comprehensive framework for assessing the impact of decisions for designating FMUs and nonbank financial companies on those entities and the wider economy.

Concluding Remarks

Over the past 2 ½ years, FSOC and OFR have made progress in establishing their operations and approaches for monitoring threats to financial stability. Both entities have also worked to establish accountability and transparency mechanisms and promote collaboration among FSOC members and with external stakeholders. However, as we reported in September 2012, continued efforts are needed. We made 10 recommendations to FSOC and OFR to strengthen the accountability and transparency of their decisions and activities as well as enhance collaboration among FSOC members and with external stakeholders.

In its November 2012 response to our report and recommendations, Treasury noted that FSOC and OFR had considered the recommendations. In March 2013, Treasury officials described steps that each entity was considering or taking to address some of the recommendations, such as reviewing FSOC's transparency policy and updating the websites. Although fully addressing the recommendations will likely take time, doing so will help FSOC and OFR shed more light on their decision making and activities and allow Congress to hold them accountable for results. Furthermore, addressing our recommendations can help FSOC and OFR enhance collaboration among FSOC's members and with external stakeholders, activities that are critical to their ability to achieve their missions. We will continue to monitor FSOC's and OFR's progress in implementing our recommendations and stand ready to assist Congress as it continues its oversight of these entities.

Chairman McHenry, Ranking Member Green, and Members of the Subcommittee, this completes my prepared statement. I would be pleased to respond to any questions that you may have at this time.

GAO Contact and Staff Acknowledgments

For questions regarding this testimony, please contact A. Nicole Clowers at (202) 512-8678 or clowersa@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Other individuals who made key contributions to this testimony statement include Kay Kuhlman (Assistant Director), Nancy Barry, Emily Chalmers, Christopher Forys, Michael Hoffman, and Rachel Siegel.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (http://www.gao.gov). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to http://www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, http://www.gao.gov/ordering.htm.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on Facebook, Flickr, Twitter, and YouTube. Subscribe to our RSS Feeds or E-mail Updates. Listen to our Podcasts. Visit GAO on the web at www.gao.gov.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Website: http://www.gao.gov/fraudnet/fraudnet.htm
E-mail: fraudnet@gao.gov
Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Katherine Siggerud, Managing Director, siggerudk@gao.gov, (202) 512-4400, U.S. Government Accountability Office, 441 G Street NW, Room 7125, Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Written Testimony of
Amias M. Gerety
Deputy Assistant Secretary for the Financial Stability Oversight Council
United States Department of the Treasury

Before the House Financial Services Subcommittee on Oversight and Investigations
March 14, 2013

Chairman McHenry, Ranking Member Green, and members of the Committee, thank you for the opportunity to appear here today to discuss the Financial Stability Oversight Council's (Council) role in implementing key reforms of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).

This month marks the five-year anniversary of the failure of Bear Stearns and the start of the financial crisis and the biggest recession our country had experienced since the Great Depression. Those events in turn led to the passage of the Dodd-Frank Act that President Obama signed into law in the summer of 2010 – the most comprehensive set of reforms to our financial system in 80 years.

The Dodd-Frank Act was a comprehensive response to a financial regulatory system that was too weak to prevent or effectively monitor risks in the financial system and that lacked the tools to respond effectively to a financial crisis that inflicted devastating damage on the U.S. economy and American families.

One of the key failures that contributed to the financial crisis was a lack of accountability for the overall stability of the financial system. The Dodd-Frank Act addresses this gap in the financial regulatory framework by creating the Financial Stability Oversight Council, which is the first federal entity vested with clear responsibility for comprehensive monitoring of the stability of our nation's financial system. The Council's three statutory missions are to identify risks to the financial stability of the United States, to promote market discipline, and to respond to emerging threats to the stability of the U.S. financial system. To support the activities of the Council and its member agencies, the Dodd-Frank Act also created the Office of Financial Research (OFR), within the Treasury Department, to collect and improve the quality of financial data and develop tools to evaluate risks to the financial system.

These complementary statutory mandates of the Council and the OFR facilitate a comprehensive approach to monitoring and analyzing emerging risks to, and trends in, the U.S. financial system. The two organizations work closely toward their common goals while minimizing duplication of efforts. OFR leadership and Council staff meet on a weekly basis to coordinate their activities and discuss current priorities.

Since the enactment of the Dodd-Frank Act, the Council has moved quickly to achieve its statutory mission while also promoting collaboration and coordination among its members. To that end, one of the Council's first activities was to build an open operational framework that included the creation of standing committees composed of staff of all of the Council members. The participation on these committees draws upon the collective policy and supervisory expertise of the Council members and institutionalizes opportunities for open and frank discussion, collaboration, and coordination. The Council's Deputies Committee, which meets bi-weekly, coordinates the activities of the Council and monitors for overlap and opportunities for collaboration among Council member agencies. Additionally, the Council has developed protocols for statutorily required consultations regarding certain Dodd-Frank Act rulemakings.

The Council is also firmly committed to operating in an open and transparent manner. At its first meeting, the Council adopted a transparency policy which states that Council meetings will be open to the public whenever possible and not less than twice each year. In fact, the Council has held nine open sessions in its first two and a half years. Council member agencies, including Treasury, have also voluntarily disclosed meetings with the public related to Council activities. For example, Treasury has disclosed on its public website hundreds of meetings related to the implementation of the Dodd-Frank Act.

The Council's annual report, which summarizes the Council's activities over the previous year and provides a forward-looking assessment of its future priorities, is a key accountability document that provides transparency to the public and to Congress. Additionally, the Council has demonstrated its commitment to transparency by actively seeking public comment on a number of key issues under the Council's consideration, including the Council's study on effective implementation of the Volcker Rule, its proposed recommendations for money market mutual fund reform, and its rule and interpretive guidance related to the designation of nonbank financial companies. In particular, the Council's rules and guidance on nonbank financial company designations and on the designation of financial market utilities were not statutorily required, but the Council believed it was important to provide the public with insight into how the Council intended to evaluate these firms for potential designation. Finally, Council members have also informed both the Congress and the public of Council activities through a large number of public testimonies, briefings, and speeches.

Although the Council is a relatively young organization, it has quickly assumed a central role in financial regulatory reform and in addressing risks to the financial system. Since its establishment, the Council has convened 28 times, has published two annual reports and six additional studies or reports on matters including concentration limits on financial companies and contingent capital, and has designated eight financial market utilities as systemically important.

In 2012 alone, the Council convened 12 times to conduct its regular business and respond to specific market developments including issues such as the sovereign fiscal developments in Europe and the United States, the trading losses of JPMorgan's Chief Investment Office, and the state of mortgage foreclosures in the United States. When superstorm Sandy ravaged the East Coast, the Council convened twice in two days to monitor market conditions and closures, discuss the effects on financial infrastructure, assess operational challenges facing banks, thrifts, and credit unions, and receive information on preliminary state and federal insurance loss estimates as a result of the storm.

The Council is also in the final stages of evaluating an initial set of nonbank financial companies for potential designation, which will subject them to enhanced prudential standards and supervision by the Federal Reserve, closing an important regulatory gap. Over the last year, Council member staff has participated on interagency teams to review public data, engage with an initial set of companies to gather additional information, and coordinate with the companies' regulators to develop thorough assessments. Moreover, the Council has laid out a process in its final rule and guidance to reevaluate any designated companies each year, consistent with the statutory standards, to determine if the company continues to meet those standards.

During the past two-and-a-half years, the Council staff has also been pleased to work with a number of teams from the Government Accountability Office (GAO) as they have conducted multiple reviews of the Council's activities. In particular, we have worked closely with Nicole Clowers and her staff and appreciate their important suggestions for the continued improvement of the Council's effectiveness.

***

The Committee's letter asked me to address a GAO report issued in September 2012 that examined the progress of the Council and the OFR in achieving each organization's mission. This report reinforced that the work of the Council and the OFR is critical to safeguarding the stability of our financial system and highlighted examples of how both organizations have demonstrated transparency and accountability while carrying out their respective missions. The report also made a number of recommendations to further enhance the progress that each organization has made in these important areas.

Enhanced Transparency

As Treasury emphasized in its comment letter included as an appendix to the GAO's report, the Council is firmly committed to promoting transparency and accountability in connection with its activities. In November 2012, the Council and the OFR jointly provided a response to Congress and the GAO with a description of the actions planned and taken in response to each of the recommendations in the report.

Specifically, the report made a number of constructive recommendations on ways in which the Council could further enhance its transparency, including improving the Council's website. Subsequently, the Council's website was reintroduced, in December 2012, to improve transparency and usability, to improve access to Council documents, and to allow users to receive e-mail updates when new content is added. Continued enhancements to promote further transparency are expected over time. We also expect the Council's Deputies Committee to review whether to recommend any further changes to the Council's transparency policy.

The Council is firmly committed to holding open meetings and closes its meetings only when necessary. However, the Council must continue to find the appropriate balance between its responsibility to be transparent and its central mission to monitor emerging threats to the financial system. Council members frequently discuss supervisory and other market-sensitive data during Council meetings, including information about individual firms, transactions, and markets that require confidentiality. In many instances, regulators or firms themselves provide nonpublic information that is discussed by the Council. Continued protection of this information, even after a period of time, is often necessary to prevent destabilizing market speculation or other adverse consequences that could occur if that information were to be disclosed.

Enhanced Collaboration

The Council and its committees are key forums for coordination among regulators.

The Council has developed protocols for the statutorily required consultations regarding certain Dodd-Frank Act rulemakings. Collaboration and coordination beyond these statutory consultation requirements are inherent in the work of the Council, and occur routinely through the work of the Council members, Council committees, and member agency staff. For example, the Council has engaged in extensive consultation with the Federal Reserve Board on its proposed enhanced prudential standards, and Council members have frequently engaged in discussions on key regulatory issues, such as the international coordination of derivatives rules. Additionally, this collaborative approach is evidenced by the Council's ongoing work related to short-term funding markets, including working with the Federal Reserve Board on reforms to strengthen the tri-party repo markets, as well as the Council's recently proposed recommendations regarding money market mutual funds reforms.

The Council's framework for regulatory coordination has supported a broader and more collaborative approach than existed before the Dodd-Frank Act, and it illustrates that a more rigid approach to interagency coordination could constrain the open and collaborative environment that exists today. Additionally, Congress did not provide the Council or its Chairperson with authority to require the independent member agencies to coordinate in all cases, nor did the Dodd-Frank Act change the statutory independence of the Council's member agencies. Nevertheless, the Council will continue to seek to identify ways to further enhance collaboration through the Council's committees and working groups.

Enhanced Accountability

The Council's annual reports serve as key accountability documents. Two of the GAO's recommendations relate to ways in which the Council can improve the content of these reports. Work on the Council's 2013 annual report is underway, and we will consider the GAO's recommendations as the Council works to refine its approach to communicating key recommendations regarding financial stability in the report.

As with the Council's 2012 annual report, future annual reports will continue to articulate any intent by the Council to indicate when a particular member agency is responsible for addressing an identified risk, such as the Council's 2012 recommendation that the SEC and CFTC consider error control and risk-management standards for exchanges, clearing firms, and other market participants that are relevant for a high-speed trading environment. Appropriate timeframes will also be included, where applicable. At the same time, the Council's annual reports may contain recommendations that are directed to market participants or other entities. The GAO also recommended that the Council adopt a more formal and quantitative approach to identifying risks to financial stability. The Council's Systemic Risk Committee has worked with the OFR to develop a monitor of key financial and economic data and to highlight areas of potential concern. This information is now presented every month by OFR staff to the Council's Systemic Risk Committee and assists the Council and member staff in identifying potential risks.

Enhanced Public Outreach

Since the GAO issued its report in September, the Council and the OFR have leveraged outside expertise in several ways. In December 2012, the OFR and the Council co-hosted a second annual conference on key analytical and data needs regarding financial stability, bringing together industry experts, academics, advocacy groups, Congressional staff, and staff of Council members. In November 2012, Treasury announced the members of a new Financial Research Advisory Committee, which will work with the OFR to recommend ways to develop and employ best practices for data management, data standards, and research methodologies. The Committee is made up of 30 distinguished professionals in economics, finance, financial services, data management, risk management, and information technology. In addition, we continue to actively seek engagement with a wide range of experts outside of government. Further, in November the Council issued proposed recommendations regarding money market mutual fund reform in order to solicit feedback from market participants, academics, and others on this important issue.

The Council members and its committees also continue to help the Council benefit from the expertise of, and facilitate coordination with, outside parties. For example, the Council's state banking, insurance, and securities members were instrumental in coordinating outreach to state authorities during superstorm Sandy and have facilitated valuable information sharing with state regulators.

***

We strongly support GAO's important oversight function, and we appreciate the constructive input and feedback received during our interactions. I also appreciate the Committee inviting me here to provide this update on the Council's responses to the GAO report, and I look forward to working with the GAO in the future.

Thank you.

Denny Heck Question for the Record

March 14, 2013 Oversight and Investigations subcommittee hearing entitled "Who is Too Big to Fail? GAO's Assessment of the Financial Stability Oversight Council and the Office of Financial Research"

> In April 2012, the FSOC stated that it had asked the Office of Financial Research (OFR) to conduct a study of the asset management industry, to determine what risks, if any, the industry poses to the financial system and whether any such risks were best addressed through designation or some other means. Will the results of the analysis be made public and to what extent and in what form? What policies does OFR plan to follow for publishing research going forward?

The OFR is providing the results of the analysis to the Council and the Council will decide if they will move forward with this analysis.

The OFR believes that publishing of fundamental research to encourage public debate is essential. Consistent with Dodd-Frank, the OFR will continue to publish the Annual Report, the Working Paper series and will continue to look for ways to share information with the public and Congress.

Congresswoman Maloney Questions for the Record:

1. Standardizing key reference data like the Legal Entity Identifier is one of the OFRs objectives in supporting data analysis and systemic risk management for FSOC. While OFR does not yet gather data, what is the Office doing to begin to move standardization in the right direction by ensuring all the US regulatory agencies use the agreed International Organization for Standardization (ISO) LEI standard for all entity identification in emerging and existing regulatory reporting? Does the OFR have a timeframe for completion of the LEI system?

   The OFR considers it critical that the LEI emerge as the common standard for entity identification for reporting in the US and abroad. With regard to US reporting requirements, as you may know, the Securities and Exchange Commission has issued rules related to LEI reporting for investment advisors and private funds, and a proposed rule relating to security-based swaps and the Commodity Futures Trading Commission has issued a final rule relating to swaps. In addition, the National Association of Insurance Commissioners is requiring LEI use in reports that it collects. Beyond existing requirements, the OFR is working through the Financial Stability Oversight Council Data Committee and bilaterally with regulators to embed the LEI in reporting requirements across the domestic financial regulatory community.

   The global system will grow over time as new jurisdictions issue requirements to use the LEI and new utilities become available to issue LEIs, but significant operational milestones have already been reached, and others are coming this summer. Earlier this year, the governance of the Global LEI System was established with the formation of the Regulatory Oversight Committee (ROC). Prefixes have been issued to seven different entities so that they may begin operational preparations to issue precursors to the LEI, or pre-LEIs. These pre-LEIs are expected to become LEIs after the Central Operating Unit of the global system becomes operational. In the US, well over 50,000 pre-LEIs have already been issued, and in Europe a new registrar began issuing pre-LEIs in early April. These pre-LEIs comply with the ISO standard, have been issued by pre-Local Operating Units (LOUs) that are sponsored by authorities that have joined ROC, and the pre-LEIs are expected to be honored by swaps regulators in the US and Europe for reporting purposes, regardless of which pre-LOU issued the pre-LEI.

   Given the ultimate goal of complete coverage of all financial market participants anywhere on the globe, the concept of a "completion date" is a difficult one. However, we fully expect to have a pre-LEI mutual acceptance regime in place in the coming months that will allow reliance on pre-LEIs that are compliant with the agreed global standard. Also in the coming months, we expect to have the private-sector central operating unit up and running, and increasingly taking responsibility for operational decisions for the global system.

2. The purpose of the Global LEI initiative – in which the OFR plays an important leadership role – is to ensure that in today's complex global markets, firms can be identified through a unique global identifier, that will facilitate the ability of regulators

and firms to better understand risk in the financial system, thereby enhancing financial stability. Consequently, it is critical for the OFR and the global regulatory community to make sure that LEIs that exist today are used in current and emerging reporting, and not changed or removed from the system. Can you please tell us what steps the OFR is taking to ensure the integrity and value of the LEI system?

The OFR fully agrees that it is critical that the global regulatory community make certain that the pre-LEIs that are being issued today can be used in current and emerging reporting without alteration once the system becomes more fully operational. As Chair of the Regulatory Oversight Committee (ROC) and in its position supporting the Council, the OFR is working vigilantly to make this happen. Those steps include confirming, on a multilateral basis, that due diligence is taken and adequate representations are made regarding pre-LEIs issued abroad so that the CFTC and other domestic regulators will be able to rely on those pre-LEIs issued abroad, and visa-versa. More broadly, the ROC, under the leadership of the Chair, is constructing a path toward global acceptance of pre-LEIs issued by LOUs that are sponsored by ROC members. To that end, the ROC has already issued public guidance identifying six steps that issuers of pre-LEIs must take to ensure compatibility with the global LEI system. And, as noted in that guidance, the ROC is further refining these requirements to gain greater certainty for regulators, LEI issuers, and LEI users that these pre-LEIs will be globally compatible and will seamlessly transition into the global LEI system.

3. What is the OFR doing to ensure the existing CICI (CFTC Interim Compliant Identifiers) codes are integrated into the global LEI system?

   As noted above, the ROC has already issued guidance aimed at assuring that pre-LEIs issued now can be globally compatible, and continues to refine its guidance to create greater certainty for a seamless transition from pre-LEI to LEI without change. Notably, this work involves input from authorities on the ROC, including those with reporting rules pending or passed and those sponsoring utilities that issue pre-LEIs, and input from a Private Sector Preparatory Group composed of experts from these pre-LOUs and other users.

House Financial Services Subcommittee on Oversight and Investigations
Hearing entitled "Who is Too Big to Fail? GAO's Assessment of the Financial Stability Oversight Council and the Office of Financial Research"
Questions for the Record for Amias Gerety, Deputy Assistant Secretary, FSOC
March 14, 2013

REPRESENTATIVE DENNY HECK (D-WA):

Question 1:

March 14, 2013 Oversight and Investigations subcommittee hearing entitled "Who is Too Big to Fail? GAO's Assessment of the Financial Stability Oversight Council and the Office of Financial Research"

In April 2012, the FSOC stated that it had asked the Office of Financial Research (OFR) to conduct a study of the asset management industry, to determine what risks, if any, the industry poses to the financial system and whether any such risks were best addressed through designation or some other means. Will the results of the analysis be made public and to what extent and in what form? What policies does OFR plan to follow for publishing research going forward?

The Council is reviewing generally the activities of asset management companies and their impact on the U.S. financial system. The Council has asked the OFR to supply data and analysis to inform the Council's review. As part of this analysis, Council and OFR staff have met with market participants, including asset managers, to learn more about their activities and business models.

The Council's work is ongoing. Were the Council to determine that it would be appropriate to develop additional metrics that would be used to identify asset management firms for further evaluation for potential designation, I expect that the Council would provide the public with an opportunity to review and comment on those metrics, in accordance with past practice. As demonstrated by the Council's multiple requests for public comment on its rule and interpretive guidance regarding nonbank financial company designations, the Council values the input of all interested parties, stakeholders, and the public.

With regard to the OFR's policies for publishing research, I respectfully refer you to the OFR.

○