OVERSIGHT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL

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OVERSIGHT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL

Tuesday, December 8, 2015

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:04 a.m., in room 2128, Rayburn House Office Building, Hon. Jeb Hensarling [chairman of the committee] presiding.

Members present: Representatives Hensarling, Royce, Lucas, Garrett, Neugebauer, Pearce, Posey, Fitzpatrick, Westmoreland, Luetkemeyer, Huizenga, Duffy, Stivers, Fincher, Stutzman, Mulvaney, Hultgren, Ross, Pittenger, Wagner, Barr, Rothfus, Messer, Schweikert, Guinta, Tipton, Williams, Poliquin, Love, Hill, Emmer; Waters, Maloney, Velazquez, Sherman, Meeks, Hinojosa, Clay, Lynch, Scott, Green, Cleaver, Ellison, Himes, Carney, Foster, Murphy, Sinema, Beatty, Heck, and Vargas.

Chairman HENSARLING. The Committee on Financial Services will come to order. Without objection, the Chair is authorized to declare a recess of the committee at any time.

Today's hearing is entitled, "Oversight of the Financial Stability Oversight Council." Today, we have 8 of its 10 voting members as witnesses. Secretary Lew testified, according to statute, earlier in the year, and Chair Yellen has regrettably declined to give testimony today.

I now recognize myself for 3 minutes to give an opening statement. Financial regulators possessed every regulatory power to prevent the 2008 financial crisis, but failed to do so. Yet, Washington rewarded them with vast new sweeping powers over our lives and our economy. Nowhere is that more evident than in the Dodd-Frank Act's Financial Stability Oversight Council (FSOC), whose members, again, save two, sit before us today.

FSOC is clearly one of the most powerful Federal entities ever to exist. Unfortunately, it is also one of the least transparent and least accountable.

First, the Council's power is concentrated in the hands of one political party, the one that happens to control the White House. All but one of its members is the presidentially-appointed head of an agency, but interestingly the agencies themselves are not members, thus denying bipartisan representation. This structure clearly injects partisan politics into the regulatory process. It erodes agency independence and harms accountability.

Furthermore, FSOC's budget is not subject to congressional approval, removing yet another check and balance to its immense power. FSOC has earned bipartisan condemnation for its lack of transparency. Two-thirds of its proceedings are conducted in private. Minutes of those meetings are devoid of any useful substantive information on what was discussed.

Dennis Kelleher, the CEO of the left-leaning Better Markets, has said, "FSOC's proceedings make the Politburo look open by comparison. At the few open meetings they had, they snap their fingers and it is over. They are all scripted. They treat their information as if it were state secrets."

Of all the Council's activities, none generates more controversy than its designation of non-bank financial institutions as systemically important financial institutions, or SIFIs, by acronym.

Designation anoints institutions as too-big-to-fail, meaning today's SIFI designations are tomorrow's taxpayer-funded bailouts. Designation also ominously grants the Federal Reserve near de facto management authority over such institutions, thus allowing huge swathes of the economy to potentially be controlled by the Federal Government.

Members of the Council can merely raise the prospect of a SIFI designation and thereby eliminate entrepreneurial risk-taking, innovation, and growth from our economy. As a result, Americans may find themselves paying more to insure their homes and families. Investors who relied on mutual funds to save for their children's education or their own retirement will find they have earned less.

In addition to SIFI designations, FSOC is charged with identifying emerging threats to our financial stability, but refuses to look in the mirror. In its latest annual report, it conspicuously omits any references to specific government policies or agencies as helping to cause the systemic risk it identifies: "Greater risk-taking across the financial system is encouraged by an historically low yield environment," the Council reports. Yet, the Council refuses to identify the obvious source of this apparent risk: the Fed's unprecedented loose monetary policy.

The Council warns of reduced liquidity in the capital bond markets, yet never acknowledges that Dodd-Frank's Volcker Rule and other regulations have drastically reduced liquidity. The Council lists risk-taking in large, complex interconnected financial institutions as a threat, yet again, it fails to mention that Dodd-Frank amplifies the threat by empowering the Council to designate certain firms as too-big-to-fail.

FSOC typifies not only the shadow regulatory system, but also the unfair Washington system that Americans have come to fear and loathe: powerful government administrators; secretive government meetings; arbitrary rules; and unchecked power to punish. Thus, oversight and reform is paramount.

I yield back.

The Chair now recognizes the gentleman from New Jersey, the chairman of our Capital Markets Subcommittee, Mr. Garrett, for 1 minute.

Mr. GARRETT. I thank the chairman. And I thank all of our witnesses for being here today.

I guess all of our witnesses have gotten to know each other pretty well, because you meet regularly in closed-door sessions where the public is not allowed, to basically discuss how to fundamentally change the U.S. economy.

So I thought I would just take this minute to introduce ourselves to you. We are the U.S. Congress. We were created by Article I of the U.S. Constitution. We are the ones who are actually elected representatives of the American public. And we are the ones who send you all those pesky letters that you all routinely ignore.

And I know you are probably confused by this setting, that the public is here, that there are TV cameras here, so this is probably unusual for you. But this is what we do. We are open to the American public. We are transparent. And we are before the American public.

So, if there is one thing that you take away today, it should be that in the way you run your hearings, and the way you conduct yourselves, you need to become more like us: more transparent and more open to the American public. You need to adopt these policies so you are no longer working behind closed doors and in secret.

With that, I yield back.

Chairman HENSARLING. The Chair now recognizes the ranking member for 5 minutes.

Ms. WATERS. Thank you, Mr. Chairman. And thank you to the distinguished members of the Council for joining us for this hearing.

We gather today to examine the activities of the Financial Stability Oversight Council, or FSOC, which, since the passage of the Dodd-Frank Act, has fulfilled its mandate to monitor and respond to the types of systemic risks that nearly brought our economy to its knees in 2008.

This important work cuts across every corner of our banking, capital markets, housing, and insurance sectors. Which is why Congress specifically designed the Council to draw on all of the expertise of the witnesses here before us today.

Unfortunately, many of my colleagues on the other side of the aisle seem to have caught a convenient case of amnesia about this important mandate.

Indeed, it was only 7 short years ago that our economy lost nearly $16 trillion in household wealth, $13 trillion in economic growth, and 9 million jobs.

In large part, this was because our regulators were too often caught in silos not communicating with one another and not considering gaps between their agencies or interconnectedness within the financial sector. Even worse, we saw too many cases where regulators were captured by the very entities they were meant to police.

Many of these lessons appear to be forgotten, as we have seen with recent markups, as well as attempts to laden government funding bills with poison pill riders. Some opponents of Dodd-Frank are far too focused on dismantling Wall Street reform by attacking core elements like the FSOC and the Consumer Financial Protection Bureau.

These attempts to roll back Dodd-Frank started the minute this reform was signed into law, and make no mistake, these attempts continue today, even as our economy has experienced a remarkable rebound with 6 to 9 straight months of positive job numbers, GDP growth, and a housing market where sustainable access to credit continues to expand, all of which are signs pointing to the sort of stability and growth that the law was designed to promote.

FSOC has contributed to this growth and stability by convening the 10 component regulatory agencies for periodic information-sharing about emerging risk and reporting on those risks to the public. Further, the Council has now designated four institutions for enhanced supervision by the Federal Reserve. This designation will ensure that companies like AIG never again are able to engage in risky, unregulated activity that could threaten the entire global economy.

And far from the talking points of some members on the opposite side of the aisle, this enhanced oversight is now causing some large non-bank financial companies to consider whether simplifying their structures and breaking themselves up might provide better value to their shareholders.

I am also encouraged that the money market fund industry is now less susceptible to bank lack runs as a result of the pressure the FSOC brought to overcome gridlock at the Securities and Exchange Commission.

Finally, I appreciate that the Council has made an effort to conduct this work in a manner that is responsive to feedback from Congress and outside stakeholders. For example, with this announcement in February, the FSOC took the step of voluntarily agreeing to certain due process and transparency measures that will further serve to improve their operations. This type of dialogue and openness to feedback should be applauded.

As we hear from the voting members of the Council today, I will be interested to learn more about their interagency collaboration and their work to address emerging threats. Again, this work is central to preventing the types of contagion and risk that nearly crashed Main Street just 7 years ago.

Thank you, Mr. Chairman, and I yield back the balance of my time.

Chairman HENSARLING. The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, chairman of our Housing and Insurance Subcommittee, for 1 minute.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. An inefficient secretive regulatory structure that does not reflect the reality of the U.S. financial system can have real economic consequences for businesses and the American people. This is particularly true of the banks that have been deemed to be SIFIs, not based on risk posed to the U.S. financial system, but purely on arbitrary asset size.

On the non-bank side, designations are part of the regulatory system that has become synonymous with the overzealous enforcement climate so prevalent today. In vital power, the FSOC should alarm all Americans, judging by what we know of the staff hours spent on non-bank analysis, which we will get into shortly in the question-and-answer period.

It is clear to me that these designations, and the lack of a clear path for de-designation, is a Federal Reserve-driven effort to expand government's power and influence.

It is time to force more transparency, to require pragmatic regulation, and to curb the growing regulatory scene crippling our institutions and their customers. With that, Mr. Chairman, I yield back.

Chairman HENSARLING. The gentleman yields back.

We will now turn to our panel. Today, we welcome the testimony of the Honorable Mary Jo White, Chair of the Securities and Exchange Commission; the Honorable Timothy Massad, Chairman of the Commodities Futures Trading Commission; the Honorable Roy Woodall, Jr., the FSOC's independent member with insurance experience; the Honorable Debbie Matz, Chairwoman of the National Credit Union Administration; and an especially warm welcome to our former colleague, the Honorable Mel Watt, Director of the Federal Housing Finance Agency; the Honorable Martin Gruenberg, Chairman of the Federal Deposit Insurance Corporation; the Honorable Richard Cordray, Director of the Consumer Financial Protection Bureau; and last but not least, the Honorable Thomas Curry, the Comptroller of the Currency.

Since all of our witnesses have previously testified before Congress, I believe they need no further introduction. Without objection, your written statements will be made a part of the record by agreement with the ranking member. Each of you will be recognized for 3 minutes to give an oral presentation of your testimony.

Chair White, you are now recognized.

STATEMENT OF THE HONORABLE MARY JO WHITE, CHAIR, U.S. SECURITIES AND EXCHANGE COMMISSION

Ms. WHITE. Thank you. Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for inviting me to testify regarding the Financial Stability Oversight Council.

As you know, the Dodd-Frank Act established the Council to provide comprehensive monitoring of the stability of our Nation's financial system. It also provides a formal forum for coordination among the various financial regulators, assisting in bringing about the kind of collaborative sharing of information and concerns that is very important to safeguarding the U.S. financial system.

As one of two capital market regulators on the Council, the perspective that I and the SEC staff bring to the Council is important. In particular, the SEC's historical tripartite mission of protecting investors, maintaining fair, orderly and efficient markets, and facilitating capital formation necessarily gives the SEC unique insight into many areas on which the Council is focused, such as the potential financial stability risks of asset management activities and products, the ongoing changes to market structure, and the role of central counter-parties.

SEC engagement with the Council on these issues helps to ensure that relevant expertise is brought to bear on these important subjects. With respect to designations of any non-bank financial companies as systemically important, it is important to be data-driven and to conduct rigorous analysis throughout the process.

The Council is also focused on enhancing its process and the transparency of its functions, which I consider to be quite important. Toward that end, as the ranking member indicated, in February of this year the Council unanimously adopted changes to the designation process, including increased and earlier engagement with companies under review, increased public transparency concerning the designation factors, and an opportunity for designated firms to meet with Council staff in connection with the annual review of their designations.

I look forward to our continued study of possible further enhancements and agree with the observation that the Council is a relatively new organization and should continuously study ways to optimize its functioning.

Thank you again for the opportunity to testify today. I would be pleased to answer your questions.

[The prepared statement of Chair White can be found on page 125 of the appendix.]

Chairman HENSARLING. Chairman Massad, you are now recognized.

STATEMENT OF THE HONORABLE TIMOTHY G. MASSAD, CHAIRMAN, COMMODITY FUTURES TRADING COMMISSION

Mr. MASSAD. Thank you, Chairman Hensarling, Ranking Member Waters, and members of the committee. I appreciate the invitation to testify today.

The CFTC oversees the U.S. derivatives markets, and although most Americans do not participate in these markets, they are vital to our economy, affecting the prices we all pay for food, energy, and other goods and services. For these markets to work well, sensible regulation is essential. We learned that lesson in 2008 when a lack of oversight led to a buildup of excessive swap risk that contributed to the worst global financial crisis since the Great Depression.

My perspective as a member of the FSOC is shaped by my responsibilities as CFTC Chairman, and today I would like to highlight a few of the CFTC's priorities that are particularly relevant to the FSOC.

First is the implementation of a regulatory framework for over-the-counter swaps where we have made great progress, and a number of financial regulators have responsibilities in this area, and the FSOC provides a useful way to communicate.

The second area is making sure clearinghouses are strong and resilient. While we are the primary supervisor of clearinghouses in the derivatives markets, we work together with the Federal Reserve, the FDIC, and the SEC on these important issues. The CFTC has taken many actions to strengthen clearinghouse resilience, but there is more work to do in this area.

Another priority of the FSOC and the CFTC is strong, resilient markets. Following the volatility in the Treasury market on October 15th of last year, the FSOC served as a forum to share information. Shortly after the events, CFTC staff provided a preliminary analysis of what happened in the futures markets to the Council, and subsequently, we worked with other FSOC members to prepare a detailed report analyzing what happened.

Together, we continue to look at these issues pertaining to the evolution and oversight of these markets.

In addition, cyber-security is one of our agency's top priorities and one of the greatest risks to our financial system today. And here again, the FSOC plays an important role in facilitating co-operation.

Another area of focus for the CFTC that is important to FSOC is the oversight of benchmarks. Integrity is critical and has been a priority in our enforcement efforts.

One of the most valuable functions of the FSOC is simply to bring together the agencies and regulators responsible for oversight of our financial institutions and markets. I believe doing so better positions us to identify and address potential threats to financial stability and better serve the American people.

Thank you, and I look forward to your questions.

[The prepared statement of Chairman Massad can be found on page 109 of the appendix.]

Chairman HENSARLING. Mr. Woodall, you are now recognized.

STATEMENT OF THE HONORABLE S. ROY WOODALL, JR., INDEPENDENT MEMBER WITH INSURANCE EXPERTISE, FINANCIAL STABILITY OVERSIGHT COUNCIL

Mr. WOODALL. Thank you, Mr. Chairman, Ranking Member Waters, and members of the committee for inviting me to appear before you today.

Mr. Chairman, you have asked that we be succinct in our oral testimony this morning. The committee received my written testimony last Friday morning, and in view of your request, I do not feel it is necessary for me to expound on it in detail.

But in short, as the committee examines ways to improve the structure and the operations of the Council, my written testimony discussion falls into three broad categories.

First, the background and legislative history of the independent member position in Dodd-Frank. Second, the lack of explicit statutory duties and authorities pertaining to the position, other than just being a member of the Council and the difficulties that has presented from being only "three lines in the statute." The first line creates the position. The second one sets the 6-year term. And the third one sets salary. That is all that is in Dodd-Frank about my position.

Finally, the third section of my written testimony tries to go into my willingness to work with Congress on how the role and authorities of the position can be clarified to strengthen the independence of the position in order for the holder of this position to be more effective in contributing to the work of the Council.

Thank you. I am happy to answer any questions.

[The prepared statement of Mr. Woodall can be found on page 131 of the appendix.]

Chairman HENSARLING. Chairwoman Matz, you are now recognized for your testimony.

STATEMENT OF THE HONORABLE DEBBIE MATZ, CHAIRWOMAN, NATIONAL CREDIT UNION ADMINISTRATION

Ms. MATZ. Thank you, Chairman Hensarling, Ranking Member Waters, and members of the committee. I appreciate the opportunity to discuss the Financial Stability Oversight Council.

Congress established the Council in response to the 2008–2009 financial crisis. The crisis made clear that financial markets cannot quickly absorb the collapse of very large, interconnected companies.

FSOC's primary goal is to prevent system-wide financial crises. The Council's multi-agency structure also ensures that a diverse array of views on emerging risks in each financial sector is considered when making decisions.

From the beginning, the Council has recognized the importance of transparency and public participation. The Council committed to publicly disseminating timely information about decisions, while balancing the need to protect proprietary information and avoid unduly moving markets. Public feedback has also helped FSOC clarify procedures, enhance analysis, and improve decision-making. As an FSOC principal, I am committed to continuing such improvements.

Each Council member brings to the table a unique perspective informed by our areas of expertise and experiences. As a Federal financial regulator for almost 10 years, I lead an agency that now supervises and insures more than 6,000 institutions with assets exceeding $1.1 trillion.

Financial institutions of every size must carefully manage assets and liabilities. In fact, major elements of FSOC's designation of a systemically important institution include the composition of the balance sheet, off balance sheet exposure, and interconnectedness with the entire financial services sector.

FSOC has moved deliberately in creating its process for identifying non-bank financial companies. In response to public comments and congressional feedback, the Council has also invited company participation earlier in the process.

Another important aspect of FSOC's work is its annual report. The 2015 report called for heightened risk management and supervisory attention in areas such as cybersecurity and reaching for yield.

In conclusion, FSOC has promoted collaboration across financial regulators, established rules and procedures which reflect public input, identified systemically important institutions, and furthered public awareness of threats to our financial system.

Going forward, the Council must continue to evolve, provide transparency, and remain flexible when considering new issues.

I look forward to your questions.

[The prepared statement of Chairwoman Matz can be found on page 113 of the appendix.]

Chairman HENSARLING. Director Watt, you are now recognized for your testimony.

STATEMENT OF THE HONORABLE MELVIN L. WATT, DIRECTOR, FEDERAL HOUSING FINANCE AGENCY

Mr. WATT. Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for the opportunity to testify today about the Financial Stability Oversight Council. And to be back before this committee, on which I served for 21 years.

As an independent regulator, FHFA is responsible for the supervision, regulation, and housing mission oversight of Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System. In addition, since 2008 FHFA has served as conservator of Fannie Mae and Freddie Mac. FHFA's housing market expertise contributes to FSOC's ability to understand and better assess broad systemic risk.

As I recall, ensuring that FHFA contributed this kind of expertise to FSOC was especially important to Congress, both because housing represents a significant part of our economy, and because the most recent severe disruption that our economy experienced resulted from business entities and others making unsafe and unsound housing and housing finance decisions.

Through FHFA's active participation in all FSOC committees, FHFA engages with other FSOC members to share information, evaluate policy matters, and conduct risk assessments of business entities and markets in which they operate. FHFA also participates with other members of FSOC in making assessments of whether to designate non-bank financial companies for supervision by the Federal Reserve.

If so designated, these companies are required to meet enhanced prudential standards. This is a significant and important FSOC function, and it is one that all FSOC members, including myself, take very seriously. These decisions are made only after extensive engagement with the company, a thorough analysis of the facts, and careful deliberations.

Going forward, I look forward to continuing to engage with fellow FSOC members to meet our duties and responsibilities in a manner that fosters transparency, is fair and analytical, and contributes to appropriate risk management and risk reduction.

I will limit my comments to these statements, and I look forward to answering your questions today.

[The prepared statement of Director Watt can be found on page 123 of the appendix.]

Chairman HENSARLING. Chairman Gruenberg, you are now recognized.

STATEMENT OF THE HONORABLE MARTIN J. GRUENBERG, CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. GRUENBERG. Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for the opportunity to testify today on the work of the Financial Stability Oversight Council. The financial crisis that began in 2007 exposed a number of serious vulnerabilities in the U.S. financial system.

While some risks affecting individual products and institutions have been recognized, neither the financial markets nor the regulatory community was able to see the whole picture. The FSOC was established in 2010 by the Dodd-Frank Act to address this gap in the regulatory framework. Its key functions are to facilitate information sharing among its member agencies, to identify and respond to emerging risks to financial stability, and to promote market discipline.

The FSOC is also responsible for designating non-bank systemically important financial institutions for heightened supervision by the Federal Reserve. We now have the benefit of five FSOC annual reports, which together outline the key systemic risks facing the financial system and how they have evolved over time.

The first report, published in 2011, described a still fragile financial system recovering slowly from the deepest financial crisis since the Depression. In contrast, the most recent report describes a more stable but still recovering economy, and broad-based improvement in most financial markets and market participants.

Three areas of risk which the FSOC has been following closely and which are of particular consequence to the FDIC are interest rate risk, credit risk, and cyber-security, which are expanded upon in my written statement.

As previously noted, the Dodd-Frank Act also authorizes the FSOC to designate a non-bank financial company if the FSOC determines that material financial distress at the company or the nature, scope, size, scale, concentration, interconnectednees or mix of activities of the company could pose a threat to the financial stability of the United States.

FSOC policies and procedures were crafted to ensure an exchange of information throughout the designation process. As the process has evolved, opportunities for additional transparency both within the operations and the designation process were identified by the FSOC and in comments by external parties. As a result, the FSOC undertook several initiatives over the past year-and-a-half to improve both transparency and engagement with financial companies. These steps are outlined in my written statement.

Mr. Chairman, that concludes my oral statement, and I will be glad to respond to questions.

[The prepared statement of Chairman Gruenberg can be found on page 94 of the appendix.]

Chairman HENSARLING. Director Cordray, you are now recognized for your testimony.

STATEMENT OF THE HONORABLE RICHARD CORDRAY, DIRECTOR, CONSUMER FINANCIAL PROTECTION BUREAU

Mr. CORDRAY. Thank you, Chairman Hensarling, Ranking Member Waters, and members of the committee for the opportunity to testify today. I am glad to work with you and with my colleagues on the Council to strengthen our financial system.

As we are all aware, just a few years ago disruptions in the housing market preceded a financial crisis that caused significant damage to our people and our economy. The ensuing deep recession caused millions of Americans to lose their jobs, and millions of families to lose their homes, as the ranking member noted. Many saw their retirement savings diminished as Americans lost trillions of dollars in household wealth.

Severe deficiencies in the loans supporting mortgage-backed securities in particular created shocks that upended the financial system.

In the aftermath of the crisis, Congress passed financial reform legislation to address the problems that led to the crisis and help ensure they would not happen again. Among the steps taken were the creation of the Financial Stability Oversight Council and the Consumer Financial Protection Bureau (CFPB).

The creation of the FSOC provides for the first time a means of comprehensively monitoring the stability of our Nation's financial system. Prior to the crisis, the U.S. financial regulatory framework focused more on individual institutions and individual markets in isolation from one another. No one regulatory body was responsible for monitoring and addressing overall risk to financial stability, which too often involved different types of financial firms operating in complex and intertwined ways across multiple markets.

The potential for supervisory and regulatory gaps were viewed as creating blind spots in important parts of the financial system. After the crisis, Congress recognized the need for a mechanism to bring financial regulators together to monitor the financial system, share information and expertise, and coordinate the regulatory efforts to respond effectively to emerging threats to financial stability.

One approach that Congress specified to address these issues was to designate certain financial institutions and financial market utilities as systemically important to the stability of the U.S. financial system for the purpose of applying enhanced prudential standards and supervision.

As you know, the FSOC includes the Consumer Bureau, which is the first Federal agency solely focused on protecting consumers in the financial marketplace. Products such as mortgages and credit cards are involved in some of the most important financial transactions in people's lives. These products are often funded through complex financial markets and they may constitute the underlying assets for more complex and highly levered securities.

As the crisis made clear, financial stability, market discipline, and consumer protections are closely interrelated. Part of the mission of the Consumer Bureau, therefore, is to help ensure that the recent economic meltdown is not repeated. The practices that led to the financial crisis are inconsistent with principles of fairness, transparency, and competitiveness in markets.

We are exercising the authority Congress gave us to ensure balanced oversight and prevent harmful practices in consumer financial markets. When honest and innovative businesses can succeed on the merits, fair competition drives growth and progress and the entire financial system rests on stronger and sturdier foundations.

As the Director of the Consumer Bureau, I look forward to continuing to fulfill Congress' vision for our agency in my role in the FSOC. That is what we are here today working together to do. Thank you again for the opportunity to testify, and I look forward to your questions.

[The prepared statement of Director Cordray can be found on page 84 of the appendix.]

Chairman HENSARLING. And Comptroller Curry, you are now recognized for your testimony.

STATEMENT OF THE HONORABLE THOMAS J. CURRY, COMPTROLLER OF THE CURRENCY, OFFICE OF THE COMPTROLLER OF THE CURRENCY

Mr. CURRY. Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for this opportunity to provide the views of the OCC on the functions and operations of the FSOC.

The OCC charters, regulates, and supervises national banks and Federal savings associations. These banks range from small community banks to multitrillion dollar institutions that are among the world's largest financial companies. Together, they hold nearly $11 trillion in assets, or just over two-thirds of the industry's total.

The OCC's mission is to ensure that these banks operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations. As the only Federal financial regulator with prudential regulation as its primary focus, the OCC has specialized knowledge about the safe and sound operations of banks.

In 2010, as part of the Dodd-Frank Act, Congress established the FSOC to identify, monitor, and respond to systemic risk. The Council brings together its member agencies to fulfill this critical mission. Through its committees and staff, the FSOC provides a formal, structured process for communicating, coordinating and responding to emerging market, industry, and regulatory developments as well as to unforeseen events.

As one of the FSOC's 10 voting members, the OCC brings considerable expertise to the Council. Our examiners monitor several areas of financial risk in the banking sector every day, including credit, liquidity, interest rate, and operational risk. These are among the risks that the FSOC reviews in its evaluation of systemic risks with respect to non-bank financial companies and financial market utilities.

Similarly, as many of the institutions we supervise are engaged in asset management activities, the OCC's expertise in this area is also quite robust. Since its establishment, the Council has demonstrated a sustained commitment to working collaboratively to fulfill its statutory mission.

Council members and their staffs have developed strong working relationships and the Council provides a constructive forum to hold candid conversations, share confidential market sensitive information, and ask the tough questions that help make the U.S. financial system safer.

The Council has also made positive strides in enhancing its transparency both to the general public and to the companies under consideration for designation. Dodd-Frank provides the FSOC with important duties and responsibilities to promote the stability of the U.S. financial system. The issues that the Council confronts in carrying out these duties are by their nature complex and far-reaching.

My written testimony includes additional information about the specific mandates Congress has given the FSOC and a discussion of some of the important actions the Council has undertaken recently. For our part, the OCC is strongly committed to helping the Council achieve its mission.

Again, thank you for the opportunity to appear today, and I would be happy to answer any questions.

[The prepared statement of Comptroller Curry can be found on page 86 of the appendix.]

Chairman HENSARLING. The Chair now recognizes himself for 5 minutes for questions.

By a show of hands, how many of you have any professional experience in the private insurance industry? Please raise your hand. I see two, Mr. Woodall and Ms. White. Let the record reflect that.

How many of you have had experience in regulating insurance companies? By a show of hands, please raise your hand. Let the record reflect that only Mr. Woodall raised his hand.

Mr. Woodall, as FSOC's independent member having insurance experience, you dissented in both the MetLife and Prudential SIFI designation. In your dissent to the designation of MetLife, you wrote, "It confounds me that much of the Council and staff continue to misunderstand and mischaracterize the insurance regulatory framework." You went on to say that FSOC's analysis "relies on implausible, contrived scenarios as well as failures to appreciate fundamental aspects of insurance and annuity products and, importantly, State insurance regulation and the framework of the McCarran-Ferguson Act." Do you still stand by those comments?

Mr. WOODALL. Yes, I do, Mr. Chairman. And if I could expound just a little bit, the basis of all of that, to put it in perspective, is that I was pointing out that under the statute, there are two determination standards under which the Council comes up with its idea that a company is a SIFI, and the first one is the only one that has been used so far, which is if there is material financial distress at that individual company which could be a threat to the entire U.S. financial system.

The other is activities, are there activities that could be a threat? My push has been to get the second standard of activities to be used across sectors so we can get at the very things that are causing this systemic risk. If we have a situation where if we have a company that is a SIFI, and it knows that it is doing an activity that is systemically risky, it can sell that activity to somebody that is not a SIFI and then, essentially, we have lost them. They are there, but the systemic risk could still be in the system.

Chairman HENSARLING. Mr. Woodall, what are the implications of designating a traditional insurance company as a SIFI, since they are under State-based regulations? Will we have a duplicate regulatory system? Do you believe those costs could be imposed upon policyholders and insurance company investors?

In other words, what is the harm in designating a traditional insurance company as a SIFI?

Mr. WOODALL. I think there is a harm that it could come to higher prices because they have higher regulatory costs. Also, with a higher regulatory cost, their products have to be priced higher, as I said, and that costs more.

It puts them in an unlevel playing field with the people and the companies that are not designated SIFIs.

Chairman HENSARLING. Chairwoman Matz, prior to voting to designate Prudential as a SIFI, did you make inquiries, or request any type of economic analysis on what this designation could mean to insurance policyholders? Was that part of your decision-making process?

Ms. MATZ. No, it was not.

Chairman HENSARLING. It was not. Do you believe it should have been?

Ms. MATZ. That was not the mandate that we had. The mandate is to determine if material distress at a non-financial institution could pose a threat to the stability of the United States.

Chairman HENSARLING. Under Section 113(a)(2) of Dodd-Frank, there are 11 different factors you are to consider in making your designation. With respect to the Prudential decision, to what extent did the leverage of the company play a role in your decision to designate it a SIFI?

Ms. MATZ. It was the combination. We were briefed extensively on the financial—

Chairman HENSARLING. I'm sorry. Briefed by whom?

Ms. MATZ. Briefed by the FSOC staff and the NCUA staff that works with them, that participates with them—

Chairman HENSARLING. So does the NCUA staff have expertise in insurance company leverage? What was the specific leverage of Prudential that caused you concern?

Ms. MATZ. No. The determination wasn't based on the insurance activities. It was based on the financial activities of the company and how they are interwoven with other—

Chairman HENSARLING. And specifically, which activities were interwoven that concerned you?

Ms. MATZ. It was their derivatives position, the extent of their leverage. Their—

Chairman HENSARLING. But I asked you about the leverage.

Ms. MATZ. The securities lending. Their debt position. The extent of the difficulty to resolve them if there was financial distress. So, it was not one factor.

Chairman HENSARLING. The Chair's time has expired. The Chair recognizes the ranking member for 5 minutes.

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

Let me first go to Mr. Woodall. Is AIG designated as a SIFI, Mr. Woodall?

Mr. WOODALL. Yes.

Ms. WATERS. Should it be?

Mr. WOODALL. At the time when they were designated, we were coming right out of the financial crisis. The first two designations were AIG and JECC, companies which had had some problems during the crisis.

Ms. WATERS. Some problems? Big problems.

Mr. WOODALL. Big problems.

Ms. WATERS. Okay. So, it should be designated a SIFI?

Mr. WOODALL. At that time.

Ms. WATERS. At this time?

Mr. WOODALL. It is not half the company now that it was then.

Ms. WATERS. At this time? At this time, should it be a SIFI?

Mr. WOODALL. Right.

Ms. WATERS. Let me just go on to Mr. Gruenberg on another matter. In the Dodd-Frank Act, Congress recognized that our banking regulators failed to engage in regulatory oversight of large banks leading up to the crisis.

As such, we put in place enhanced prudential standards that set forth the basic requirements for a bank to be well-run—capital resolution; risk management; and liquidity, among other factors—at the same time the deliberative process in Congress led to an exemption from these requirements for banks below $50 billion in assets.

Congress also directed the Fed to tailor certain regulations for large regional banks based on size, as well as provided the Fed with the option to exempt certain banks above $50 billion from certain requirements. Both in committee and through potential riders to funding bills, Congress is now contemplating legislative proposals that would undo this important work.

These proposals would, instead, rely on the Financial Stability Oversight Council to affirmatively designate banks for enhanced prudential standards for all but the very largest global megabanks.

Chairman Gruenberg, do you think that such proposals would be ill-advised? What did the 2008 financial crisis teach us about how the failure of one or more large regional banks could harm our financial system? And in terms of bank resolution, which failure during crisis era was the most costly for the FDIC's deposit insurance fund?

Mr. GRUENBERG. To answer the question you raised at the end, the most costly failure to the FDIC during the crisis was the failure of IndyMac, which was a thrift institution with assets of about $30 billion that ultimately cost the deposit insurance fund over $12 billion, which is the most significant loss during this crisis, and I believe in the history of the FDIC.

And it does show the importance of having a prudential framework for larger institutions relating to capital and liquidity and other standards, and to respond to the first part of your question, as a general matter, I think the framework in place is a reasonable one. It generally gives discretion to the agencies to tailor the prudential standards to the size and complexity of the institution. And I generally think that is an appropriate approach.

Ms. WATERS. Let me just ask you this, so it can be reiterated. Has the Federal Reserve begun tailoring enhanced prudential standards for banks above $50 billion with increased stringency based on bank size? Would you just kind of continue on that?

Mr. GRUENBERG. Yes, Congresswoman. I believe—I wouldn't want to speak for the Fed. But just as an observer, I believe the Fed has done that, generally focused the enhanced prudential standards on the larger institutions above $250 billion, and has tailored standards for those below.

Ms. WATERS. All right. Can more be done in this regard without reopening Dodd-Frank to potentially negative consequences?

Mr. GRUENBERG. Yes. I do think that as we progress in this process, this is a focus for all of the agencies to ensure our regulations are appropriate to the size and complexity of the institutions.

Ms. WATERS. So, basically what you are telling us is there has been no resistance to FSOC taking a close look at what can be done and using its discretion to make sure that they not only honor Dodd-Frank but they have the flexibility to make modifications where necessary?

Mr. GRUENBERG. I agree with that, Congresswoman.

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

Chairman HENSARLING. The gentlelady yields back. The Chair now recognizes the gentleman from New Jersey, Mr. Garrett, chairman of our Capital Markets Subcommittee.

Mr. GARRETT. Thanks, Mr. Chairman. I have been looking through the minutes, Mr. Chairman—if you can call them that—that FSOC published. And one of the things I notice is who actually shows up, and who can attend FSOC meetings. It seems that certain people, like that Governor, who is not a member of FSOC, is able to attend, and attends various meetings of FSOC, while Commissioners of the various boards and Commissions do not attend.

It seems that there is a—well, not a very clear criteria as to who can and cannot attend. In September, according to minutes, the FSOC held with about 20 or so invited guests from various agencies. And again, yes—yet again, the Commissioners of various agencies are not on those lists.

So, I am going to take a page out of Al Green's methodology here and ask for a show of hands. All of you who are on the panel today, who are part of an organization that has either a commission or a board, can you raise your hand, so we know what we are talking—because not everybody up there has a commission or a board, right?

Okay, so, for those who raised your hand, do you trust your Commissioners or your board members as their ability to keep things confidential? So, I would say, do the members who just raised their hand trust their board members?

Maybe I should flip it the other way. Is there any member here who does not trust their board members or their Commissioners? They can't keep things secret?

Okay. So, if that is the case, let me run—Chairman Massad, if any of the members of your Commission wanted to come to you and ask to attend an FSOC meeting, and you trust them, can they come to an FSOC meeting?

Mr. MASSAD. Thank you, Congressman, for the question.

I don't think that is the structure provided for in the law.

Mr. GARRETT. Would you personally object to them being there?

Mr. MASSAD. I think it is important for the FSOC to follow the—

Mr. GARRETT. I don't know that there is anything in the FSOC rules that—is there anything specifically in the requirements that says they cannot attend but other guests can attend?

Mr. MASSAD. I would have to get back to you on that, Congressman.

Mr. GARRETT. You allowed 20 other guests to be there in September, and I guess that was okay. Did you know at that time whether or not they were allowed to be there?

Let me go to Chair White, since he doesn't know. Would you object if one of your Commissioners wanted to attend an FSOC meeting personally? Would you have a problem with that?

Ms. WHITE. The protocol is for the Chairman to pick one person, typically a staff person, to accompany them. That is the structure of FSOC.

Mr. GARRETT. Right. I understand what the structure is. I understand that you have been—the whole entire board has been precluding openness and transparency. What I am trying to find out is for all of you who have just raised your hand, who said you trust your board or commission with secrecy, is there anyone who would say that they cannot attend? Well, good.

Can I have a commitment, then, from all of those people who just said they would not object, that you will work to, for the next meeting, allow your board and Commissioners? Anyone here—please raise your hand if you will not encourage your chairman to allow them to attend the next board meeting.

So, let the record reflect two people. Mr. Gruenberg, you will not—

Ms. WHITE. Can you repeat that?

Mr. GARRETT. —recommend to the chairman that your Commissioners be able to attend?

Ms. WHITE. I would follow—

Mr. GARRETT. No, let me just go there. You didn't raise your hand. Do you not trust your members? Are they not able to keep things secret? I just want to be clear on that.

Mr. GRUENBERG. I certainly do, Congressman. Just a couple of points, if I may.

Mr. GARRETT. Sure.

Mr. GRUENBERG. From the FDIC, as it happens as a matter of statue, three of the members of our board are statutory members of the FSOC. So a majority of our board are represented. And I certainly have the greatest trust in our other Directors. I would note that I share with our other Directors all of the information available to the FSOC.

Mr. GARRETT. But you have no problem with Dan Tarullo's attending quite frequently. So it is something about your board that you don't trust them is what I am taking from this.

Mr. GRUENBERG. No, sir.

Mr. GARRETT. So why do you object to them being there?

Mr. GRUENBERG. I think it is a matter of the—it is a matter for the entire FSOC, it is a matter of functionality in terms of the number of—

Mr. GARRETT. So in September, there were 20-some. That was not an issue of functionality, but for your own board members—I am taking the perception here that either you don't trust your people or that you are doing something in secret. So which one is that, Mr. Gruenberg? Do you not trust your people or you are trying to do something in secret?

Mr. GRUENBERG. Neither, Congressman. For what it is worth—

Mr. GARRETT. Then, you haven't given us an answer.

Chair White, will you recommend to the Chair, will the rest of you now—the rest of the panel who raised their hand, will you recommend to the chairman that these people—that meetings be open to the rest of the Commission?

Ms. WHITE. I will follow the congressional structure. I think that is something—

Mr. GARRETT. There is nothing in the congressional structure. That has already been pointed out, so will you make that recommendation?

Ms. WHITE. I would discuss it with my fellow members of FSOC and the Chairman. Discuss it with them, as I have done before.

Mr. GARRETT. Will anyone here make that recommendation, positive recommendation? So, let the record reflect that no one who has come before us today will make a recommendation; they want to continue to keep their meetings secret.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from New York, Ms. Velazquez.

Ms. VELAZQUEZ. Thank you, Mr. Chairman. Mr. Cordray, the CFPB's core mission is consumer protection, which may not seem linked to systemic risk. However, I don't think that is the case.

Can you elaborate on what role consumer financial protection plays in the stability of our economy and how your agencies work and help inform FSOC?

Mr. CORDRAY. Thank you, Congresswoman. First of all, Congress set the structure of the Council and determined which agencies should be represented there. And it is a broad cross-section of the Federal financial regulators.

In the case of the Consumer Bureau in particular, it is worth noting that the financial crisis that gave rise to the Council was caused, everybody agrees, by irregularities in the mortgage and housing markets.

People disagree somewhat as to the chain of events that led to this, but a meltdown in the housing and mortgage markets was transmitted by various channels throughout the economy and threatened the stability of the financial system.

The very first issue that was raised at the first meeting, which is before I joined the FSOC—I was not yet the Director of the Consumer Bureau—was mortgage servicing and foreclosures. There were briefings on those at the first several meetings. Those are issues that are very central to the work that has been done in the early years by the Consumer Financial Protection Bureau.

All of us on the Council are charged by law with examining the economic system for emerging threats to financial stability, which we do. The annual report has been a very good and transparent and thorough account of the Council's thinking about both present and emerging threats and is our best attempt to monitor and report on what we see in the financial system at that time.

There were various issues that each member of the Council and each entity that they represent is more or less expert in. And we share that expertise with one another to try to arrive at a broader, more comprehensive view of the financial system than each of us could do alone.

Ms. VELAZQUEZ. Thank you.

Mr. Gruenberg, we have heard from opponents of the SIFI process that there is insufficient opportunity to engage with the Council after designation. Do SIFI-designated firms have opportunities to meet with FSOC staff to review their status?

Mr. GRUENBERG. Yes, Congresswoman. As you know, as a statutory matter, the Council is required to re-evaluate a designation annually.

Ms. VELAZQUEZ. Thank you. I yield back.

Chairman HENSARLING. The gentlelady yields back. The Chair now recognizes the gentleman from Texas, Mr. Neugebauer, chairman of our Financial Institutions Subcommittee.

Mr. NEUGEBAUER. Thank you, Mr. Chairman.

Chairwoman Matz, there has been a lot of discussion about what it means for a bank to be systemically important. And as you know, in February the Office of Financial Research (OFR) released a report where they examined the systemic risk indicators. They used the indicators that had been developed by the Basel Committee and they applied those to some of the largest banks and holding companies.

And what was kind of an interesting finding is that the report concluded that the least systemic US GSIB was several times more systemically—more systemic than the other major U.S. banks, the regional banks. Yet, all of those institutions fall under the requirement for enhanced prudential standards based on their asset size. And so are you familiar with that report?

Ms. MATZ. I'm sorry. I have not seen that report.

Mr. NEUGEBAUER. You have not seen that report?

Ms. MATZ. No.

Mr. NEUGEBAUER. One of the requirements is—or, I guess, main functions of the OFR is to furnish the committee with the information to hopefully help them make better determinations. And so I would hope that you would avail yourself of that report.

But would you agree that setting up certain standards to measure companies is appropriate? If you haven't seen the report, basically they took the Basel standards and they took five of them and applied them to those companies. Do you think that is a good way to approach that?

Ms. MATZ. We have stayed away from creating bright lines and instead look at whether material distress at a company could pose a threat to the financial stability of the United States. And since each company has different business plans, different business models, we have not drawn a bright line or been very rigid about what the standard is. It is looking at the entire company and then making a determination after very deliberate consideration.

Mr. NEUGEBAUER. Director Watt, have you seen the OFR report?

Mr. WATT. I have not seen the report that you are referring to.

Mr. NEUGEBAUER. Well, let me—since you haven't read the report, I guess I will go to another line of questions. Section 113 of Dodd-Frank requires FSOC voting members to consider at least 11 factors before designating a non-bank financial company for heightened Federal supervision including leverage, off-balance sheet exposures, scope, size, and scale.

I will start with you, Chairwoman Matz. Do you think it is appropriate to use 11 different factors in the determination of whether a non-bank company is systemically important?

Ms. MATZ. Yes.

Mr. NEUGEBAUER. Director Watt, would you agree with that?

Mr. WATT. Yes. We are not second-guessing the statute. We didn't write the statute, but I think all of them are—well, actually, I was involved in writing the statute.

[laughter]

But I am not in a position to second-guess it now. I voted for it. Right.

Mr. NEUGEBAUER. I think the point I am trying to make here is that it is a little puzzling to me that it is appropriate for non-bank entities to be subject to standards. And I think, in fact, Director Watt, you said you are committed to an analytical process.

And so, I think the interesting thing is, is we subject these non-bank SIFIs to 11 different factors. Yet, we only subject banks to one factor, and that is size. If this is going to be an analytical process, shouldn't we establish factors for analyzing banks in a way of analyzing whether or not they are systemically risky?

Mr. WATT. I think these are really the same factors that any of us would take into account. It may not be specified in a statute for individual banks. But one of the primary problems during the meltdown was there was no supervision, and no method to get at non-bank entities, because they didn't have—they weren't answering to anybody.

Mr. NEUGEBAUER. Yes. I am not talking about non-banks. We have talked about what—

Mr. WATT. I thought that is what this was designed—specifically what this talks about.

Mr. NEUGEBAUER. I guess the question is, we are subjecting banks, based on their size; we don't even consider the other factors. So, shouldn't we be considering a litany of factors to determine whether these banks should be subject to enhanced prudential standards?

Mr. WATT. I think it would probably be more appropriate for Mr. Curry and Mr. Gruenberg to answer that. I don't regulate banks. But I would think that they take into account all of these considerations.

Mr. NEUGEBAUER. But you do sit on FSOC, isn't that correct?

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Texas, Mr. Hinojosa.

Mr. HINOJOSA. Thank you, Chairman Hensarling and Ranking Member Waters, for holding this important hearing. I also wish to thank our distinguished panelists for testifying today, and for the dedication to ensuring the safety and soundness of our financial system through their participation on the Financial Stability Oversight Council.

As a senior member of this committee, I applaud the Council's progress to date, and I look forward to hearing from our panelists on the Council's priorities moving forward.

Two particular lessons learned from the crisis come to mind today. First, it is absolutely essential to have a bird's-eye view of our financial system, in order to identify and prevent systemic risks from destabilizing our entire economy. In crafting the Dodd-Frank Act, we in Congress recognized this fact and created the Financial Oversight Stability Council, an entity comprised of our banking, insurance market, and housing regulators who are tasked with ensuring the financial stability of the system as a whole.

Secondly, we should not just assume that the markets will take care of themselves. Instead, we must support and empower our regulators to be able to act when needed. We should be looking to strengthen our financial system and the safeguards we incorporated after lessons learned from the last crisis, rather than berating our regulators and attempting to restrict their ability to act by tying them up in bureaucratic knots.

My first question is for Mary Jo White. A much criticized report from the Office of Financial Research (OFR) discussed the risk that the asset management industry posed to the United States financial system. The critics argued that the asset management industry poses absolutely no risk to our financial system.

However, haven't the Council's actions, including the publication of the report by the OFR, spurred the SEC to take action with respect to money market funds?

Ms. WHITE. The answer is that the SEC independently proceeded. I am aware, obviously, of the preliminary recommendation of the FSOC. But the SEC proceeded independently to reform the structure, in some ways, of money market funds.

Mr. HINOJOSA. Can you elaborate on how the SEC was spurred by the FSOC and how these actions were making our markets and investors safer?

Ms. WHITE. The SEC proceeded independently of the FSOC recommendation.

The SEC has been studying it for some time, certainly since I have been there as Chair, and proceeded totally independently. It was an important thing to do. To allude back to your first comment, though, I think it is very important from a bird's-eye view, that big picture view be provided by all the financial regulators who sit on FSOC.

Mr. HINOJOSA. Thank you. Next question, to the Comptroller of the Currency, Mr. Thomas Curry. Some critics have criticized Dodd-Frank's FSOC structure for allowing some of your agencies to have voting rights non-bank systemically important financial institution designations made by the FSOC.

Are you comfortable with the deliberative materials received from the Council staff? And do these materials adequately prepare you to make informed decisions?

Mr. CURRY. Thank you, Congressman. There is an extensive amount of material presented to me as a member of the FSOC in connection with any designation. And there is actually a fairly elaborate process of three stages by which that information is developed.

Stage one is from publicly available information or from contacts with supervisors. Stage two, which gives notice to and engages an institution under consideration the opportunity to engage with the Council staff and our designation committee.

And then finally, stage three, where there is extensive communication and development of analysis and records for the Council's consideration.

Mr. HINOJOSA. Thank you. Mr. Cordray, when assessing systemic risk for our financial system, has the FSOC taken a look at aggregate depth levels from various areas of the economy?

Mr. CORDRAY. We have. And I believe we should.

Mr. HINOJOSA. Do you think the current amount of debt in the aggregate poses a risk to our economy? And why or why not?

Mr. CORDRAY. I think everybody could have their own personal point of view on that. I think one of the factors that the FSOC has looked at, in terms of thinking about systemic risk, is both debt and leveraging of levels of investment.

And therefore how much risk could be transmitted through the system, if there were adverse developments to the extent to which capital is deployed. And so, I do think that is an appropriate factor in looking at the kind of issues raised before the Council.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Missouri, Mr.

Luetkemeyer, chairman of our Housing and Insurance Subcommittee.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. We have put up a chart, I don't know if everyone can see it or not; I know we can see it pretty well on the back. And it is on the side, I am not sure we can get there.

But I would like to follow up on the chairman's comments and questions while we go, with regards to non-bank designations. And what I am concerned about is perhaps Fed-driven decisions on some of these designations. And if you look at the bottom part of the chart there, you can see that the National Credit Union Administration in 2012 and 2013 had two members that they dedicated to or who had done some analysis with regard to non-bank designations.

And in 2014, we have none. Ms. Matz, are you an expert on insurance analysis? Okay, so we have—

Ms. MATZ. No.

Mr. LUETKEMEYER. You are not an expert. And we have no one at your agency who is designated to do analysis. And this information—you can't read the fine print there, you can in the back of the room. This analysis, by the way, comes from data given by your agency to the GAO, if I am not mistaken, which is in this report right here.

Ms. MATZ. I don't think that is correct, though.

Mr. LUETKEMEYER. Sorry, Ms. Matz. That is information you gave to the GAO when requested. And so, my concern is the Federal Reserve has 25 people designated to make this analysis. You have zero.

Ms. MATZ. That is not correct.

Mr. LUETKEMEYER. That is not correct?

Ms. MATZ. It has been stated. I don't know where they got that information from, but it—

Mr. LUETKEMEYER. They got it from you.

Ms. MATZ. It is not from me personally. It is not—

Mr. LUETKEMEYER. It is written on the bottom of the sheet. It says that the information came from each member agency and represents individuals involved in the analytical work. So—

Ms. MATZ. It is not correct. We still have—

Mr. LUETKEMEYER. How many do you have, then?

Ms. MATZ. We have two people.

Mr. LUETKEMEYER. Two people. Okay. Are they experts in insurance?

Ms. MATZ. They are not experts in insurance.

Mr. LUETKEMEYER. They are not experts in insurance. So, how can we make an educated analysis whenever you are making designations with regards to non-bank designations, which involve insurance companies? How do you make that determination, then?

Ms. MATZ. It is not the insurance part of the business that results in a designation. It is in the financial services part of the business, and how intertwined it is.

Mr. LUETKEMEYER. So, the insurance part of the business is not important with regards to the designation of a SIFI?

Ms. MATZ. No. It is not. It is the financial services part of the business—

Mr. LUETKEMEYER. The financial services part of the business is the only part that you look at?

Ms. MATZ. Yes.

Mr. LUETKEMEYER. Wow. Okay.

Mr. Cordray, you sort of struck out all across-the-board there as well. Are you an insurance expert, sir?

Mr. CORDRAY. I am not an insurance expert.

Mr. LUETKEMEYER. Is this number incorrect, as Ms. Matz indicated hers was?

Mr. CORDRAY. I am not exactly sure what analysis was used to get to that number. But the reality is that each of us has deputies who work together on the FSOC on the analysis. Then, I am briefed on the analysis and have a chance to review the materials—

Mr. LUETKEMEYER. Well—

Mr. CORDRAY. —extensive materials—

Mr. LUETKEMEYER. —you are saying—

Mr. CORDRAY. —submitted by Congress—

Mr. LUETKEMEYER. —this number is incorrect as well, even though this is information your agency gave to the GAO?

Mr. CORDRAY. I am saying that the slice on it here I think is not reflective of the full work done at the FSOC.

Nonetheless, I am not an insurance expert. But other members of the Council are not banking experts. Certain members of the Council are not investment experts. It is all of us together—

Mr. LUETKEMEYER. Mr. Cordray—

Mr. CORDRAY. —who work together.

Mr. LUETKEMEYER. This goes to the heart of the matter here. You are sitting on a board that makes a decision on the designation of whether something is systemically important or not. And if you don't have the personal expertise, you need to have somebody on your staff, because otherwise it is not an independent vote that you are casting.

It is a vote based on how the Federal Reserve or some other member of this board is telling you it should be done. And that is not the way the system should work.

Mr. CORDRAY. I don't think that is correct. First, there is FSOC staff. There is staff of the member agencies contributed who work together. And then there is our own analysis.

But again, to focus only on the insurance company potential designations is only a partial picture. There are bank designations. There are other financial company designations. There are investor area designations. Everybody has relative expertise in some areas—

Mr. LUETKEMEYER. Okay—

Mr. CORDRAY. —and less in others.

Mr. LUETKEMEYER. I am running out of time here.

Mr. Massad, you have zero people all the way across-the-board. Is that incorrect as well?

Mr. MASSAD. I think your chart runs through July of 2014.

Mr. LUETKEMEYER. Right.

Mr. MASSAD. I took office in June.

Mr. LUETKEMEYER. Okay.

Mr. MASSAD. Shortly after that—

Mr. LUETKEMEYER. Okay.

Mr. MASSAD. —I had my staff involved in the designation that was—

Mr. LUETKEMEYER. So now you do have some people involved in this designation?

Mr. MASSAD. A few of them—

Mr. LUETKEMEYER. How many?

Mr. MASSAD. —of our staff—

Mr. LUETKEMEYER. One, two, ten?

Mr. MASSAD. It depends on the issue, sir. We are a small agency. We are very limited in our resources. No one is fully dedicated to these issues. But certainly I try to get people involved as necessary—

Mr. LUETKEMEYER. Okay. One more quick comment before I am out of time here.

With regards to the SEC, Ms. White, your numbers are zero, two and now twelve. And in your testimony you indicate or you say that it is important that it be data-driven and conduct rigorous analysis throughout the process.

How can you do rigorous analysis when back in 2013, you made the designation true with 2 people, and now you have 12 people? Was that a stumble back then and you realized you didn't have adequate staff? Or what was the problem back then?

Ms. WHITE. I can only speak to the time since I have been there, which is—

Mr. LUETKEMEYER. You were there at the time this was done.

Ms. WHITE. But I didn't participate in the designation. I would have to drill down a little bit on those figures.

But what we do at the SEC, I think my written testimony reflects this, is—and again, it is not full-time people devoted to FSOC work streams. But who we need in particular areas are called upon to assist me and analyze—

Mr. LUETKEMEYER. The concern is still there that we are not doing our job of doing analysis—

Chairman HENSARLING. Time.

Mr. LUETKEMEYER. —and letting the Fed—

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes another gentleman from Missouri, Mr. Clay, ranking member of our Financial Institutions Subcommittee.

Mr. CLAY. Thank you, Mr. Chairman.

And I thank all of the witnesses for attending today.

Some have criticized the FSOC's designation process as being opaque. The GAO also made several recommendations to the FSOC to improve its transparency.

To your knowledge, how has the FSOC addressed the recommendations of the GAO? Would you also describe how the FSOC changed its process with the February 2015 supplemental procedures announcement? Anyone on the panel can answer. There are so many to choose from. Ms. White maybe?

Ms. WHITE. In terms of the GAO-specific recommendations, I think those were responded to by the Secretary of the Treasury as the chairman of FSOC, not agreeing or disagreeing with the recommendations.

But I do think that the, what I will call the process and transparency changes made by FSOC in 2015 address a number of those concerns in terms of both transparency, and clearer information to companies as to when they can interact, when they are being analyzed in stage two.

There was a lot of back and forth before those changes, but I think a number of those changes are responsive to those recommendations.

Mr. CLAY. Can you—oh, yes, sir? Go right ahead.

Mr. GRUENBERG. Just to respond to your question, Congressman, I think the focus of the Federal procedures was to try to enhance engagement and transparency for the stage two process. So it provided notice to the firm that it could advance from stage one to stage two, an opportunity for the firm to engage with the FSOC staff.

It requested the public information that the FSOC was using as part of that stage two review, as well as notice if a firm is not advanced from stage two to stage three. And if a firm is advanced from stage two to stage three, it would be notified of that and then a set of procedures for engagement with stage three.

So it was an effort to provide both greater insight for the firm in terms of notice and greater opportunity to engage with the FSOC.

Mr. CORDRAY. Could I simply add something? To me, this exemplifies vigorous congressional oversight.

The Congress and this committee have had comments on transparency at the FSOC. We have listened to those. The GAO did a report with comments. We have listened to those.

It is a new body. It is still just a few years old. Transparency is developing and evolving as we go, and I believe has been responsive to a lot of the concerns raised here.

Mr. CLAY. Thank you.

And what changes have you made to the annual and 5-year designation review processes to ensure more due process rights are available to companies? Mr. Gruenberg?

Mr. GRUENBERG. Yes. I think the procedures make clear that as part of the annual evaluation process, a company can submit information, engage with the staff in terms of the information being presented, and get feedback in regard to the process. And the procedures provide an assurance of a hearing with the FSOC at least every 5 years.

Mr. CLAY. General Electric has announced that it would shed most of its financial assets which operated out of GE Capital. In making the announcement, GE noted that the company will work closely with its regulators and the staff of FSOC to take the actions necessary to designate GE Capital as a systemically important financial institution.

Further, the CEO of GE noted that, "We have a constructive relationship with our regulators and will continue to work with them as we go through this process."

Can you describe how FSOC will go about working with GE? Anyone? Yes, sir?

Mr. CURRY. There is an ongoing dialogue with the company as to what its plans are, what its strategic or structural changes are.

And that will continue at an annual review or sooner. A decision will be made once those plans have been actually executed.

Mr. CLAY. I see. Thank you very much.

And Mr. Chairman, I yield back the balance of my time.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, chairman of our Monetary Policy and Trade Subcommittee.

Mr. HUIZENGA. Thank you, Mr. Chairman.

I apologize that I had to step out. I have had some visiting constituents and wanted to make sure that I understood where my fellow Subcommittee Chair was headed. And I think we are kind of on the same path and direction.

I do want to, at some point, Mr. Woodall, get back to your written testimony, which I found very fascinating, and I have a couple of questions there.

But I would like to also see a show of hands. Who here believes that Congress has the right to understand how FSOC makes its determination decisions? So if you believe that Congress should—okay. The record will reflect that all of you believe that is an important part.

I would like to get a sense of what materials FSOC members reviewed before making final determinations. And are there memoranda, other materials prepared by FSOC staff that you rely on to make your decisions?

Who here is willing to share that? If you would give me a show of hands, if you would raise your hand, who is willing to share that with us?

[laughter]

Nobody? Okay. Let me repeat the first question, I guess.

Mr. MASSAD. Congressman? Can I make a comment?

Mr. HUIZENGA. Sure, Mr. Massad.

Mr. MASSAD. I think Congress is entitled generally to whatever information it wants. I would want to simply check with staff in particular to make sure we are abiding by our obligations to keep non-public information confidential.

Mr. HUIZENGA. Sure.

Mr. MASSAD. But certainly, Congress is entitled to get whatever information it wants.

Mr. HUIZENGA. Okay. And maybe that is not even public meeting. Maybe that is a private meeting being able to share that.

So, Mr. Gruenberg?

Mr. GRUENBERG. Congressman, I think the analogy here is one of our regulatory agencies considering action with regard to a particular institution. That is what FSOC is doing.

Mr. HUIZENGA. Sure.

Mr. GRUENBERG. So, two points. One, if we are dealing with confidential, supervisory information which would probably be an applicable standard here in the FSOC. That is generally not shared. Although upon congressional request, as we have in other instances, Congress gets the information it requests.

Mr. HUIZENGA. That sometimes takes longer than the timeframe, if you haven't noticed around here.

Mr. GRUENBERG. I do understand. I think that would sort of be the—

Mr. HUIZENGA. So you believe that Congress has the right to review FSOC's deliberative materials.

Mr. GRUENBERG. I think Congress has the right to request.

Mr. HUIZENGA. Those are two very different things. Okay.

Mr. GRUENBERG. I think if you accept the premise we are dealing with confidential supervisory—

Mr. HUIZENGA. Sure. And if we can do that and whether there are certain things that—what I don't want are redacted sheets that look like they are blacked out all the way. What I am looking for is a venue then for us to be able to review to understand. Because frankly, I think if you hear a lot of questioning on both sides of the aisle, we simply do not understand.

Mr. Woodall?

Mr. WOODALL. I think there is one confidential memorandum that has been made public. The confidential basis in the Metropolitan Life case. It is my understanding has been filed in the court and is a public record.

Mr. HUIZENGA. Okay.

Mr. Watt?

Mr. WATT. I want to be clear that the reason I would not raise my hand is because I would not make a unilateral decision. This is a collaborative body. FSOC, if we got together, would turn over whatever would appropriately be turned over to Congress. And I think I would be a supporter of that being a robust turn over of information. But I certainly wouldn't make even a unilateral decision.

Mr. HUIZENGA. You have sat on this side of the microphone and know that sometimes it takes far too long to get responses.

Mr. WATT. But that is not a justification for an individual member of a collaborative body to make a unilateral decision to turn over confidential information.

Mr. HUIZENGA. I fully understand. So, I would love to have it. But you all just raised your hands. And since you are the voting members, you all said we have a right to this. So, let's come up with a collaborative way of finding out how we are going to do that.

Mr. Woodall, quickly, I was fascinated in your written testimony about how you had been prevented from "being in the room" with international insurance policymakers.

A number of us did a trip to Switzerland back about 2 months ago. They seemed genuinely surprised that Congress was not up to speed on exactly what team USA is saying and doing in that room.

And also I would—as we were indicating, many of us, both sides of the aisle again, that were on this strip, supportive of your involvement in that. They seemed genuinely perplexed that someone with insurance expertise was not being allowed to be a part of that process. So quickly, if you could comment?

Mr. WOODALL. In international things, you work by consensus as you have been told. The consensus within the team USA, you have three U.S. people, representatives at the IEIS.

Mr. HUIZENGA. And you said that you had been supported by two of those for being in the room.

Mr. WOODALL. Right.

Mr. HUIZENGA. The third who is not supportive is?

Mr. WOODALL. It is Treasury right now.

Mr. HUIZENGA. Treasury?

Mr. WOODALL. Without that consensus, and they are taking the position—and I want to be fair about this. They are taking the position that the statute gives me no such authority, that I have no duties or responsibilities designated in the statute at all.

Chairman HENSARLING. The time of the gentleman has expired.

Mr. HUIZENGA. I look forward to remedying this.

Chairman HENSARLING. The Chair now recognizes the gentlelady from New York, Mrs. Maloney, ranking member of our Capital Markets Subcommittee.

Mrs. MALONEY. I thank the chairman and the ranking member for calling this important hearing. And this is actually the most people I have ever seen at that desk at any hearing or reviewed in the history at a hearing. And it is a very important topic. I am glad to see my former colleague, Mel Watt. Welcome back.

My question is, when the FSOC is analyzing whether a company is systemically important, it doesn't measure whether the failure of the company would destabilize the system in normal times. Instead, it measures whether the company would destabilize the system in a period of stress in the financial industry.

And I have two questions for the panel related to this. First, why did the FSOC choose that standard? It seems that this standard could certainly play a key role in determining whether or not a company is systemically important.

And secondly, what historical precedence does the FSOC review in making these evaluations in a period of stress in the financial community? Do you look at the 2008 financial crisis, the Asian financial crisis of 1997 and 1998? What do you look at as precedent when you study these crises?

And I would like to start with Chairman Gruenberg. SEC Chair White, and Comptroller Curry, and the thoughts from the panel on these two questions. Thank you.

Mr. GRUENBERG. Thank you, Congresswoman. I think the view was that would—the impact, the failure the firm would have in a stressed environment would be the most realistic scenario to try to assess this systemic consequence of the firm. And I think it was very much a product, certainly of the 2008 crisis experience.

And I think we looked to the experience in other crises in trying to make these assessments. But I think that was the threshold judgment.

Ms. WHITE. If I could pick up there, I would agree with that analysis that the Council's guidance announced how it would be approaching that. It would be analyzing in a period of stress which would only make sense given what your purpose was in terms of judging—in trying to prevent significant negative impacts on the financial system.

Things that work in times of non-stress, don't work so well in times of stress. In terms of what is looked to, it is not just limited to how things operated in the 2008 period, but certainly that is typically part of the analysis, but you look to other scenarios, stress scenarios, as well.

Mrs. MALONEY. Comptroller Curry? And then, Director Watt?

Mr. CURRY. Congresswoman Maloney, I agree with my colleagues. I think in order to assess, especially the interconnected aspects of the financial system, you have to assume that it is in a period of stress. I also think there is some textural support within the statutory standard to take that approach.

And in terms of what we would look to for the range of historical experience, I think the 2008 crisis certainly stands out in terms of its significance, its breadth, and what I think people never would have assumed would be the underlying source of it or the spark, the housing crisis. And I think that would be our approach.

Mrs. MALONEY. Okay.

Mr. WATT. I was just going to refer you to the specific wording of the statute which says that we—the Council determines that material financial distress at the non-bank financial company, that is the standard that is set up in the statute.

So, it is an appropriate standard, I think. But, again, we are not trying to second-guess the statutory provision that was written by Congress. We are following the statute, not second-guessing it.

Mrs. MALONEY. I would like to ask Chair White, as you know, there has been a great, great deal of discussion this year about how the FSOC could improve its SIFI designation. One of the suggestions I kept hearing, and probably you heard also, was that the FSOC should tell companies what actions they needed to take in order to avoid being designated as a SIFI.

And this sort of struck me as a dubious idea. Because do we really want the FSOC to be making these kind of core business decisions for private companies? And in my opinion, the FSOC should identify the systemic risk. And then the company should figure out the best way to restructure its business to eliminate the risk.

And when the Council adopted changes to the designation process in February, you decided not to include this suggestion.

Can you elaborate on why the Council wanted to maintain this distinction? And do you think it is important for the FSOC not to use the designation process as a way to tell companies how they should be run?

Ms. WHITE. Speaking for myself, I largely agree with your assessment. I don't think FSOC should be telling companies how to structure their business. I do think maximum transparency, as we were discussing earlier, is obviously something that we care about at FSOC and is important to do.

But very often, also, most often, I think the designations are not going to be based on one or two or three metrics but rather a business model. So it is a very complex undertaking, as well. But I don't think FSOC ought to be telling companies how to run or structure their business.

Mrs. MALONEY. My time has expired. Thank you very much.

Chairman HENSARLING. The Chair now recognizes the gentleman from Wisconsin, Mr. Duffy, chairman of our Oversight and Investigations Subcommittee.

Mr. DUFFY. Thank you, Mr. Chairman. Just to reiterate, I believe when Chairman Hensarling asked the panel who had insurance experience, if I recall, it was Mr. Woodall and Chair White. Is that correct?

And if I asked the panel to point out the one insurance expert of all the witnesses today, who would you point to?

Yes, Chair White?

Ms. WHITE. Mr. Woodall.

Mr. DUFFY. Thank you. I would probably agree with you, Chair White.

Ms. WHITE. I overstated my expertise.

Mr. DUFFY. Does it concern the panel that the one person with insurance expertise is the one individual who dissented in the designation of Prudential and MetLife? Or, Chair Matz, as you say, that really doesn't matter because we are not looking at the insurance side, we are looking at the financial services side?

Ms. MATZ. I think that is correct. And, it should be noted that the head of the Federal Insurance Office did support the designation and also has considerable experience in the insurance industry.

Mr. DUFFY. Did they vote on FSOC?

Ms. MATZ. No.

Mr. DUFFY. No, that is right. So Mr. Woodall, who does vote, was the one dissenter—

Ms. MATZ. That is correct.

Mr. DUFFY. Who is the one with insurance expertise, which is concerning.

Does the panel—I think the panel has all agreed on the oversight front that Congress is entitled to do oversight over FSOC. Is that correct? You all agree with that?

Our committee, under the signature of the chairman and every single subcommittee chairman, sent a letter to Jack Lew asking for 13 different points of information from FSOC.

There was partial compliance with a couple of those. Does the panel disagree that if we have already gone through a designation process, that Congress is not entitled to non-public information?

You guys don't disagree with that, do you? Why aren't we getting this information? Why aren't FSOC members complying with our request?

It is concerning for our panel. If you are concerned about the questions that you get today about the transparency of FSOC, it is because the elected members of this body don't have timely compliance or any compliance from Mr. Lew or any of you.

Can—would you—if there has already been a designation, if we are asking questions about AIG, Prudential or GE, I can—you can make the argument that with MetLife there is litigation, so we don't want to give you that.

You might say that. I won't agree with that, but fair enough. AIG, Prudential and GE, will you comply with our requests about the analysis that went into the designation process? The memos, the correspondence, all that information? Everyone here, will you comply with that request?

Raise your hand if you will comply with the request to provide us that documentation.

I have no takers. So, why not? Mr. Gruenberg, why not?

Mr. GRUENBERG. Congressman, if I may say, you raise a fair question. I think I probably want to go back and look at the request. It seems to me the line here is when you are dealing with confidential supervisory information or dealing with the three companies you referenced. They are open institutions. So you have to strike a balance there—

Mr. DUFFY. Chairman Gruenberg, listen. Do you know that there was a recent attack, some alleged by ISIS, in San Bernardino?

Mr. GRUENBERG. Yes.

Mr. DUFFY. You are aware of that, correct? Do you know that this body gets intelligence briefings from the FBI in regard to ISIS and terrorist attacks?

Now, I would argue that American lives are in danger from these radical extremists. Does anyone argue on this panel think that anyone's life is in danger from the work that you do on the FSOC?

Mr. GRUENBERG. No.

Mr. DUFFY. Raise your hand. Is anyone's life in danger? And so we can get FBI briefings but you won't give us briefings on the analysis that has gone into designation of certain companies in America?

Mr. Massad, will you explain that to me? Why am I entitled to briefings on ISIS and not on FSOC designation?

Mr. MASSAD. Well, sir, I can only speak to the FSOC issues. I am not familiar with the intelligence side. But I would say that as a general matter, I think, certainly transparency and accountability is important—

Mr. DUFFY. No, no. Explain why I get ISIS FBI briefings and you can't send me information on designation.

Mr. MASSAD. I do think there are issues that we have to think about in terms of the non-public nature of certain information—

Mr. DUFFY. No, no. The FBI sends me non-public information, as well.

Mr. MASSAD. I respect that, sir.

Mr. DUFFY. Are you making decisions that affect someone's life?

Mr. MASSAD. No.

Mr. DUFFY. Is ISIS affecting people's lives?

Mr. MASSAD. Yes.

Mr. DUFFY. I would think that is far more serious. And the information that we are entrusted with is far more serious than the information you have and aren't complying with.

Mr. MASSAD. I do think—

Mr. DUFFY. One quick question. The Bank of England sent a letter to FSOC asking questions about why Berkshire Hathaway is not being considered as a SIFI. Some have argued they have political clout in this town. I think Barack Obama said he is a great friend.

Is there a political analysis and connectivity with people in power that go into the determination of designation on FSOC?

Quick answer, maybe, Mr. Chairman?

Mr. WATT. Not from me.

Mr. DUFFY. Anyone?

No. I yield back.

Chairman HENSARLING. The Chair now recognizes the gentleman from California, Mr. Sherman.

Mr. SHERMAN. Thank you.

Folks, I do think that your decisions are life and death. You will never meet the people. But if we have another 2008, every one of our districts will have higher divorce rates, higher unemployment rates, and higher drug use rates. And we will never be able to go to a particular funeral the way you can in San Bernardino and say, this is what happened. But there are thousands of Americans who would be alive today if we didn't have the 2008 meltdown.

So your work is every bit as important as those who are focused on terrorism.

Ms. White, we have the Financial Stability Board. We don't have—well, we have one of its members here. But it doesn't answer to the American people. How can we be sure that they don't push us to an activities-based approach on asset managers or anything else, that the decisions that are made that affect the American people will reflect the decisions made by those answerable to the U.S. Government? And that it won't be just a matter of, well, we went to the meeting, everybody else kind of wanted to go in this direction.

I have seen this—people talk about terrorism. We made loans from the World Bank to IMF and I was told, we would never let that happen, it is all consensus. Then they came back and said, sorry, we got outvoted.

So how do I know that to get along we are not going to go along with policies that don't reflect the U.S. decision-making?

Ms. WHITE. As you point out, the Treasury, and the Fed, and the SEC, actually sit on the Steering Committee of the FSB, and have since 2009, when it was established very importantly to look over potential risks to financial stability globally.

But whatever comes out of the FSB in terms of recommendations or suggested standards is not binding on the United States and certainly with respect to where there is overlap, for example in the designations that have been talked so much about. We act independently of the FSB. There are separate processes.

Mr. SHERMAN. Thank you.

There is all this focus on whether an organization—an entity has a lot of assets. Lehman Brothers didn't go under because it had too many assets. It went under because it had too many liabilities in contingent liabilities.

Ms. White, when you analyze whether an entity should be designated as a SIFI, do you look at the size of their assets, the size of their balance sheet liabilities, or the size of their off-balance sheet—contingent liabilities, including credit default swaps?

Ms. WHITE. All of the above and then a host of other factors, too. So that you can—

Mr. SHERMAN. I would hope that you would focus on liabilities rather than assets. No one ever went under because—

Ms. WHITE. Understood.

Mr. SHERMAN. —they had too many assets. But in looking at contingent liabilities, Mr. Woodall, I hope that we would not count those contingent liabilities of regulated insurance companies, because the State regulation of insurance companies seems to have weathered the storm.

Would we designate a company as a SIFI just because they had a lot of assets and liabilities if all the assets and liabilities we are looking on were part of State regulated insurance companies where the State regulators determined they had adequate reserves?

Mr. WOODALL. Yes, Congressman. One of the factors is the regulatory scrutiny that the company goes through. And obviously, we do have to look at not only assets and liability but the matching of the assets and liabilities. And in insurance companies, those liabilities are long-term liabilities. They are not like liabilities of a bank that could disappear if everyone came in and withdrew their account.

Mr. SHERMAN. Dodd-Frank calls for an annual review of designations. Do you have a way for a company—do we have a good process to allow companies to be de-designated, particularly if they have reduced their risk profile?

Ms. White?

Ms. WHITE. I think there is a good process. You always want to keep looking at possibly enhancing it. But essentially, at least annually, the Council has to look at that.

It was also made clear that the companies can engage with the staff on those issues. And then every 5 years, under some of the new procedures, they are entitled to a full hearing.

Mr. SHERMAN. I hope that you will refine that process further. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Oklahoma, Mr. Lucas.

Mr. LUCAS. Thank you, Mr. Chairman. And since we have this distinguished panel together, I would like to visit about my concerns with the Basel III leverage ratio rule, as it is applied to certain derivative clearing services and the impact it will have on the ability of my constituents to hedge risks.

So first, I would turn, of course, to our derivatives market regulators, Mr. Massad and Chair White. When market participants utilize derivatives to manage their risk through futures, options, and cleared swaps, they must find a member of the clearinghouse willing to guarantee their transaction with the clearinghouse.

How does the margin that a market participant posts to a clearing member affect the clearing member's ultimate guarantee exposure to the clearinghouse?

Mr. MASSAD. Thank you for the question, Congressman. I do believe it does reduce that exposure. Let me say generally on this issue that I support strong bank capital requirements and I support the SLR generally. And the issue I have raised is really a very narrow one.

I don't believe we should be excluding derivatives from the SLR, but I do believe it is important to make sure we are measuring the exposure accurately and I do believe that the margin that is held by the CCP—in other words, margin collected but then actually transferred to the CCP—that we should think about that in terms of how we recognize the exposure.

Mr. LUCAS.Chair White?

Ms. WHITE. I would just add that I think you should always be judging the impacts such as you described, frankly, in a variety of contexts and a variety of different rule contexts as well.

Mr. LUCAS. And I will now turn to our banking regulator friends, Comptroller Curry, and Chairman Gruenberg. In many instances, these clearinghouse members are banks subject to Basel capital requirements which require them to hold capital against the guarantee they provide on behalf of their clients.

Now we can all agree that banks have exposure in the event their clients are unable to fulfill the obligations and banks should hold capital against that exposure. But shouldn't that measure of exposure accurately reflect the client's margin, offsets the bank's exposure to the clearinghouse?

Mr. CURRY. Congressman, I think the number one protection in the clearinghouse context is really that the member bank be strongly capitalized and be able to perform in adverse circumstances.

So having strong capital ratios really is a fundamental part of our regulatory structure and the safety and soundness of the system, including the clearing of swaps.

I want to point out that a leverage ratio is not by definition a risk-based measure. So by definition, it would be inconsistent to import measures of exposure or risk as a general matter.

Mr. GRUENBERG. Congressman, I agree with Comptroller Curry. I think the core issue here is, the margin is posted with the CCP, but in addition, the CCP is asking the intermediary bank for a guarantee. And the potential loss from the derivative exposure could substantially exceed the margin that is posted with the CCP.

That is why the guarantee is imposed and the capital is really designed to protect the bank against the downside risk from that derivative exposure.

Mr. LUCAS. I would just simply note to my friends, if we create a system that we require such capital requirements above and beyond what would appear to be necessary, we will cause financial institutions to not participate.

And the next time we have a Lehman Brothers or an FM Global and a major failure and their clients need quickly to find a new clearing number, a new place to cover their outstanding positions of their margin, there may not be any sources.

Having been a member of this committee through the wonders of 2008, when the worst-case scenario occurs, you have to be totally prepared. I am just concerned with Basel, we are headed in a direction that will limit my constituents' options, thereby increasing their costs and reduce these risk-mitigating tools. So I would just simply note that to all of you and ask that you bear that in mind.

We are undergoing pressure back home now in Oklahoma in both the agriculture and energy sectors. It is real pressure and it is something that will take time to overcome. But these tools have been and continue to be important. So let's not allow Basel to cause unintended damage.

With that, Mr. Chairman, I yield back the balance of my time.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Massachusetts, Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman. I want to thank the witnesses for your willingness to help the committee with its work today.

I have a question for Chairman Gruenberg. A number of the members on this committee have been working with Vice Chair Tom Hoenig on a proposal that would give some regulatory relief to some of our small banks.

Now, we are looking at banks, community banks that are in the traditional business of banking, taking deposits, making loans to businesses and individuals. And the way this would work, we have not accepted all of Vice Chairman Hoenig's recommendations, but we have focused on a number of them which would be to be eligible for regulatory relief, the financial institution must hold no trading assets, no derivative positions other than interest rate or foreign exchange, have a limited notional value of all the bank derivative exposures or otherwise, and maintain a ratio of gap equity to assets of about 10 percent; no less than 10 percent, I'm sorry.

And in return for that, under this legislation, we would give relief in this form. The compliant banks would be exempt from Basel risk-based capital standards. The test, the stress tests, in some cases, they would be exempt, in other cases, the stress test would be every 18 months instead of every year, so we are trying to reduce the cost there for compliance. And also exemptions from submitting call reports and schedules.

Now, this actually goes back to Mr. Sherman's question before where we are actually regulating activity, not necessarily size. So if a bank is not engaged in risky activity, we think—and they are doing the right thing—we think they a ought to be entitled to relief. And this has been a high-cost issue for the smaller banks.

I just wanted to get your sense on whether this is something that you would be receptive to?

Mr. GRUENBERG. Congressman, I am similarly sympathetic to the concept, the core concept being that if a smaller institution is very strongly capitalized on the leverage ratio—that is the 10 percent that you referenced—and does it engage in high-risk activities, it would be eligible to reduce or compliance with risk-based capital standards. I think that core concept really makes some sense and I think that is certainly is an issue for Congress to consider.

And I think as part of our regulatory review process, within the framework of our capital rules, that may be something that we might be able to consider on a regulatory basis.

Mr. LYNCH. Okay. I do want to fixate on that word "sympathy" because I think a lot of our small banks are good with the sympathy. They are looking for actual relief now.

Mr. GRUENBERG. I am—let me say I am open to pursuing that approach.

Mr. LYNCH. All right. Mr. Cordray, do you have any worries about that? Have you thought about that proposal? I don't want to—you might be out of pocket on this issue, I am not sure.

Mr. CORDRAY. No. We have been—if you look at our mortgage rules, we tiered the application of those rules on the qualified mortgage, what we call the ability-to-repay rule. We made special provisions for smaller creditors, and in fact, they have increased their share of the mortgage market, credit unions and community banks.

And frankly, it is appropriate, because if you look through the financial crisis, the default rates on loans that were issued by smaller creditors, particularly depository institutions, had a much better—that is, lower rate of default—than other mortgages made generally in the marketplace.

So where we can take that into account and think about how we can apply different provisions for different levels of risk, I think that is entirely appropriate.

We will continue to do so.

Mr. LYNCH. You hit right on a point that I didn't mention, which is that in most cases where a bank is willing to keep their FAT mortgage in their portfolio, it would be deemed a qualifying mortgage because you are not issuing to sell it.

Mr. CORDRAY. We are comfortable with that, particularly for smaller entities, but there were larger entities before the crisis that kept mortgages on their balance sheet and blew up the system, Washington Mutual, Countrywide, and others. So at smaller levels, I am quite comfortable with that.

Mr. LYNCH. All right, fair enough.

Thank you, Mr. Chairman. I will yield back.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from California, Mr. Royce, chairman of the House Foreign Affairs Committee.

Mr. ROYCE. Thank you, Mr. Chairman. Last month, in a hearing before the committee about due process issues with the FSOC, Professor Jonathan Macey of Yale Law School stated that with respect to the actions that the FSOC have already taken, there is a significant danger of increasing rather than decreasing systemic risk.

His point, as he explained, was that this was because the FSOC is ignoring certain risk mitigation strategies and herding entities into particular risk strategies, which decreases diversification and then increases the systemic risk.

This could also happen indirectly with companies making choices to merge, sharing in the cost of compliance and creating greater economies of scale. We have seen this in the banking sector, or more directly, with the implied or explicit backing of the government, as in the case with the GSEs.

So I was going to ask Mr. Curry, do you view the potential for regulators to create systemic risk as a problem, and what actions have you taken to make sure that—and I will also ask Chair Matz, that the FSOC's designations and enhanced prudential standards of the Fed are not increasing systemic risk, per the thesis that the Yale professor puts forward.

Mr. CURRY. Congressman, the FSOC actually is looking at, and this is referenced in our annual report, some of the consequences of changes within the marketplace, including regulatory changes. There are behaviors that have changed. Institutions have either left or entered different types of business, the impact of non-banks.

Those are all things that we have identified as emerging or potential emerging risks that require further monitoring, and if necessary, potential action down the road.

Mr. ROYCE. And Chair Matz, if you could just weigh in there?

Ms. MATZ. Thank you. More specifically, as the designation is being considered, the company has an opportunity to present any evidence to the staff, whether in person or in writing, and so if they think that there might be information that would be helpful in determining whether to designate, they have every opportunity to make that information available to us.

Mr. ROYCE. And lastly, I will just ask Chair White, do you agree that this is a problem? Would you like to weigh in on it?

Ms. WHITE. I think it is certainly something that I think we need to be constantly keeping in mind with all of our regulations, what impacts they are having, what mitigators we ought to be considering in addition.

Mr. ROYCE. Now I am trying to better understand how the interaction on another subject here, between the Office of Financial Research and FSOC members works. After criticism by this committee in public on an OFR report regarding the asset management industry, the FSOC sought public views on the industry, and later issued a request or notice and comment on asset management products and activities.

Separately, the SEC put out the OFR report for public comment. Can I ask the panel, do any of you see a reason why all OFR public reports should not be open to the public notice and comment? Does anyone take exception to that concept?

For the record, Mr. Chairman, I would like to say that the witnesses, for the record, saw no reason to continue the practice of OFR not allowing for public comment on their reports. That is the point I wanted to make. I think it is important that they do so.

If I have time here, the FSOC has not designated any asset managers as SIFIs, which is a step I support, as these firms operate with little leverage, if any, and the risks they manage are borne by those whose funds they invest.

But the FSOC is now apparently considering the industry under activities base regulation, the second prong of Section 113 of the Dodd-Frank Act, rather than material financial distress, the first prong.

My question is not about asset managers but rather how FSOC came to this decision and why a similar process wasn't used when designating insurance companies?

Mr. Woodall, is it fair for the FSOC to offer different amounts of process to different industries, and why not take the same amount of time and get it right?

Mr. WOODALL. Congressman, I think that we have already discussed the fact that in activities, which has been my main goal in the insurance company, it is evolving now in the Council. The Council is young, it is evolving, and I welcome the idea of taking a pause and getting into looking at the activities across the segment. I hope that they will do that for the insurance industry.

Mr. ROYCE. Thank you, Mr. Chairman.

And thank you, Mr. Woodall.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you very much, Mr. Chairman. Panel, I am very concerned about the Department of Labor's fiduciary rule. Let me explain why.

I have spent most of my adult life working hard in the area of wealth building in the African-American community, and our President is a wonderful person; he is a decent, good man. But as an African-American, I am not sure that he has been properly advised as to how devastating this Department of Labor ruling will be on the African-American families in terms of wealth building.

Now I say that as one who—I am a graduate of the Wharton School of Finance, where I got my MBA. I went off and much of my work has been in investment. I had an investment portfolio in my own business that I started. As a result of that, they put me on the board of directors, the executive board of directors of the Wharton School.

And there, in that position, we pulled together, along with John Sculley, who was the chairman of our board and chairman of Pepsi-Cola at the time, an extraordinary program of wealth building. But what we found out was there were three elemental areas that prohibited wealth building and investment: education; financial advice; and the overarching complexity and diversity of the investment options in our system.

This Department of Labor rule will have a devastating effect on the African-American community, and on other lower and middle income, because they don't have that money to pay up front the fee costs. And when you put a contract there for them to sign, they are going to run away. I know. I have been there. I have worked with the African-American Chamber of Commerce on this.

So what I want to ask you all, you all are the Financial Stability Council of the United States Government. Take for a moment and look at the most unstable financial caring in this country as in African-American communities. Is it not too much for somebody on your committee to ask the President to hold off until we actually see just how devastating it is, affecting African-Americans? That is what I am asking you to do.

I asked Ms. White the other day in our meeting at the SEC, but she seems to have ceded her authority to the Labor Department, when we clearly put it, as you know, Mr. Watt, you were here. We wrote it into Section 913 in Dodd-Frank, that was the domain fiduciary of the Securities and Exchange Commission.

At no time did we hear from the Labor Department at the recent—talking about they had the retirement. And if they do, wouldn't it be respectful for them to sit with the regulatory agency that handles financial investments—the SEC and FINRA and work that out? I just urge you to examine these because the devastating impact is terrible.

My paper—the Atlanta General Constitution—I urge you to read it. Sunday's edition—front page of the business talks about the struggle of African-American families to build and growth wealth. And the number one reason why it is so slow is they can't get the education or the information.

Rich people investing, they don't have any problem. They can pay for that fee for service and most of them do. But when you get to annuities or trying to turn your life insurance into whole life or whatever you need advice for that.

Anyway, I urge you to ask the President to put a pause on this and let us see what the impact is on the Black families. Now, Mr. Massad, I wanted to—I think I have time. We had a terrible problem with the European Union on this equivalency with derivatives.

December 15th is the deadline and I want to know because it is going to have a devastating effect on our end users, on our exchanges and clearing houses. If we don't get equivalency in terms of our regulatory regime with the E.U. especially when they have given equal status to Singapore and other areas. What is the status on that in that we are just a week away from the deadline?

Mr. MASSAD. Thank you, Congressman. They have pushed out that immediate deadline. I think we are still working in good faith to try and resolve this. I think we have narrowed our differences. I am hopeful that we can do so.

I of course believe they should have granted us equivalence some time ago but I recognize the issues that they are concerned about. And we are working very hard to work them out.

Mr. SCOTT. Thank you, sir.

Chairman HENSARLING. The time of the gentlemen has expired. The Chair now recognizes the gentleman from Ohio, Mr. Stivers.

Mr. STIVERS. Thank you, Mr. Chairman. I appreciate all of you for being here. I would like to go on a quick tour of the segments of the financial services industry. How many of the witnesses believe that small banks and credit unions caused the crisis in 2008? Could you raise your hand if anybody believes that? Okay. I would like to note that no one did.

You have an important role as a coordinating council of regulators as well and I am curious if you could go down the line, starting with Ms. White, and tell me how many hours in the last year you have spent discussing and identifying regulatory conflicts and unnecessary regulations that might be harming our community banks and credit unions?

Where better coordination could reduce unintended consequences and costs and differing regulatory interpretations by agents in the field. Just how many hours this year the Council spent talking about that? Just if you could each give me a number and we could do this quickly.

Ms. WHITE. I do not think we have a very accurate estimate. Those discussions have occurred at the staff level but I can't say.

Mr. STIVERS. You would say zero—

Ms. WHITE. I wouldn't say zero but yes.

Mr. STIVERS. At the staff level, okay but on the Council. That is what I care about. That is who you are. Let's keep moving.

Mr. MASSAD. I also could not give a number but I—

Mr. STIVERS. Okay. Sounds like another zero. Keep moving. Mr. Woodall?

Mr. WOODALL. I don't think there is a definite figure, but I think there has been discussion leading up—

Mr. STIVERS. Okay. So some discussion. Nobody can put a number on it in hours. Ms. Matz?

Ms. MATZ. I would agree that—

Mr. STIVERS. You would agree you don't have any idea how many hours but it has happened—

Ms. MATZ. No—but I think it has happened but—

Mr. STIVERS. Okay. Let's keep moving. Obviously, there is a pattern. Does anybody have a number? Will anybody give me any kind of number?

Mr. WATT. I quit keeping time when I left—

Mr. STIVERS. Good man—

Mr. WATT. —to practice law, Mr. Stivers.

Mr. STIVERS. I am still keeping time so let's move—

Mr. WATT. We spend a lot of time—

Mr. STIVERS. I got it.

Mr. WATT. —discussing a lot of issues and I—

Mr. STIVERS. Okay. I think we have a pattern—

Mr. WATT. Regulatory overlap is one of those I think—

Mr. STIVERS. I appreciate it. I think we have a pattern here. You are not discussing it enough at the Council level. The staff is discussing it but you need to discuss it. These are important community assets that dot the fabric of our country and the 15th district of Ohio. And these companies—small companies, small banks and credit unions are struggling to keep up.

Many of your field agents actually misinterpret regulations intended for big banks and put extra pain and cost on these small banks and they are having real struggles. Let's move on to regional banks. How many of you believe that regional banks, which I will define as kind of $50 billion to $250 billion, caused the crisis? Again, no—oh, I have a couple of hands there maybe.

Mr. GRUENBERG. Just to make the point for what it is worth and—

Mr. STIVERS. We are running out of time. It can be quick.

Mr. GRUENBERG. The regional banks generally are individually not systemic. I would point out that as was mentioned earlier the most expensive bank failure during this crisis and in the history of the FDIC was a $12 billion loss caused by the failure of IndyMac, which was a $30 billion thrift. So a regional institution can have its—a failure of one or more regional institutions can have a significant consequence—

Mr. STIVERS. It can, and I believe that. So let's talk about what you have done to use your regulatory flexibility that Secretary Lew says you have between trillion dollar banks and $50 billion banks. Can anybody explain to me exactly how you have used that regulatory flexibility? Mr. Curry?

Mr. CURRY. Congressman, the OCC supervises a range of institutions: small rural banks to globally active banks. We are very concerned about the regulatory burden, particularly on community banks. The FSOC is not necessarily the forum where we discuss reducing regulatory burden. We do that on the banking and credit union side on the Federal Financial Institutions Examination Council (FFIEC).

We really are concerned about the impact the EGRPRA process really is designed to reduce regulatory—

Mr. STIVERS. I appreciate that, Mr. Curry and I want to talk about that. But we are talking about regional banks now. So can you tell me how you use the flexibility that—

Mr. CURRY. Definitely, definitely—

Mr. STIVERS. Secretary Lew says you have. Have you used it? And if so, exactly how—

Mr. CURRY. Yes. As a supervisor of a number of regional or midsized institutions we place a great deal of value on collaboration and coordination with our other regulatory agencies. And I would include the Fed, the FDIC and the CFPB. It is really a regulatory imperative to make sure we are working together and not—

Mr. STIVERS. You haven't answered how—you are trying to eat up time here, it sounds like.

Mr. CURRY. No.

Mr. STIVERS. You have not answered one specific way in which you have used your regulatory flexibility. Could you give me one specific way, Mr. Gruenberg? One way. That is all I am asking.

Mr. GRUENBERG. As you know, Congressman, one of the consequences of—is a requirement of submitting a resolution plan. And we certainly for the smaller institutions have—

Mr. STIVERS. The tailored plan is the only true answer. And how—that cuts a little cost but they still have to do the CCAR stress test, the regular stress test. There are way too many things built in that you have the power to fix and I wish you would take a look at it. I didn't even get to non-bank financial entities and my time has expired. But please look at those things. Thank you, Mr. Chairman. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Texas, Mr. Green, ranking member of our Oversight and Investigations Subcommittee.

Mr. GREEN. Thank you, Mr. Chairman. And I thank the ranking member, and of course I thank the august body of witnesses who have appeared today. In my years on the committee, I don't think I have seen quite the number of financial stability heads assembled at one time for the purposes of questioning. So I thank you for being here.

Mr. Woodall, much has been made of the fact that you are the only person on the FSOC with insurance expertise. Incidentally, is that the only area that you claim expertise in? Do you claim expertise in other areas to this extent?

Mr. WOODALL. I will say being on the Council is a learning experience. They are learning about insurance and I am learning about banking.

Mr. GREEN. So you don't claim expertise in banking but you are learning about it. Mr. Woodall, based upon what has been said, there seems to be an implication or an indication that only persons with insurance expertise should judge an insurance company. And I ask this because MetLife has appealed its case in this study that is file in a district court in the District of Columbia—Federal District Court. Do you think that judge ought to be an insurance expert to hear the MetLife case?

Mr. WOODALL. I am not going to make any statements about the MetLife appeal.

Mr. GREEN. I understand. I will continue to ask you questions and you will continue to have no response. Do you think that the jurors who will hear the MetLife case—if we do have a panel of jurors—will have to have insurance expertise?

Mr. WOODALL. Of course not.

Mr. GREEN. Of course not.

In fact, across the length and breadth of this country on a daily basis, we have jurors who are ordinary, everyday working people who hear complex cases involving antitrust, billions of dollars. In Texas, you had the Pennzoil case; there were lots of laypeople there hearing a case. People hear these cases all the time and make life-and-death decisions who don't have expertise in a given area that the case happens to be focused on.

Do you agree with this, Mr. Woodall?

Mr. WOODALL. I would say that the FSOC—

Mr. GREEN. I think you do. Let me continue. It appears to me, Mr. Woodall, that the indication of only a person with expertise in a given area should be able to judge would lend itself to asking at least one question. Have you made any decisions with reference to banks since you have been on the FSOC?

Mr. WOODALL. Banking regulators are the ones who do that.

Mr. GREEN. But have you voted—have you had a vote on anything related to banks? Have you had a vote since you have been there on anything related to banks?

Mr. WOODALL. Not as such.

Mr. GREEN. Not as such. I don't have the time to drill down with that, Mr. Woodall. There is a way to get to the "not as such" answer, but I don't care to do it now. So have you voted as such on some things related to banks?

Mr. WOODALL. Obviously, we get into financial market utilities—

Mr. GREEN. I understand. So you have not recused yourself from issues related to banks? You have voted because you are a Phi Beta Kappa from Kentucky. And as a Phi Beta Kappa from Kentucky, you can understand these banking issues, can't you?

Mr. WOODALL. Yes. And they can understand insurance issues—

Mr. GREEN. And that leads me right to my next question. Thank you so much, Mr. Woodall.

My next question is this: If you believe that a person must have insurance expertise to sit in judgment of an insurance company on FSOC, raise your hand. If you think you only can do it if you have insurance expertise, raise your hand. Anyone? Let the record reflect, none.

But because I want the record to be perspicuously clear, let me ask the question another way. If you believe that you can sit in judgment of an insurance company and not be a Phi Beta Kappa from Kentucky, raise your hand, please. If you believe you can. All right.

Mr. WOODALL. You have voted for—

Mr. GREEN. You are the only person who thinks that you have to be a Phi Beta Kappa from Kentucky. I see his hand didn't go up. So Mr. Woodall, I assume that I should now put in the record that you are a person who believes that you must be a Phi Beta Kappa from Kentucky before you can sit in judgment of an insurance company on FSOC? Should I put that in the record?

Mr. WOODALL. No, but I think you should put in the record—

Mr. GREEN. Okay. That should go in the records. I am going to take it from that comment, Mr. Woodall, that you joined the rest of your colleagues and let the record should show there is unanimous consent that you don't have to be an insurance expert to sit in judgment of an insurance company.

Mr. WOODALL. I am not sure what an insurance expert is.

Mr. GREEN. I am glad you said it, because some people have claimed that you are, so my assumption is that you don't know what you are.

Mr. WOODALL. That is because it was put in the title of Dodd-Frank.

Mr. GREEN. Okay. Well—Mr. Woodall—look, by the way, let me share this with you before I end. Mr. Woodall, I want to make this very clear: I love you.

[laughter]

Because sometimes it can appear that I don't love people because I have to ask the tough questions, and I regret that I didn't get to some other things. But God bless you, dear brother. I love you.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Illinois, Mr. Hultgren.

Mr. HULTGREN. Thank you, Mr. Chairman. And thank all of you for being here.

I am going to address my first question to Chairwoman Matz, if that is all right. You said earlier that designation of insurers was not about life insurance activities; it was about financial activities. My understanding was at the time of the designation, which again, my records show to be June 30, 2013, the reference date for much of FSOC's analysis, 98 percent of MetLife's consolidated assets, 96 percent of its liabilities and 95 percent of its revenues were in these highly regulated insurance subsidiaries.

So I just wanted to make sure I understand the basis for your decision. Are you saying that FSOC analyzed only 2 percent of MetLife's consolidated assets and only 4 percent of its liabilities and 5 percent of its revenues? These activities are outside of regulated insurance entities at the company, I believe, and found that those assets alone to be systemically important and a threat to the financial system? Is that your testimony?

Ms. MATZ. I do want to say that we cannot comment on MetLife, but in terms of our designation of other insurance companies, we do look at how their balance sheet and off balance sheet activities are interconnected with other systemically important institutions.

Mr. HULTGREN. I am going to stick with Chairwoman Matz on this, then open it up to others as well.

As all of you should know, insurance companies are extensively supervised by States. Despite the existing regulation, FSOC has designated three insurers as systemically important. Chairwoman Matz, could you provide an overview of how and why you determined the State insurance regulation, and in particular, State guarantee system for failed insurers, is ineffective?

Ms. MATZ. Thank you for asking that. I don't think any of us—and I can't speak for anyone else, but on this, I would say that I don't think any of us think that the State insurers are ineffective.

But our mandate is to look at how the activities of the insurance companies affect the financial stability of the United States. They are really looking at the effect on policyholders. It is a very different direction that they are taking.

Mr. HULTGREN. With making that determination of what you should pull away from the States—again, clearly legislatively, authority—most authority of regulation for insurance companies is with the States.

I would argue both for protection of policyholders, but also—protection of policyholder would, by definition, State—you know, financial stability of that company. Those would be directly related. Those aren't separate issues.

So what specific information analysis did you, as a voting member of FSOC, rely on to reach the determination that should be separated out, that States were unable to handle this?

Ms. MATZ. As I said, they have a different mandate than we do. They are looking at the institution and the solvency vis-a-vis the policyholders. We are looking at the institution and its interconnectedness with other institutions and its ability to threaten the financial stability of the United States.

It is a different mandate. It doesn't mean that they are doing their job any better or worse than we are or vice-versa. It is just a different tack that they are taking.

Mr. HULTGREN. As you are making this decision, was there an independent analysis done by your agency?

Ms. MATZ. An independent analysis of?

Mr. HULTGREN. Again, the standing, I guess, of these insurance companies, their ability, if there was a threat nationally to financial markets or—I would say also to policyholders, was there an independent analysis done by your agency to make the determination, again, that the States weren't capable of doing this, that this was something that you all needed to do?

Ms. MATZ. We rely on the FSOC staff. We did not do an independent evaluation, no.

Mr. HULTGREN. Let me switch in my last minute here—a little-discussed provision of the Dodd-Frank Act, Section 170, directs the Fed, on behalf of and in consultation with FSOC, to issue regulations setting forth criteria for exempting certain classes or categories of non-bank financial companies from heightened Fed supervision.

However, to date, no such regulations have been issued. This requirement represents a tool Congress created to delineate between those entities that pose systemic risks and those that do not, and provide clear criteria for institutions on how to conduct their business and structure their operations in such a way as to be non-systemic.

Chair White, in the last few seconds I have, why has this provision never been used?

Ms. WHITE. I really can't answer that. It would have to come from the Fed initially.

Mr. HULTGREN. I guess, in my last seconds, just a show of hands, following on my friend from Texas, who among you has advocated for a class of financial company to be exempted from heightened supervision? If you could raise your hand, if you have advocated for a class of financial company to be exempted from heightened supervision?

For the record, nobody raised their hand. My time has expired. I yield back, Mr. Chairman.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from Ohio, Mrs. Beatty.

Mrs. BEATTY. Thank you, Mr. Chairman. And thank you, Ranking Member Waters.

Let me associate my opening comments with those of my colleagues. As someone relatively new, I have certainly never seen the number of people, which is not as important as the work and the service you do. So thank you for that.

We have heard a lot of questions about what you don't do. What is interesting to me is, I listen to the example about what you would provide as it relates to giving us information. And I think the analogy was to us getting classified information for ISIS.

We certainly know, from everything we have read and we have heard that our country is in trouble. So you were asked, and given that analogy, do you think, since your role is to protect the financial stability for us, are we in financial crisis right now, as we were, let's say, in 2008?

So I am trying to get—are we like ISIS is, to a threat in your world? And that is a yes or no, if you could just go down the panel. Are we in that same kind of threat in financial?

Ms. White?

Ms. WHITE. No, but I think we can't be complacent.

Mrs. BEATTY. Yes or no, straight down. Quickly.

Mr. MASSAD. I would agree with Chair White's statement.

Mr. WOODALL. Me too. No.

Ms. MATZ. No.

Mr. CORDRAY. No.

Mr. WATT. I agree.

Mr. GRUENBERG. No.

Mrs. BEATTY. Okay. I have an insurance question, but I will come back to that, Mr. Woodall, since you have been asked so many questions about this.

I also would like to associate, for the sake of time, myself with the words of Congressman Scott from Atlanta as it relates to not only the issue he talked about, but more importantly about Black wealth or minorities.

I am very concerned, and I know many of you have OMWE boards. But my question is beyond OMWE because I am not pleased with the answers that I have been given by you all with OMWE. While it is a big deal to me in Section 342, I don't think people have taken it as seriously as we should.

With that said, as a group, as you look at making your projections, as you evaluate where we should be financially, can at least three of you tell me what you do with minorities, and more specifically African-Americans, as it relates to banks, financial institutions? How are they included? Because you make projections that affect us and our constituents. And so I am concerned. Can anyone address that, quickly?

Mr. CURRY. I will start in terms of what we do with minority-owned institutions and populations. In terms of minority depository institutions, I have an advisory committee that advises me on the issues facing those committees, how we can help alleviate those issues through technical assistance and other means that are mandated by the statute.

As a bank regulatory agency we also enforce the Community Reinvestment Act, which has a direct impact on low- to moderate-income communities. And we have active outreach efforts associated with that in both banks and interested groups.

Mrs. BEATTY. Okay.

Mr. CORDRAY. I would—

Mrs. BEATTY. —quickly.

Mr. CORDRAY. I would add that we enforce the Equal Credit Opportunity Act. We work with the Justice Department on those matters. We recently resolved the largest redlining mortgage lending matter in the history of this country.

We have had significant matters in auto lending discrimination and credit card as well. This is an important means of making sure that everybody across our society has equal access to credit and aren't discriminated against on the basis of race and ethnic origin.

Mrs. BEATTY. Okay. We will take one more.

Mr. GRUENBERG. Congressman, I will just mention we also have an extensive program as required by law to support minority depository institutions. The FDIC also has an advisory committee on economic inclusion where one of the things we focused on is asset building for low- and moderate-income families. And certainly the mortgage crisis, as you well know, had a disproportionate impact on the minority households and African-American households.

Mrs. BEATTY. Okay. Thank you.

If Congress were to reduce stability of FSOC to perform its statutorily mandated function of overseeing financial markets for threats to stability, how could that impact the U.S. economy? We will go to the other end. Ms. White?

Ms. WHITE. It would defeat the entire purpose of FSOC, which is a very important one, which is to look out for the financial stability of the U.S. financial system.

Mrs. BEATTY. Okay.

Mr. Chairman, the Commodity Futures Trading Commission—later today the committee will be marking up a data security related bill, which I am sure should be very interesting to us. I am interested to hear what measures specifically FSOC has taken to facilitate dialogue to help us protect that.

Mr. MASSAD. I think generally, FSOC has taken the issue of cybersecurity, broadly speaking, very seriously. It has listed that as a primary concern in its annual reports.

It is—FSOC also serves as a very useful way for all of us as members to compare notes and coordinate what we are doing individually in our agencies.

Mrs. BEATTY. And do we have any—my time is up, I am sure. Do we have any best practices developed? Yes or no?

Mr. MASSAD. I think, most definitely so. A lot of us are very focused on those best practices issues. We are in our own agency, I hope that we will come out with some standards specifically on—

Mrs. BEATTY. Thank you. And—

Chairman HENSARLING. The time of the gentlelady has expired.

The Chair now recognizes the gentleman from Florida, Mr. Ross.

Mr. ROSS. Thank you, Mr. Chairman.

Mr. Woodall, I have to just follow up on what my colleague from Texas was pursuing. And as a litigator of 25 years I know that the trier of fact, whether it be a jury or judge, must rely on evidence brought before them. And that evidence, of course, is in the best form when it is brought by an expert. And when that expert testimony is uncontroverted then it becomes clear matter of fact that that opinion should gain the day.

Clearly on this board, on FSOC, you are eminently qualified and by far the only person who could be considered an expert in the insurance arena. You have experienced not only academically but also practically as an insurance commissioner.

So I have to ask. What was it, in your opinion, that drew FSOC to disregard uncontroverted expert insurance opinion, and designate MetLife and Prudential as SIFIs?

Mr. WOODALL. I think what you outline might be a professional disagreement. I have a lot of respect for all my colleagues. We had a very hearty debate. I listened to them and they listened to me and we—

Mr. ROSS. I don't think they listened to you, is the problem.

Mr. WOODALL. —agreed to disagree.

Mr. ROSS. And I think that there might have even been some influence.

In reading your testimony about not being at the table with the IAIS, is that a factor that may play into the domestic category of creating these SIFIs, the non-bank SIFIs because they are more concerned about the international process than they are the domestic process?

Mr. WOODALL. But my job is to try to monitor the whole insurance industry international so I can give my recommendations. There is a statutory provision that every member is supposed to monitor developments in international insurance matters.

Mr. ROSS. They haven't been listening to you, though, have they? That is clear in your testimony.

Mr. WOODALL. Well—

Mr. ROSS. And I—

Mr. WOODALL. I voted with them on AIG.

Mr. ROSS. Right.

Mr. WOODALL. It was a unanimous decision.

Mr. ROSS. But with regard to the designation—

Mr. WOODALL. —right.

Mr. ROSS. Yes, no—

Mr. WOODALL. These were companies that have not had the type of problems with—

Mr. ROSS. Right. There hasn't been a run on life insurance, has there? Are people all of a sudden going to go and cash in their life insurance policies? Because if they are, then our serious consequences for economic structure are way out of line.

Chair Matz, 90 percent of Prudential's balance sheet assets and liabilities are in regulated insurance companies. It engages in no proprietary trading and its limited security of ease lending business was fully collateralized. What would be the basis for your decision that Prudential poses a risk to the financial stability of the United States?

Ms. MATZ. We look at the overall composition of the company's assets and liabilities, their balance sheet and off balance sheet activity. And in their case we looked at, and we were concerned about, their derivatives position.

Mr. ROSS. And you testified, I think earlier to Chairman Luetkemeyer's question, that you relied on staff, the expertise of the staff.

And I think, Mr. Cordray, you went on to say even further that everyone on FSOC has their own expertise and that FSOC members also rely on the expertise of FSOC staff, among others.

This begs the question, who are the other people FSOC is relying on to make these determinations if not the panel? And who are the staff? And what is their expertise in such arenas as insurance? Yes, sir?

Mr. CORDRAY. I think we rely on FSOC staff. We rely on the analysis done by them. There are people loaned from the member agencies of FSOC who do work on this. And then we talk to our own staffs.

But to go back to the point my colleague Mr. Woodall made a moment ago, in terms of insurance companies there seems to be a lot of dissatisfaction here with the designation of MetLife and Prudential.

Mr. ROSS. Yes, I would think so.

Mr. CORDRAY. AIG is also an insurance company—

Mr. ROSS. Yes, but—

Mr. CORDRAY. —designated by this body. And it had tremendous reach—

Mr. ROSS. But they had a diversified portfolio—

Mr. CORDRAY. That is right—

Mr. ROSS. —not unlike Prudential and—

Mr. CORDRAY. And there have also been a number of insurance companies that meet the $50 billion asset threshold that have not been designated. So it is a spectrum here. And it is a judgment that has to be made—

Mr. ROSS. On your FSOC staff, I doubt if you have anybody as eminently qualified as Mr. Woodall. If you are relying on those expert as opposed to the member, Mr. Woodall, then I think there are some problems there.

But let's talk about asset managers. What are we doing here designating asset managers as SIFIs when in fact they are basically brokers? They are not carrying the assets.

And in fact, the impact it will have on mom and pops and retirees because of now what they are going to have to do is pay fees in order to justify why they are brokering with a SIFI when we have not even established that an asset manager should be a SIFI. Yes, sir?

Mr. CORDRAY. We have not designated any asset managers as SIFIs. It is a matter that is—

Mr. ROSS. Oh, you got them in stage two already.

Mr. CORDRAY. —under consideration—

Mr. ROSS. They learned through a Wall Street Journal article.

Don't you think it would be more prudent to allow these asset managers to have the ability to correct whatever may be wrong so that they can save not only the financial system, but also those with whom they serve, instead of waiting until the opportunity where a collapse may occur that you seem to foresee?

Mr. CORDRAY. That is a point of view. And these are the kinds of issues that are under consideration—

Mr. ROSS. If I went to the doctor and knew I had something wrong, I would want to be diagnosed and treated immediately, rather than wait until I was on life support.

I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Washington, Mr. Heck.

Mr. HECK. Thank you, Mr. Chairman.

Mr. Woodall, I think I would like to direct this to you if I may, please. Over the last couple of—I am over here. Over the last couple of years we have heard a lot of witnesses and no small number of the members of this committee indicate publicly and explicitly that receiving a SIFI designation was locking in an unfair competitive advantage.

It seemed to be premised on the idea that lenders would be willing to extend debt to them at a discounted rate. I am having a hard time squaring that circle in the face of the fact that everybody who is a target for designation fights it tooth and nail. And secondly, the action of the S&P recently to downgrade the debt rating of, I think, eight financial institutions.

What is your impression? Is this a good thing, to be SIFI designated? Is it a desirable thing by them? Does it in fact lock in a competitive advantage?

Mr. WOODALL. It is a good thing if they are systemic, and present a systemic risk.

Mr. HECK. Is it a good thing for them?

Mr. WOODALL. But we need to know and they need to know what activities they are doing that make them a significant—

Mr. HECK. Does it give them a competitive advantage?

Mr. WOODALL. Yes, we have talked about that, it can give them a competitive—we don't know, yet.

Mr. HECK. Why do they fight it?

Mr. WOODALL. We don't know yet, because the Fed hasn't come up with their capital standards are.

Mr. HECK. Why would they fight it and why would S&P downgrade them?

Mr. WOODALL. I think they don't know what the future is, they don't know how high their capital requirements are going to be, and they don't know how it will affect them, and they don't know what businesses that they sell that they would have to get rid of.

Mr. HECK. Director Watt, as I pursue this, please remember that I respect you, I wouldn't go quite as far as the gentleman from Texas, but I have affection as both a former colleague and somebody I respect.

Since you have taken over, I have written you two letters, or signed on to two letters. The first had to do with the forced marriage of the Seattle and the Des Moines Federal Home Loan Banks. And I specifically asked that you ensure that the new bank's affordable housing program distribute its funding equitably throughout the combined district.

And that is something that when the bank was just in Seattle, they ensured. And in fact, the Des Moines bank, the new consolidated bank, came out with its nine criteria for distributing funds, and made no mention whatsoever of equitable distribution.

I cannot exaggerate to you the depth of my disappointment on this. I convey it to you. I am not letting go of this, and I am deeply disappointed that there was not more attention paid to this basic principle.

The second letter that I sent to you had to do with concerns about the proposed rule to limit membership, I think 66 of my colleagues got on, the rule came out, we hear rumors that it is not going to be changed. I have signed on to legislation with Mr. Luetkemeyer, Mr. Carney, and Mr. McHenry, to sponsor a bill is to stop it.

Now, in a private meeting I put a question to you, which I now put to you publicly. And I am asking you to respond personally, not necessarily with your agency hat on. You are a long time former member, much respected, of this committee.

Given the forced marriage between Seattle and Des Moines, given the blowback and apparent disagreement about the proposed membership rule, is it not time that the Congress take a look at the basic structure of Federal Home Loan Banks? It has not been touched in 80 years. For all practical purposes, its roots are the same as when they were created.

I believe that in 8 decades, circumstances have evolved and it should be up to us to take a look at that. In fact, the disagreement you and I had privately was, I think it should be up to you or your agency to bring forth ideas of how you might do that.

Your reaction, please, sir?

Mr. WATT. I think there is an ongoing obligation of Congress to look at every aspect of the financial services industry and the housing finance industry. And I think there are important needs that could be looked at in the Federal Home Loan Bank System.

Mr. HECK. Thank you. Comptroller Curry, you are the sole Director of an agency that is not subject to appropriations. How many times have you testified before this committee?

Mr. CURRY. Three times.

Mr. HECK. Over what period of time?

Mr. CURRY. Since my appointment in 2012.

Mr. HECK. Dr. Watt, same question?

Mr. WATT. I come whenever you call me. I have been here one time, since I was—

Mr. HECK. One time? Director Cordray, how many times?

Mr. CORDRAY. I don't know here, but in front of Congress, more than 50 times the Bureau has been called to testify.

Mr. HECK. I think the point is clear. Thank you.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from New Mexico, Mr. Pearce.

Mr. PEARCE. Thank you, Mr. Chairman. I appreciate each one of you being here. Mr. Woodall, you have been, I think, engaged in a discussion at a previous appearance you made in front of this committee, talking about some of the downstream effects of the listing of AIG and Prudential and MetLife. So that is going to have an effect on the insurance market itself, will it not, if I remember from our previous discussion?

Mr. WOODALL. Yes.

Mr. PEARCE. So we in the United States enjoy competitive advantage throughout much of the world. And coming from the business world, specifically repairing oil wells, down hole—which is filled with liability, we utilize that insurance market to great advantage, to allow us to create jobs, to do a better competitive effort than some of our friends overseas could do.

And so will there be downstream effects from any actions you all take regarding the too-big-to-fail? Will there be effects in the insurance market?

Mr. WOODALL. Well, yes. You used terminology that—obviously, if someone has increased regulatory expenses, it is going to affect how they operate in the market.

Mr. PEARCE. So there is a possible threat from what you all do to the market?

Mr. Massad, have you all discussed that in the FSOC meetings?

Mr. MASSAD. Congressman, I wouldn't characterize it that way. I would point out for example, that what we do can protect people. When we consider AIG, for example, this government had to commit $182 billion to prevent the collapse of that company, which would have probably taken us into a worse Great Depression than what we had in the 1930's. Fortunately, we were able to get all that money back.

Mr. PEARCE. What about MetLife and Prudential?

Mr. MASSAD. Congressman, with all due respect, I was not there for the Prudential designation. With respect to MetLife, that is a matter under litigation, so I don't think it is appropriate to comment on the reasons for it.

Mr. PEARCE. Ms. White, would you have a comment on that? In other words, you all, as FSOC, your underlying call is to prevent excessive risk to the U.S. financial system. And what I am saying is that there are certain financial risks to what you are doing, to the actions you all are taking.

So Ms. White, did you all discuss the potential downside of what you are doing here and how it might affect the market? And now you have referred to the guy who made his living regulating insurance and living in the insurance. And sometimes staff have not had that on the ground experience.

So regardless of what anybody else says, do you all sit quietly behind the doors and say, hey, we ought to really take a close look at what we are doing?

Ms. WHITE. I think we have to carry out the mandate we were given, which is basically to identify and address systemic risks to the financial system, the financial stability of the financial system.

Mr. PEARCE. So you don't think that you as an agency could be the systemic risk yourself?

Ms. WHITE. You want to consider all factors. And certainly when we do our rulemakings at the SEC, we directly consider all of the impacts. I think we do consider and discuss factors, a wide range in FSOC, too. But our primary responsibility is to carry out the mandate we were given to—

Mr. PEARCE. The mandate is to watch—excuse me, I keep shifting back and forth. The mandate is to watch for systemic risk, is that right?

Ms. WHITE. It is to identify and address systemic risk to the overall financial system.

Mr. PEARCE. And so I am saying that if you all—according to Mr. Woodall's discussion back some time, and kind of reiterating now, you all could be the systemic risk that you are trying to avoid, if you are not very careful, because this insurance market is extraordinarily thin.

If you are watching—I don't mean to be rowing in other stuff—but if you are watching people bail out of the insurance market in healthcare right now, you understand what I am talking about.

We have disrupted an entire insurance market, and before you all do something that causes the same evacuation out of the insurance, just remember the poor saps out there in the field like myself who are just trying to buy insurance off the open market, to where we could do our business.

And it could be that you all are the problem which causes that market to disappear. And that is my point. I would hope that you all would have more thorough discussions about the problem that you all represent instead of the systemic risk that maybe you ought to be identifying somewhere else.

Thank you, Mr. Chairman, I yield back.

Chairman HENSARLING. The gentleman yields back. The Chair wishes to alert all Members that there is currently one procedural vote on the Floor. There are 11 minutes remaining in that vote.

I will recognize the gentlelady from Missouri. Members may want to go vote and come back. And then after the gentlelady from Missouri, we will recess briefly for the vote. The gentlelady from Missouri is recognized.

Mrs. WAGNER. Thank you, Mr. Chairman. And thank you all for being here. I would like to quickly associate myself with my colleague across the aisle from Georgia, Mr. Scott, about this very misguided Administration's rule-laying by the Department of Labor, on fiduciary issues. I would encourage you all to speak to the President and his team on this issue, too. He did not seem interested in my concerns last night at the Christmas party.

I am particularly interested in knowing the role that the international forum, known as the Financial Stability Board, has played with regard to decisions about domestic matters made by FSOC. Due to the non-transparent nature in which FSOC conducts its business, it can cause one to question, I think, whether our U.S. regulators are really fighting on behalf of the interests of the United States of America when they are at the international negotiating table, or whether they are simply letting international counterparts make important decisions for us.

Mr. Woodall, in your dissent to the Prudential SIFI designation, you made the point that the international and domestic designation processes are not entirely separate and distinct. Specifically, sir, you noted that an unnamed U.S. national authority agreed to the international designation of Prudential before the company's determination before FSOC. Could you please be specific and elaborate, who is that? The national authority?

Mr. WOODALL. Yes, the national authority. Well, there are three at FSB, there are three national authorities: Treasury; the Fed; and the FCC.

Mrs. WAGNER. Yes. And who is the unnamed authority that agreed to the international designation of Prudential before the company's hearing and final determination before FSOC?

Mr. WOODALL. That is hard to say. As far as I know, actually, before the hearing at Prudential, the Treasury notified Prudential that they had been designated as a global SIFI.

Mrs. WAGNER. Before their hearing, before their final determination before FSOC, Treasury—if I understand your testimony—let them know that they had been designated.

Mr. WOODALL. That is my understanding.

Mrs. WAGNER. This seems questionable. As you stated, the U.S. representatives on the FSB—Treasury, the Fed, and the FCC—are not insurance regulators, as has been pointed out by so many of my colleagues. Nor are they necessarily Phi Beta Kappas from Kentucky.

Meanwhile, the FSB's membership is dominated by banking regulators who know little about the insurance industry. Does it concern you that those regulators are the only U.S. representatives in the room when decisions are made about insurance issues, sir?

Mr. WOODALL. Yes. I think the CFTC and the FDIC should be in the room at the meetings at the FSB. And I think insurance regulators should be in the room if they are making decisions that are going to affect the businesses that they regulate.

Mrs. WAGNER. Thank you. Given the sequencing of FSB designations, and then later FSOC's SIFI designations, how can U.S.-based insurers be confident that their designations are the result of a domestic decision, rather than an international process that isn't accountable to the U.S. policymakers like us?

Mr. WOODALL. As I said, they are technically separate things, but they are not—

Mrs. WAGNER. They are not. They are not accountable to U.S. policymakers. Thank you. Can you describe what attention or consideration FSOC gives to designations by the FSB?

Mr. WOODALL. No direct—it is not mentioned in the discussions, because we try to base it on what Dodd-Frank says.

Mrs. WAGNER. Do you believe that your colleagues would feel comfortable disagreeing with a decision, or challenging a decision made by the Fed, the Treasury, and the FCC at the Financial Stability's Board?

Mr. WOODALL. Of course, they are still just three votes on the board. The board, the Financial Stability Board is not an organization that this Congress created by a treaty, or any other statutory thing. It is kind of an ad hoc group.

Mrs. WAGNER. Absolutely, it is an ad hoc group. Do you believe—

Mr. WOODALL. It is really self-appointed.

Mrs. WAGNER. Do you believe that your colleagues would vote to de-designate any of the insurance companies, if such companies were still designated by the FSB?

Mr. WOODALL. I would hope so.

Mrs. WAGNER. One last question. Since everyone has said that they—I don't have much time left—rely on FSOC's staff for info, is there a memo or analysis that is distributed to members before a vote? Who writes this? Is it Treasury? Is it the Fed? Would you allow the committee to view any of these documents?

Mr. WOODALL. It goes through a committee called the Non-Banks Designation Committee. It goes to the secretariat, which is within Treasury. And you are looking at 600, 700 pages sometimes in these memos. They are more than memos. It is quite extensive with a lot of good work done by the top economists at the Fed and other agencies.

Mrs. WAGNER. Thank you, sir.

Chairman HENSARLING. The time of the gentlelady has expired. The committee will now recess for the vote pending on the House Floor. The Chair expects the recess to last approximately 10 minutes. The committee will reconvene immediately after the vote. The committee stands in recess.

[recess]

Chairman HENSARLING. Members will take their seats.

The Chair now recognizes the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman.

And Mr. Woodall, since you have been the topic of much conversation as a Phi Beta Kappa from Kentucky, as a fellow Kentuckian, I am going to try to leave you alone for the most part today.

Let me start with some of our bank regulators, our prudential regulators, and note that at a macro prudential level, FSOC and our banking regulators have participated in international agreements with the Financial Stability Board, Basel, and other forums. And the main difference between U.S. requirements and those promulgated internationally is that it seems that our domestic standards are more stringent than our foreign counterparts.

So just a few examples: A capital surcharge on global financial firms nearly doubled the international standard; supplemental leverage ratio that is double adopted—that adopted internationally; a liquidity coverage ratio that is more restricted than the international standard, and arbitrarily punishes certain products like municipal securities; a total loss absorbing capital rule that goes beyond international standards; OTC margin requirements that are considerably more punitive than international standards.

So this question is for Ms. Matz, Mr. Watt, Mr. Gruenberg, Mr. Cordray, and Mr. Curry. I assume that you all agree that these prudential rules and other reforms have improved safety and soundness. And if you agree with that general proposition, raise your hand.

So, all of you agree that these new prudential rules enhance safety and soundness. A follow-up question: do you believe that the benefits of these new prudential rules outweigh potentially the cost to international competitiveness, given that we have higher standards than that international—okay. So, most of you agree with that.

When combined with Volcker, financial institutions seem to be making a couple of changes in the regulations and producing a couple of results. One is that there is a migration of activities out of heavily regulated banks and into much less regulated non-bank financial firms, the so-called shadow banking system. And I want you to address that.

But also there is much talk about illiquidity in the markets, institutions dropping certain products and services, pulling back from market-making functions critical to investors, extension of credit affecting various fixed income asset classes in different ways.

So my question to some of our market regulators, Mr. Massad, Chair White, is that the FSOC annual report acknowledges that there are changes in terms of reduced liquidity in the capital markets. The Office of Financial Research is corroborating this.

Certainly, there are other indicators. The Center for Financial Stability found that market liquidity has declined by 46 percent. And as you all have already noted, and Mr. Curry has noted, this potential lack of liquidity that is resulting from regulation could mean that financial markets have less capacity to deal with shocks, and would more likely seize up in a panic just as they did in the 2008 financial crisis.

So, given that our bank regulators are making the case to FSOC that this is good for financial stability, and yet we see a liquidity problem developing, from your perspective, what do you make of all this?

Ms. WHITE. I talked a little bit about this, I think, at my last hearing. It is a concern for all of us in terms of significant reduction in liquidity. Obviously, there are rules that have very beneficial purposes that may or may not be causing that.

We do analyses to see whether Volcker, for example. We will report quarterly to this committee. We have not determined that the Volcker Rule is having a negative impact on liquidity.

When we talk about shadow banking, I think we have to be careful too. That term covers a broad swathe. A lot of the things that fit under that category are heavily regulated by the capital markets regulators.

But I think you know the bottom line is that we are all, and should be, very concerned about impacts on the—

Mr. BARR. I think we should look at regulation as a cause of financial instability as a result of the lack of liquidity that we are seeing developing in the marketplace. That is something that FSOC should be paying attention to and revisiting some of these regulations to the extent that they do compromise financial stability.

Finally, let me just go back to Mr. Watt really quickly.

The GSEs are exempt from Mr. Cordray's QM rule. They are exempt from capital and liquidity rules that I am talking about. Agency MBS's are carved out of the Volcker Rule, and agency MBS's are some of the few cash and cash-like equivalents that banks need to hold to comply with these capital and liquidity rules.

My question to you in my limited remaining amount of time is, why are these standards good for the private sector, but not for GSEs under your oversight? And why have a double standard if, as you signaled by raising your hand, these capital requirements are important for financial stability? Shouldn't it be important for the GSEs as well?

Mr. WATT. If they were not in conservatorship, I think you would be absolutely right.

Mr. BARR. Why should we continue to have the risk on the taxpayer?

Mr. WATT. Because we continue in conservatorship because the Legislative Branch has not acted on GSE reform.

Mr. BARR. I think we should look at that double standard.

And I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Delaware, Mr. Carney.

Mr. CARNEY. Thank you, Mr. Chairman. And thank you to the ranking member and to everyone who is here today. This is the biggest panel that I can remember that we have had here before.

Part of our responsibility, I think, for today's hearing is oversight of the FSOC. And as I understand it—I was not here when Dodd-Frank was passed—the primary responsibility of the FSOC was to identify emerging systemic risks. And I would just like to hear from many of you what you see out there as those emerging risks. And can you share those with us?

Why don't we start with Mr. Gruenberg and go to Comptroller Curry in terms of your responsibility as part of the FSOC. What are the emerging risks? What are the systemic vulnerabilities that you are seeing out there?

Mr. GRUENBERG. The annual FSOC report outlines a series of systemic risks to focus on, interestingly, in this report, the leaderess—that it cites is cybersecurity and the potential consequence, vulnerabilities relating to cybersecurity could have for the functioning of the financial system.

And that certainly has been a focus of discussion and attention by the FSOC. And I frankly think for each of our agencies individually.

I would also reference—

Mr. CARNEY. Is there anything that we should be doing or looking at with respect to providing you with the necessary tools? We are going to be talking about a data breach bill later today.

Mr. GRUENBERG. I note the Congress is considering legislation to facilitate information sharing, which I think is one of the critical issues in terms of being prepared to deal with a cyber incident.

So I think there is a significant role for the Congress, and certainly for the—all the agencies at this panel working among the regulatory agencies, as well as with the law enforcement and national security communities. It is really going to require—

Mr. CARNEY. The classified briefings that we have had are pretty scary, frankly. And the attacks are coming on a regular basis, on a daily basis.

And frankly, it feels like to me that we are fortunate that we haven't had a more significant attack than what we have had. And I know that institutions are dealing with this on a regular basis.

Comptroller Curry, what would you say in terms of emerging risks or existing vulnerabilities?

Mr. CURRY. I would agree completely with Chairman Gruenberg. Cybersecurity is a number one concern, both as Comptroller and as a member of the FSOC.

I think the ramifications of a successful attack on the core systems of financial institutions, regardless of their size, could really undermine public confidence in our entire banking system. And that is really why it is imperative from a regulatory standpoint to make sure all of our banks, from the smallest to the largest, are prepared to repel attacks and are in a position to respond as quickly as possible in the event of a successful intrusion.

The chairman also mentioned, and it is in the FSOC annual report, increased risk-taking in a low yield environment. We are very concerned about the decisions that the financial institutions we supervise are taking today, whether it is to go along or to get into activities that they are either unfamiliar with or not prepared to deal with the risks that are inherent in those activities. We think that is a potential emerging risk for individual institutions and for the system.

Mr. CARNEY. Thank you.

Chair White, is there anything you would like to add?

Ms. WHITE. No, I think you can't emphasize enough the cyber risk. It is not a coincidence that it is listed first in the emerging risks in the FSOC annual report.

Mr. CARNEY. Thank you.

Director Watt, you and I have had some conversations about the last subject you talked to Mr. Barr about with respect to the GSEs, and I know it has been your view that you are waiting on Congress to act.

What vulnerabilities exist there? Increasingly, the taxpayer or Freddie and Fannie are guaranteeing those mortgage-backed securities. What is your view of the sense of urgency around that issue?

Mr. WATT. I think we been in conservatorship, Fannie and Freddie, for 8 years. It is the longest conservatorship that has ever occurred under government control. While the risk of the work that we are doing is much, much less now than it was at the onset of the meltdown, staying in conservatorship is just not sustainable.

You have a high risk of losing the most qualified people to the private sector. I could keep going on.

Mr. CARNEY. We should do something. We should act.

Mr. WATT. You should act, yes.

Mr. CARNEY. Thank you, Mr. Chairman. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Pennsylvania, Mr. Rothfus.

Mr. ROTHFUS. Thank you, Mr. Chairman. Mr. Woodall, your criticism of the MetLife SIFI designation process is a matter of record and has been discussed at the hearing today. Your well-founded concerns are shared by many of us, and ultimately we should all ask ourselves whether it is wise for people with little or no experience in a given industry to be given the power to make significant consequential decisions such as SIFI designation.

There is a broader question as well that I was hoping to get your thoughts on. Many of us are concerned that American regulators are ceding responsibility to the FSB, which is composed of central banks, finance ministers, and regulators from around the world.

Given our shared misgivings about, for instance, FSOC members without insurance experience deciding to designate an American insurer, shouldn't we also be concerned about letting foreign regulators who lack experience in the American financial services industry, and who act in the best interest of their respective countries, take the lead in regulating our financial firms?

Mr. WOODALL. Well, that is the point that has been discussed quite a bit, and a lot of it goes to the fact that the European insurers have a lot different background. They have a different accounting system, their products aren't the same. Now, they are pretty well united with their solvency 2 regulation, which goes into effect next year.

And they are working on equivalencies as to whether we are equivalent. There has been some temporarily equivalencies given. If we don't get equivalency, it could increase the cost of our companies doing business in EU countries tremendously.

Mr. ROTHFUS. One of FSOC's most basic authorities under Section 112 of Dodd-Frank is to make recommendations to the Fed concerning which heightened prudential standards should apply to non-bank financial companies. Yet to date, the FSOC has not done so.

It would appear that FSOC is putting the cart before the horse, designating companies for heightened supervision but making no recommendations for what those heightened requirements must be.

The basic principle of regulation is that the benefits of imposing a regulation should outweigh the costs associated with doing so. Designating a firm for heightened supervision is not without costs. It is a serious matter that impacts firm behavior and may have even broader repercussions for the financial services industry, as well as consumers.

Chair White, how is it possible to ascertain the costs and benefits of designating an insurance firm as a SIFI if the Fed has not yet prescribed the heightened prudential standards that will apply to designated firms?

Ms. WHITE. Again, I go back to the primary mandate of FSOC, which is to identify systemically important financial institutions that can impact the financial stability of the U.S. financial system.

I do think the Fed has actually adopted, if I am right, but certainly it put out for notice and comment, standards with respect to GECC. So that is there now. But I certainly understand the point that you are making in terms of if you don't know what the standards are that are going to be applied, it is obviously part of your analysis that you can't do.

I don't think we are obligated to do it. And indeed, I think we are obligated to deal with the issue of systemically important institutions in the first instance, and not wait for that action.

Mr. ROTHFUS. It is a good idea, wouldn't you agree, that a basic principle of regulation is that the benefits of proposing a regulation should outweigh the costs associated with doing so?

Ms. WHITE. Again, I think the premise of the responsibilities of FSOC is what a tremendous cost the financial crisis was, and to try to prevent that. One of the tools that FSOC has is the systemic designation powers.

However, speaking for myself, we certainly want to act on full information, including that.

Mr. ROTHFUS. Director Watt, is the FSOC evaluating the Fed's historically accommodative monetary policy stance to see whether that policy has led to excessive risk-taking in the financial system?

Mr. WATT. Not directly. We are always evaluating every decision that all of these regulators make. But we don't oversee the Fed.

Mr. ROTHFUS. Do the Fed's destabilizing monetary policies get a pass from the FSOC because the Fed Chair sits on the FSOC?

Mr. WATT. That assumes that they are destabilizing. I wouldn't assume that position or conclusion.

Mr. ROTHFUS. So the Fed—or the FSOC isn't taking a look at the Fed's balance sheet, for example, that it has gone from $800 billion to $4.5 trillion over the—

Mr. WATT. That is not in the jurisdiction of FSOC.

Mr. ROTHFUS. Thank you, Mr. Chairman. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Minnesota, Mr. Ellison.

Mr. ELLISON. Thank you, Mr. Chairman, and Ranking Member Waters.

I want to thank each of the witnesses and your staffs for your comprehensive and insightful written testimonies. I also want to thank you for your service on the Financial Stability Oversight Counsel. We have all learned the painful reality that markets do not regulate themselves, and a nation as powerful as ours must invest in regulation and identify in response to emerging threats to our stability.

So your report, 150 pages, details the Council's unprecedented progress to protect the financial system from risk and to prevent another economic disaster from happening, which I remember very well. I wish everyone running for President would read it. Maybe then we could have folks talk about how to really understand how to protect our economy and be successful in that effort.

So my first question is to Comptroller Curry. It has been a while since you have been before the committee. I want to welcome you back. And since you are here, I want to ask you again about a topic that you and I have spoken about in the past, and that is the issue of Somali remittances.

Are financial institutions regulated by the OCC closing accounts of money services businesses serving Somalia due to compliance costs, reputational risk, inability to cover the cost, lack of clarion exams, or for other reasons?

Mr. CURRY. Congressman, as we discussed, I think there are a variety of reasons why individual institutions are making determinations about what their risk tolerance is under the Bank Secrecy Act and the anti-money laundering statutes.

In terms of regulatory clarity, we have tried to make clear what our expectations are. We did put out in 2014 additional guidance on dealing with money services businesses, but ultimately it is the decision of the individual institution whether or not to do business with an individual business or individual.

Mr. ELLISON. I just want you to know the Somali parliament—I have had a chance to talk with some of them. They are passing an anti-money laundering, antiterrorist financing law. They haven't passed it yet, but they are working on it. That is coming up. They opened up their embassy here in the United States, and I believe that the more stable that country is, the less susceptible it will be for terrorists to come and set up shop and try to operate out of there.

Mr. CURRY. I think those are very good improvements. As we discussed, it is important that there be a strong local banking system and the regulatory system overseeing its compliance with important laws like the BSA.

Mr. ELLISON. Yes. Thank you.

Mr. Watt, it's always a pleasure to see you. I'm very proud of you and the work that you do. Welcome back to the committee. It must be weird to be on that side of the divide.

But anyway, I just want to say to you, the report calls for a comprehensive litigation legislation to address the conservatorship of Fannie Mae and Freddie Mac. It also urges Congress to clarify the future role of the Federal and State Governments in mortgage markets. While Congress has not acted on any particular proposal regarding the GSEs, I am interested in what your current policies are doing to improve credit access to African-American and Latino borrowers.

I have a chart up, which I will direct your attention to. And as shown by the chart, we know that the majority of new households are going to be African-American, Latino, Pacific and Asian-Pacific American. Yet, they seem nearly shut out of the mortgage market now.

GSE loans to African-American borrowers in 2013 were about 2.2 percent, and GSE loans to Hispanic borrowers in 2013 were about 5.8 percent, both low. What policies can GSEs implement post-conservatorship to improve access to credit for African-American, Latino, and Native American borrowers that Fannie and Freddie cannot implement now?

Mr. WATT. You are asking about post conservatorship or—

Mr. ELLISON. What can they do—what is it that might be done later that can't be done now? And I am basically asking, how do we make progress on this?

Mr. WATT. Well, a lot of what can be done after conservatorship depends on how GSE reform is done—

Mr. ELLISON. Right.

Mr. WATT. —and what the rules of the road going forward are.

Part of the challenge of being in conservatorship is one of the things I have found to be true is that lenders price uncertainty. And right now they don't know what the future is. So as prices go up, there is a price to uncertainty of what the future holds in this area.

So, I just—there are a number of things that need to be done to address this because we need the availability of capital for people to be either homeowners or affordable renters.

Mr. ELLISON. We will follow up—

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Arizona, Mr. Schweikert.

Mr. SCHWEIKERT. Thank you, Mr. Chairman.

Just first conceptually, because it has been sort of floated around a couple of times, in many ways when I read the articles about what you are all doing it is a discussion of, are we fighting the last war, and the concentration of risk of unintended consequences.

We have our Section 113, the list of criteria. Are we going to wake up tomorrow and find out that the shadow on the horizon, the black swan was something that because of the concentration of the way you look at the world you completely miss?

But there have been a couple bits of testimony here that I need to drive into because I am a little disturbed and concerned about some of the things I heard. The gentleman from Florida, Mr. Ross, was asking some questions about insurance. And a comment was made by Ms. Matz—you actually stated that on Prudential, one of the reasons they made your list, shall we say, is their derivatives book.

Now is that because they didn't have enough hedging of their interest exposure? I don't know if they were doing duration exposure, but their interest exposure. And are you saying they had a derivatives book and because they were actually insuring their interest—exposure that forced them onto your list? What do you mean when you said the derivatives book?

Ms. MATZ. They had such a large exposure that the failure of that institution or financial—

Mr. SCHWEIKERT. When you say that institution?

Ms. MATZ. Of Prudential.

Mr. SCHWEIKERT. Okay. So they are buying an additional hedge to protect their interest rate exposure so if that moves against their 100 percent coverage. Explain to me how that would work.

Ms. MATZ. First of all, the derivatives position is just one position. But if they are so interwoven or so interconnected with other financial institutions that if they failed—

Mr. SCHWEIKERT. No, no, no, no. Not—if they—they are not—

Chairman HENSARLING. I'm sorry. Will the gentleman suspend?

I wish to alert Members that regrettably there is yet another procedural vote on the Floor. I think we are drawing near to the end of the hearing so if Members who have yet to ask questions wish to go vote now and return, I think we can keep this thing going, except for Mr. Tipton, who is next. So if Members wish to go vote and return quickly.

I am sorry to interrupt the gentleman. The gentleman from Arizona is recognized again.

Mr. SCHWEIKERT. Thank you, Mr. Chairman.

Look, we are talking past each other because you know everything I know about why your derivatives contracts to protect your interest rate exposure, that would be something you would find joyful, not put them into a designation.

Also, in looking over parts of the reports about Prudential, okay, so their repo contracts are 100 percent offset and collateralized. I am just trying to figure out where you found exposure.

Ms. MATZ. It is all exposure. What is the assumption that—

Mr. SCHWEIKERT. If you are 100 percent covered and you have also covered your interest rate risk, the exposure is what?

Ms. MATZ. The assumption that is made in making our determination is that there is material distress at the designated institution. So we are starting from the assumption—

Mr. SCHWEIKERT. So I have an institution. It is 100 percent covered. Plus, it has also done additional financial products insurance to cover markets moving against them.

Ms. MATZ. But we are operating from the assumption that there is material distress at that institution. So, if there is material distress, that they can cover the outstanding debt that they have or the loans that they have.

Mr. SCHWEIKERT. But they are contract loans. The insurance products that they are offering are all under contract. So they have the ability to say, according to our contract you may be making a claim for this, but under the contract we have the ability to pay as the contract is designated. Because—

Ms. MATZ. Unless they are in material distress.

Mr. SCHWEIKERT. Okay. I will give this one to you in writing because we are talking past each other because that makes absolutely no sense.

When I look at your Section 113 tests, and I go up and down this, is it the last one? Are there risks that the Council may deem appropriate? When I look at this list, particularly on an insurer like this which is 100 percent covered and then hedged their coverage, I am trying to find out on this list where do you find the exposures?

Ms. MATZ. Interconnectedness. It is their interconnectedness with the other institutions. And the assumption that a financial institution is suffering material distress, I think is—

Mr. SCHWEIKERT. I wish I had you in grad school because there would been some fascinating questions.

All right. Last bit in my last 20 seconds, Mr. Curry, you are the only one in the panel I have heard actually touch on something that made me very happy. And that was sort of the unknown, the reality that future financial markets are moving Silicon Valley bank—or excuse me, Silicon Valley centric, the new ways people are going to borrow money, buying credit, invest, move around.

Isn't that, though, actually much safer and much more robust than a concentrated banking system because the way capital is acquired is much more distributed model?

Mr. CURRY. Again, from the FSOC's standpoint we have identified as one of our emerging risks the financial innovation and migration of activities. So it is an area that we are discussing. And I think we will devote additional attention to those issues.

As the Comptroller, we are very interested in this because of the impact of financial technology and innovation on the delivery of banking services—

Mr. SCHWEIKERT. Okay. And I am going to give you something in writing—I know we are way over time.

Mr. CURRY. Sure.

Mr. SCHWEIKERT. But I beg of you, if it is creating diffused risk, if we are seeing sort of a distributive model, please do not beat up innovation. We desperately need it—

Mr. CURRY. Actually, I am calling for fostering responsible innovation.

Mr. SCHWEIKERT. And with that, I have to yield back. Thank you.

Mr. GARRETT [presiding]. The gentleman yields back from a very salient point, which I think he will agree with the chairman that just citing interconnectedness is not enough of a criteria because—and no one else from the panel I see was able to answer your question as well.

My daughter's former lemonade stand is also interconnected if you go through the whole realm. So I think there has to be more substance to it than that. But with that, I will now yield to Mr. Tipton for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman. And I thank the witnesses for taking the time to be here. We have a large group, and I would like to be able to echo some of the comments that were made by Mr. Lucas, Mr. Stivers, in regards to community banks, something that is critical for rural America, and particularly in my district.

You have had to raise your hand, simply because of the size of the panel, several times here. But I would like to be able to just get a sense of your feeling on the panel, who is concerned about the challenges faced by America's community banks and financial institutions in these small communities.

Everyone has raised their hand. In response to Mr. Stivers, you have made comments that—how much time does the Council actually spend in regards to community banks? And the answers were some, or it is going to be at the staff level. And I would maybe like to start with Chair Gruenberg, and maybe Comptroller Curry. If it is actually something—this is in your wheelhouse, why isn't more time spent on community banks?

Mr. CURRY. It actually is. The OCC supervises approximately 1,700 banks. The majority of them are community banks. A major focus of my tenure as Comptroller is to look at and make sure we have a strong, viable community banking sector.

I think we are very fortunate to have a diverse banking system in the United States. We have looked at the burdens particularly facing community banks. We have identified some areas where we think we can make a difference, whether it is call-report reform or capital reform.

At the OCC, we are really looking at how can we reduce the cost structure. So we put out a White Paper a little over a year ago, encouraging from a regulatory standpoint, banks, particularly smaller banks in rural communities, to collaborate, whether it is a joint venture, sharing employees, working on participation, so that they can continue to be viable entities and serve their communities.

Mr. TIPTON. If I may, let's talk a little bit about—when you are talking about a viable, vibrant baking system, you are aware that right now, approximately one-third of the counties in the entire United States are served by only one community bank. Do you recognize that?

Mr. CURRY. Yes.

Mr. TIPTON. How vibrant, how competitive is that?

Mr. CURRY. What we are trying to do is really make sure there is a balance between appropriate supervisory standards in how we supervise those institutions, so that banks can continue to lend and be leaders in their communities going forward.

Mr. TIPTON. You talked a little bit about collaboration, for the banks to be able to come together, to be able to share employees. What type of collaboration is going on in the FSOC to be able to identify redundant regulations that are overlapping, and requiring small community banks to be able to answer to several masters, if you will, and driving up those costs, which were increasing the cost for loans, for communities, inhibiting those banks' ability to be able to survive, driving, actually consolidation, or actually failure of some of these small banks?

Mr. CURRY. I think the primary area where we are addressing that for community banks is at the Federal Financial Institutions Examination Council, which State and Federal bank and credit union regulators are part of. That is really part of the mission of the FFIEC.

Mr. TIPTON. Just as a little bit more of a follow up on this, as we reviewed the FSOC minutes, there is never a mention of small banks in the minutes. So I am pleased to hear that you are actually putting out some comments and some White Papers. I think the question that our community banks would like to have answered is, when are they actually going to get some relief, rather than talk?

Mr. GRUENBERG. If I may say, Congressman, I do think community banks have been a focus of enormous attention by the bank regulators who have responsibility for it.

Mr. TIPTON. That is what really disturbs the community banks.

Mr. GRUENBERG. As you know, community banks play a critical role in the financial system. We have shown at FDIC studies that community banks account today for about 14 percent of the banking assets, and hold about 45 percent of all the loans to small businesses and farms by all banks in the United States. So the role they play is really quite critical.

I do think that is to be distinguished from whether they pose, in and of themselves, a threat to the financial system that would warrant the FSOC's attention, or they are critical to the financial system certainly can be impacted significantly by systemic risk, as we saw in this recent crisis. They themselves are not a source of systemic risk. And where they are the focus, are by the bank regulatory agencies.

And we, as you know, have been conducting a review, as we are required by law, of the regulations we have imposed over the past 10 years, have held outreach meetings across the country, are seeking public comment. And I am hopeful we will be able to come out with a series of regulatory measures that will be helpful in terms of reducing the cost of regulatory—

Mr. TIPTON. I hope you can, because simply, as Mr. Schweikert was pointing out when we were talking about the connectivity that is going on, while you may say—and are accurate, they are not going to be systemically important to the overall economy of the United States.

They are certainly feeling the impacts of those broader rules, regulations, through loan participation, whatever it happens to be, that is cascading down and inhibiting their ability to be able to address the very people that you cite—and I agree with you are very important—are small businesses and our agricultural communities.

Thank you, Mr. Chairman. I yield back.

Mr. GARRETT. The gentleman yields back. Mr. Poliquin is recognized now for 5 minutes.

Mr. POLIQUIN. Thank you, Mr. Chairman. I appreciate it very much. I wish everybody a merry, merry Christmas, and a happy holiday season. Thank you all very much for being here. It is very important for us here on the committee, and for our fellow Americans.

Chair Matz, I would like to ask you a couple of questions, if I may. Are you familiar with the December 14th announcement by Chair White dealing with the new regulatory process, dealing with asset managers? Are you familiar with that?

Ms. MATZ. I have read about it, but I am not—

Mr. POLIQUIN. Okay. Can you remember what the content of that was, ma'am? Okay, let me help you out. Could you speak a little bit closer to the microphone? My ears aren't what they used to be.

In that, Chair White mentioned that going forward and regulating the asset managed, she would be looking at liquidity risk, leverage, as per use of derivatives, stress testing, and things of that nature. Does that ring a bell?

Ms. MATZ. Pardon me?

Mr. POLIQUIN. Does that ring a bell?

Ms. MATZ. Yes.

Mr. POLIQUIN. Okay, good. And can you think of anything that the SEC is not doing to regulate asset management, so good at doing this for 75 years. Can you think of anything that she has left out in the new way that she is proposing to raise asset managers?

Ms. MATZ. As I said, I haven't reviewed it. I am not intimately familiar with it, but I have great confidence in Chair White.

Mr. POLIQUIN. Okay, good. I am going to take that as that you don't have anything to add with respect to her job regulating asset managers. Are you familiar, ma'am, with the FSOC's decision to review asset managers' products and activities?

Ms. MATZ. Yes.

Mr. POLIQUIN. You are? Okay, because you voted on that, it was unanimous back in December of last year, I believe. Are you also familiar with Section 113 of the Dodd-Frank Act?

Ms. MATZ. Yes.

Mr. POLIQUIN. Good, okay. There are 11 different parts of that Section 113, Ms. Matz. One of them, which deals with what you folks are responsible for in weighing whether or not an asset manager, mutual fund, pension fund managers, so forth and so on, should be so designated as SIFI.

One of them, "The degree to which the company is already regulated by one or more primary financial regulatory agencies—"

The SEC is one of those primary regulatory agencies, right, from asset managers? Okay. So my question to you, Ms. Matz, is what in the world is FSOC even doing in this business? We have a regulator here that has been doing this for 75 years.

You agreed there was nothing you can think of to add to her job. But at the same time, you voted along with everybody else to consider designating asset managers as SIFIs. So what am I getting wrong here?

Ms. MATZ. We didn't vote to consider—

Mr. POLIQUIN. Speak up, please. My ears are bad.

Ms. MATZ. We didn't vote to consider asset managers as SIFIs. We voted to consider to have the staff look at the activities of the asset managers, to determine whether—

Mr. POLIQUIN. That is legal speak. That is the same thing. If you are asking the staff, and you folks are going to decide whether or not you are going to designate an asset manager as a SIFI, and looking at the criteria thereof, that is the same thing, isn't it?

Ms. MATZ. We have not made any determination.

Mr. POLIQUIN. I know you haven't. Why are you even in this business?

Ms. MATZ. Because our mandate is to look at those institutions that could pose a threat to the financial stability of the United States.

Mr. POLIQUIN. She is already doing that. The SEC is already doing that. I just read you the criteria, ma'am. She is dealing with liquidity risk, and leverages, respect to derivatives, and stress testing, and everything else. And you couldn't add anything else to the parade. So my question is, why don't you folks move on? You have other good things to do. Why should you get involved in this space at all?

Ms. MATZ. Well, two things. One is that we have not made that determination yet, and also that the SEC is not looking at the threat to the financial stability of the United States. They are looking at the narrow securities market.

Mr. POLIQUIN. Okay. Let me—no, I am asking you, ma'am. Ms. Matz, I am asking you. Thank you.

All right. Let me ask you this question. Since you folks clearly have gone down this path or are going down this path to consider whether or not you should designate an asset manager as a SIFI, you must have some analysis which concludes that what the SEC doing is not full. Do you have that analysis for me or for my office?

Ms. MATZ. Their mandate isn't to look at the financial stability of the—

Mr. POLIQUIN. Do you have the analysis that you use, Ms. Matz, and everybody else used to so determine that the SEC is not fulfilling their job?

Ms. MATZ. We—

Mr. POLIQUIN. It does dictate advice—

Ms. MATZ. We did not come to that conclusion, that the SEC is not fulfilling its job.

Mr. POLIQUIN. Okay. Well, you had to make the decision based on what?

Ms. MATZ. Based on our mandate.

Mr. POLIQUIN. Let's move on a little bit. Are you familiar with a study done by Mr. Douglas Holtz-Eakin, the former Director of the nonpartisan CBO?

Ms. MATZ. The study on?

Mr. POLIQUIN. All right. You are probably not. It was done in 2014. Let me just give you the ultimate conclusion. It basically says the following: If an asset manager that represents no systemic risk to the markets or to the economy, if they are so designated as a SIFI, then the costs will go up. And we have discussed this today. The product offerings will go down. And the long-term rate of return of savers for their retirement and putting their kids through college will likely go down by 25 percent.

Now also in Section 113 of Dodd-Frank, there are other risks that you should consider. Do you folks consider the risk to the small investor such as a nurse in Lewiston, Maine, or a logger in Dover-Foxcroft, Maine, who are trying to save money for their retirement or for their kids' education, are you considering the risk to them if the asset managers that run their money are so designated as SIFI and they get dinged by about 25 percent in their rate of return? Do you consider that?

Ms. MATZ. We have not made any—even been given any potential recommendations. So we have not considered any aspect of—

Mr. POLIQUIN. Okay. So when you factor in the economic cost to the people we are supposed to help in this country in making these decisions, whether or not an asset manager should be so designated a SIFI.

Ms. MATZ. We are not even at that point of making that determination.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Arkansas, Mr. Hill.

Mr. HILL. Thank you, Mr. Chairman.

And I thank the witnesses for being here today. So many questions, such a distinguished panel, and so little time; it's very frustrating.

Chair White, if I could start with you, please. Traditionally your testimony and in your capacity and previously always has our boiler—famous boilerplate that says the views expressed and the testimony are those of the Chair of the SEC and do not necessarily represent the views of the full Commission or any Commissioner, standard procedure.

But while this is a good disclaimer, I think for general testimony we do love it when you all actually give personal views occasionally and not stand on the party line.

Here in the concept of an FSOC testimony it causes me to want to ask you a few questions. You serve on FSOC as one of the 10 voting members. Here is my question: If one of the other four SEC Commissioners was opposed to one or more of your FSOC positions, does Dodd-Frank require the SEC to vote ahead of the FSOC meeting to determine how you would then represent that view at the FSOC meeting?

Ms. WHITE. It does not, although I do consult with my fellow Commissioners before and after the FSOC meetings. But the short answer is "no."

Mr. HILL. And so in that consultation can you give me an example of where there has been disagreement between Commissioners?

Ms. WHITE. No. It is more just informationally briefing on what is going to come up before FSOC, what I am intending to do.

And again, under the structure, I am the member and obviously the voting member of FSOC. If there is anything to take a position on at the meeting, I convey that and obviously listen to any input or different points of view, and then afterwards report to the Commissioners on what transpired at the meeting. But there is not a structure to take a vote in advance.

Mr. HILL. But to continue sort of the line of questioning early this morning, if you had a Commissioner who was particularly passionate on a topic, would you be open to taking them to an FSOC meeting?

Ms. WHITE. Again, I certainly am totally amenable to that point of view and making certain that I fully understand it and take it into account.

Again, under the current structure and protocol, the Chair or the head of the agencies that are the designated 10 voting members, can bring a plus one, as it is called in this town, to the meeting with us, which has been a staff member.

So it is really not structured to have the other Presidential appointees attend these meetings or vote on these matters. Obviously, that creates some sensitivities, no question about it. As I said, it is up to Congress if they want to change that structure.

Mr. HILL. It just seems that internally it would be good if there were that level of disagreement where maybe a Commissioner wanted to express their views directly to FSOC, that that might even merit a formal Commission discussion and a formal view of the Commission potentially, before you simply represented the Commission in your own individual capacity.

Ms. WHITE. When I became Chair, I tried to change how we proceeded to get fuller input. But again, existing structure presents some of the challenges you are outlining.

Mr. HILL. So, I have only been in Congress 11 months or so, but one thing that has come up consistently, Mr. Watt—it is very helpful to have so many of you in one hearing—is this lack of transparency in the process that many in the industry feel.

And yes, it is a new agency and it has growing pains and has structure to be put in place.

But there is a right way and kind of a wrong way, I think, to do things in Washington. We all know the Administrative Procedure Act. We all know our obligation to openness. And in some cases we have taken actions before we even have rules. I think somebody referenced that we have designated insurance companies before we have even set what the standards might be for insurance companies.

So one thing I looked at is that for—in G-SIFIs certain capital surcharges there is a very transparent, mathematic—I have seen it written down, how to designate somebody for a G-SIFI surcharge. And that looked very transparent to me.

And yet, we don't even have that level of information on routine decisions in considering non-bank SIFI designations, or even, to some degree, activities-based SIFI analysis.

Who wants to comment on that? Maybe Chairman Gruenberg, you might comment on that, since it is both a banking and a non-bank designation question?

Mr. GRUENBERG. Congressman, as was discussed earlier, the FSOC established a process for a SIFI designation pursuant to a rulemaking and public notice and comment. Actually, I think the rulemaking went through three series of public comments.

And the first stage of the process, as I am sure you know, is a set of metrics, a set of thresholds through which an institution would pass.

And I must say there is a very high set of thresholds which would, almost by definition, be limited to some of the largest or most interlinked companies in the financial system. And that is something that is—any company can calculate in terms of projecting what the impact might be. And anyway, I will stop here.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentlelady from Utah, Mrs. Love.

Mrs. LOVE. Thank you, Mr. Chairman.

First of all, thank you all for being here. I know everyone is excited about the holiday season. I want to wish you all a Merry Christmas. And also to have such a great group of just so many of you here today, it is just really beneficial to me as a freshman. So, thank you. I have learned a lot today.

I have just a couple of questions. Comptroller Curry, you have previously testified that tailoring is an important tool in the OCC supervisory and regulatory toolbox because, as you have stated, while bank asset size is often a starting point in our assessment of appropriate standards, it is rarely, if ever, the sole determinant. Do you still agree with your statement to that effect?

Mr. CURRY. Yes, I do.

Mrs. LOVE. Okay. So when a regional bank with simple trading lending model and minimal interconnectedness grows to $49.9 billion to—in total assets to $50.1 billion in total assets, what new requirements apply to that institution?

Mr. CURRY. There is a cliff effect for the holding company under Section 165 of Dodd-Frank. So it will trigger heightened capital liquidity and other standards because it has crossed that threshold.

Mrs. LOVE. Okay. So does it make sense to automatically designate that institution, even though it does not engage in trading or other complex operations?

Mr. CURRY. Again, I am the supervisor of the bank—

Mrs. LOVE. I know—

Mr. CURRY. That is what I want to clarify. As we supervise the bank part of the holding company, we are not driven by the asset figure in terms of how we supervise that institution.

Mrs. LOVE. Okay. But we just determined that new requirements are applied to that institution. So I am trying to figure out your thoughts on this, and whether that designation—does that actually make sense, in terms of engaging in that type of regulatory—

Mr. CURRY. An asset threshold is initial, it has some value as initial or a first screen. So you can make some general observations about some institutions, that a certain asset size level may or may not be engaged in a particular activity.

As I stated in my earlier testimony, our focus as a supervisor is on that particular institution, the particular activities it is engaged in, and what are the risks that those activities present. And then we deal with our individualized or tailored plan of supervision according to that analysis and assessment.

Mrs. LOVE. Okay. So what I am trying to say is that the triggers automatically are applied to that institution. They automatically have those new requirements. So I guess what I am asking you is if you think that an institution like that, without just having that automatically trigger, do you think an institution like that realistically threaten the financial stability of the United States?

Mr. CURRY. I think it is an individualized determination. And again, I don't think that there is any magic to any asset threshold.

Mrs. LOVE. Okay. So wouldn't it make sense to look more closely at some of the banks which are actually similarly situated, and determine whether that designation is more beneficial or burdensome to the community in which they serve?

Mr. CURRY. I supervise the banking subsidiary, and that is exactly what we do.

Mrs. LOVE. Okay. But right now, it automatically—instead of actually doing the work first to see if that is actually—

Mr. CURRY. That is the effect of the statute, yes.

Mrs. LOVE. Okay. Well, I guess that is the point I am making.

Mr. CURRY. I understand.

Mrs. LOVE. Okay. If a $50 billion SIFI threshold were raised or eliminated, could the OCC still have the regulatory or supervisory tools that they need, necessary to make sure that all supervised banking organizations are operated in a safe and sound manner?

Mr. CURRY. As supervisor, that is what we would want to see, to make sure we have a safe and sound institution.

Mrs. LOVE. Okay. So you are pretty much saying that you would like to do that work first before it is automatically designated?

Mr. CURRY. That is what we do as a matter of course, as a bank supervisor to the national bank.

Mrs. LOVE. So would you support that statute being changed?

Mr. CURRY. Again, as stated in previous testimony, that is really a matter for Congress to decide what that initial first threshold is. In terms of my role as a supervisor of the bank, we will continue to apply a risk-based focus to our supervisory activities and standards.

Mrs. LOVE. Thank you. Thank you, Mr. Chairman.

Chairman HENSARLING. The time of the gentlelady has expired. The Chair now recognizes the gentleman from Minnesota, Mr. Emmer.

Mr. EMMER. Thank you, Mr. Chairman, and Ranking Member Waters. And thank you to the witnesses for being here for so long today.

Chair Massad, for you, it is good to see you again. We first had the opportunity, or inopportunity, to meet while I was serving on the Agriculture Committee. I wanted to ask you—I will put it this way. I wrote it out so I can do it right. Does it concern you that a regulatory body comprised primarily of banking, credit union, housing, and other regulators has the authority to intervene in markets that you, the CFTC, regulate, and potentially substitute their judgment for yours in highly complex or highly technical matters?

Mr. MASSAD. Thank you for the question, Congressman. I think the structure we have is a very good one, in that it brings all the regulators together, which allows us to look across the financial system, to look at emerging risks. There are issues in our markets where other regulators have certain responsibilities, whether they are things like margin rules for swaps, regulation of central clearing houses.

Mr. EMMER. If I could interrupt you, because it is limited time, and I appreciate—I wasn't asking for the mission statement. I am asking specifically with respect to the CFTC. I have heard all kinds of questioning today.

I have done a little reading about how the FSOC decided that in spite of the one insurance expert voting member, they substituted their judgment in place of his. And I am asking you, doesn't it concern you, or does it present any concern to you, that this body, this regulatory body, might substitute its opinion for yours at the CFTC?

Mr. MASSAD. I see it as a structure which doesn't so much involve substituting its opinion for ours, but rather, bringing regulators together so that they can share information, cooperate, and coordinate what we are doing. And I think that is very beneficial to the overall system.

Mr. EMMER. Let me put it to you this way: When the CFTC members meet to consider issuing a proposed or final rule, or decide an enforcement matter, even your—even though you are the Chairman of the CFTC, your vote counts the same as all of your fellow Commissioners, correct?

Mr. MASSAD. That is correct, sir.

Mr. EMMER. All right. But now, when you sit on the FSOC board, and you take a vote that might be different from what your fellow Commissioners would do at the CFTC, how is that not corrupting, if you will—maybe that is a very strong word—the process that we put in place, or that has been put in place to operate the CFTC?

Mr. MASSAD. The FSOC isn't taking votes on our enforcement matters, or on the rules that we are issuing. So I don't see a conflict there, sir.

Mr. EMMER. What if your position on the FSOC differs from one of your four Commissioners at the CFTC? What recourse do any of those Commissioners have for your votes on the FSOC?

Mr. MASSAD. I try to have an open door with all my Commissioners, and I am always willing to share my thoughts and hear theirs.

Mr. EMMER. So they just have to trust you?

Mr. MASSAD. I would say that the structure that Congress has decided is one where each of us as individuals are the—

Mr. EMMER. I know what they decided, and I apologize. I don't mean to be disrespectful. But the bottom line is they don't have any recourse other than your open door, and then they would have to trust you to do what they—to change or do what they are asking you to do.

Mr. MASSAD. I think again, we try to have a good dialogue about all these issues. And I am someone who likes to listen, and I try to respect other people's opinions, and take those into account, sir.

Mr. EMMER. Mr. Watt, Article 1, Section 7—and I am directing this at you because of your experience, your lengthy experience, and the respect you have from Members in Congress for your service here. And I will just cut to the chase. The Constitution gives Congress the power of the purse, correct?

Mr. WATT. Yes.

Mr. EMMER. When we look at the Financial Stability Oversight Council, how is it funded?

Mr. WATT. It is funded the way it is set up under the statute. You will have the authority to change it if you wanted to do that. But—

Mr. EMMER. Well, let me help. Assessments from bank holding companies managing $50 billion or more in assets, are taken and placed into a fund at the Treasury called a Financial Research Fund. This money is given to FSOC in the Office of Financial Research without oversight.

I have a bill that would actually subject the FSOC and the Office of Financial Research to oversight. Do you agree with that, congressional oversight?

Mr. WATT. I don't agree or disagree. If you can get it passed, I am sure FSOC would comply with it.

Mr. EMMER. I am looking at the budget that your—that FSOC approved for itself by 2015. Can you tell me, sir, under non-labor costs, what is "included in other support?"

Mr. WATT. We had a full briefing before we voted on that budget, and I am sure at the time, I understood every aspect of it. I don't remember specifically what each category is now. But we didn't just rubber-stamp that budget, I can assure you.

Mr. EMMER. And would you submit that briefing to my office on request?

Mr. WATT. I think it would be appropriate for you to make that request to FSOC rather than to me individually. I would not submit it as an individual member of FSOC.

Chairman HENSARLING. The time of the gentleman has expired. Members are advised there is another procedural vote on the Floor, with approximately 12 minutes remaining in the vote. We have three Members remaining in the queue, one who has left to go vote on the Floor, so I think we can get through this, and hopefully adjourn thereafter.

The Chair now recognizes the gentleman from Florida, Mr. Posey.

Mr. POSEY. Thank you very much, Mr. Chairman. I would like to just read a couple of quotes. This is from The Wall Street Journal.

"For the weekend of October 28th, the banks reported holding negative $1.4 billion of investment-grade corporate bonds maturing in at least 13 months, according to the Federal Reserve Bank of New York data. The figures, which signify banks, have pledged to sell more bonds than they will buy, reflect the net holdings at banks that act as a primary dealer authorized to trade billions of dollars of U.S. securities with the Fed, and buy Treasury debt direct at auction.

"On May 1, 2015, FINRA CEO Richard Ketchum stated there have been dramatic changes with respect to the fixed income market in recent years. Many of them have come in the reaction of the failures and market impact coming out of the credit crisis. That has led to much higher capital requirements, the Volcker Rule that limits the ability of proprietary trading with respect to bank holding companies, a range of other issues that have all had significant impact from the standpoint of liquidity of the fixed income market."

And then finally, Dave Nadig, Director of Exchange Traded Funds for the search firm FactSet said buy-in in the corporate bond market has dried up so much that it alone may pose a significant systemic threat.

And so my question for Director Cordray is, according to the FSOC website, the Financial Stability Oversight Council has a clear statutory mandate that creates for the first time collective accountability for identifying risk and responding to emerging threats to financial stability.

While the rest of the world has identified an emerging threat to financial stability, namely regulations like the Volcker Rule, Basel III's capital and liquidity standards, and other Dodd-Frank mandates that are draining liquidity from our fixed income markets, the FSOC and its chairman, Treasury Secretary Lew, has steadfastly refused to acknowledge that regulations are playing any role in creating this systemic risk.

As a voting member of FSOC, what resources have you marshaled, and what experts have you consulted to better understand the causes and consequences of reduced bond market liquidity?

Mr. CORDRAY. I think I would add that to a point that I thought made earlier was also a good point, which is as we add structure and regulations and requirements, we should consider the effects on international competitiveness.

I also think that you are raising a fair point, which is we should consider the effects on potential liquidity in the markets. It has been raised earlier in the hearing as well.

These are the kinds of considerations that should go into the kinds of work that is being done by the FSOC, and frankly work that is being done by the Congress. Quite a bit of the criteria that FSOC is employing are criteria that were embedded in the statute that Congress set that we are merely following, enforcing and carrying out.

But I think it is a fair point that you are making about how different requirements and different structures can potentially affect on the one hand stability and safety, and on the other hand potentially liquidity. I think it is fair for us to consider that as we go.

Mr. POSEY. What kind of technical expertise is there on the Treasury staff to address that?

Mr. CORDRAY. I think we have the same technical expertise there that we have on all the other issues the FSOC is considering, which is, there is FSOC staff itself in the Office of Financial Research, and from the member agencies of FSOC.

There was a graph put up earlier from the GAO report, and it was used at the time to suggest that certain agencies didn't devote enough people to certain problems. But I thought it was notable that when you look down the columns, the aggregate numbers of people being devoted by the agencies to address certain issues was ranged from in the 50s to in the 90s.

It is a considerable amount of support. This is very high level of support. We are talking about some of the top analysts, economists, statisticians, and researchers from all of these member agencies, including Treasury and the Federal Reserve. They are the same kind of people who work on all the complicated, difficult financial issues in our economy such as monetary policy, fiscal policy, international issues, and the like.

Mr. POSEY. So essentially, we are talking about the Treasury staff?

Mr. CORDRAY. No. I think we are talking about staff from all the member agencies. Depending on the issue, there may be more or less staff from different parts: more banking agency staff on a banking issue; more investment regulator staff on an investment issue; and the like.

Mr. POSEY. If compelling evidence is presented to the FSOC that regulations are in fact contributing to the illiquidity of the bond market and thereby creating potential systemic risk, do you agree that FSOC's mandate from Congress requires it to make recommendations designed to mitigate the risk, which could include revisiting the wisdom of aspects of the post-crisis regulatory response like the Volcker Rule and Basel III?

Mr. CORDRAY. You are asking me to speak only for myself. This is not a consensus view of FSOC. But if that were shown to be the case, if the evidence so demonstrated, I think that would be fair game.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from North Carolina, Mr. Pittenger.

Mr. PITTENGER. Thank you, Mr. Chairman.

Director Cordray, the CFPB ombudsman recently released their 2015 annual report to the Director. In the report it reviewed the Consumer Complaint Database on page 28. The recommendation was made to improve the process of how difficult the complaints in the database can be identified, including a recommendation that to remove the requirement, it must be verbatim to be deemed duplicative.

Mr. Cordray, do you recognize the grave concern that this is to these companies who are stigmatized through it? They are regarded—this is regarded really as unfair attribution. Do you see the impact this is having, and particularly that there is not investigation to determine that these—to verify these complaints before they go to the website?

What does the department plan to do and the Bureau plan to do to correct this?

Mr. CORDRAY. We actually just had a completed report and audit study done by our Inspector General of the Consumer Complaint Database. It was just issued in September, so less than 2 months ago. It indicated that there were a very small number of errors in the system. And that was a report and study and investigation that we followed very closely. There are recommendations that—

Mr. PITTENGER. Is that study available for review?

Mr. CORDRAY. Yes, I believe it is publicly available. It has been issued. And the GAO has also looked at this over the years and made a number of recommendations to us.

We are very mindful of those. We are very mindful of recommendations that you and your colleagues may want to bring to us as well. We do feel strongly that a public complaint database is an important incentive for institutions to step up their customer response—

Mr. PITTENGER. But do you agree—

Mr. CORDRAY. —and I think they are learning a lot from—

Mr. PITTENGER. —that they shouldn't have to be verbatim to be deemed as being the same complaint? They don't have to be verbatim.

Mr. CORDRAY. There are issues around the term "verbatim." And I have been in discussions about that with our ombudsman, been in discussions with that with other overseers, including the Inspector General and the like. It is something our consumer response group is looking at carefully to try to make sure—

Mr. PITTENGER. Okay . Thank you.

Mr. CORDRAY. —that they scrub that.

Mr. PITTENGER. I appreciate that.

Mr. CORDRAY. So we will be happy to give you more information as you—

Mr. PITTENGER. Would each of you provide the committee with any FSOC documents containing or relating to communications between the Financial Stability Board and FSOC? And each body members or staff concerning the designation non-bank financial companies, are there systemically important financial institutions or as global SIFIs? Is that acceptable to each of you all?

Mr. WATT. I don't have any. So, I can tell you that now.

Ms. MATZ. Nor do I.

Mr. MASSAD. I am not a member of the FSB. I have attended one or two meetings. I would like to hear the question again, but I don't believe I have anything.

Mr. PITTENGER. Go ahead, Chair White.

Ms. WHITE. I was going to say that I think there has been some production of documents in that vein. But I would have to check.

Mr. PITTENGER. Isn't the basis here one of transparency? I think we have recognized today the lack of adequate transparency with the agencies. And we are looking to find ways to rectify that.

Let's have a show of hands then, if you would, regarding your belief that FSOC's deliberations should be more open to the public scrutiny than in current practice. Would you all agree to that, then? Do you believe that there should be more openness?

Mr. CORDRAY. I think we have provided for more openness as we have been amending and changing procedures as we go—

Mr. PITTENGER. Do you think there is a basis to be more open?

Mr. CORDRAY. I think we—

Mr. PITTENGER. In light of what has been discussed today? Let me tell you what I have in mind.

Clearly, we believe that transparency is vital in our government. And I will be introducing a bill later on today that will provide a greater measure of transparency. Here are the two elements of this bill.

The first is to testify semiannually, each of you, before the House Financial Services Committee and the Senate Banking Committee. And you cannot decline the requirement. It would be mandatory. Or permit all members of the Financial Services Committee and the Senate Banking Committee to attend all FSOC meetings, whether or not they are open to the public.

Would you agree that would be acceptable? Do you have any problem with any of those?

Mr. WATT. If you can get it passed, we will comply with the law. I will comply with whatever law you pass. But—

Mr. PITTENGER. But do you think that is reasonable?

Mr. WATT. I don't think it is reasonable—

Mr. PITTENGER. Chair White, do you think it is reasonable?

Ms. WHITE. I certainly think we all should be responsive to Congress, all of us, at any time we are asked, frankly, without the necessity of a bill.

Mr. PITTENGER. Would you say—testify semiannually, or allow us to come to the hearings?

Ms. WHITE. But I think in terms of the FSOC process, we have to be very careful about what it is designed to do, and the nature of the information it considers.

Mr. PITTENGER. It is designed for openness and transparency.

Ms. WHITE. I think we should continue to look at openness for sure.

Mr. PITTENGER. That is what it is designed for. Thank you.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from New York, Mr. Meeks.

Mr. MEEKS. Thank you, Mr. Chairman.

Let me start with Mr. Gruenberg. The banking regulator just concluded that total loss-absorbing capacity (TLAC) for global systemically important banks would require banks to hold a certain amount of capital, but also requires them to issue a certain amount of unsecured debt that could be converted to capital in case of the bank's failure.

However, some observers, including I believe your Vice Chair, are concerned that the proposals call for banks to take on more debt at a time that the Fed is getting ready to raise interest rates. And he says that this is a risky and dangerous proposition. Is his concern legitimate?

Mr. GRUENBERG. I think the unsecured debt requirement is an important component of efforts to make these systemic companies able to fail in an orderly way without putting the taxpayer at risk, Congressman. The experience is that when a financial institution fails, all of its capital, all of its equity, is wiped out.

The only thing that remains is the debt held by the firm, which is then available on a closed-institution basis, after the institution fails, to be converted to capital, so that the private creditors of the failed company bear the losses for managing the failure of the institution.

And as it turns out, most of the large financial companies in the United States, most of our G-SIFIs, have substantial amounts of unsecured debt.

The rule that the Federal Reserve has proposed would ensure that they maintain a minimum amount. So if they get into difficulty, they can fail, and it is the private creditors, and not taxpayers, that are on the hook. And so for that reason, I think the proposal has merit.

Mr. MEEKS. Thank you. Let me jump to someone whom I am used to seeing sit up here. It is still funny to see him sit down there. That is the Honorable Mel Watt.

In recent weeks, the debate over what to do about the mortgage giants, Fannie Mae and Freddie Mac, has shifted from wholesale replacement to genuine reform, as replacing Fannie and Freddie as the political environment seems more unlikely. It seems like just replacing them is completely unlikely.

We all want more private capital in housing finance. But my question is, do you believe there is enough private capital to fulfill the role the GSEs play without raising mortgage rates substantially? And what are the challenges and lessons you are experiencing as you get more involved in the risk-sharing mechanisms?

Mr. WATT. We have tried out a number of risk-sharing mechanisms, trying to transfer as much of the risk to the private sector as possible. We are concerned about the capacity of the private sector to take on this risk, particularly in an economic downturn, or a distress situation.

And if the entire system were converted to the private sector, you would have that risk of not having a backstop during a downturn, and you would have the risk of—I think—of increased cost to a borrower, both of which I think would need to be evaluated by Congress as they evaluate how to move forward.

Mr. MEEKS. Thank you. I have a few seconds left, but I have one other question. I would have loved to have gone back. Let me just quickly direct this question to Comptroller Curry.

Amid regulations and supervision, the good news is that we are starting to see banks taking bolder steps to reduce risk and exit out of certain risky activities. On the other hand, I see that this raises concerns, because some of the activities are just shifting to less-regulated shadow banking entities. And banks are getting out of certain communities, and in certain countries.

Are we denying services to millions of lower-income Americans, not because the risk is too high, but simply because the profit margins are not as high or are too low?

Mr. CURRY. To my knowledge, there is no evidence of that, Congressman. It is something that we would assess in the course of our compliance examinations for the Community Reinvestment Act.

Chairman HENSARLING. The Chair now recognizes the gentleman from South Carolina, Mr. Mulvaney, for 5 minutes.

Mr. MULVANEY. I thank the chairman. And I thank the panel, especially for sticking around. It means a lot to us that you all don't put hard stops on us, and let us have some flexibility, and do this throughout the day.

I also apologize for having to run in and out during the day. We are evidently having serial motions to adjourn, Mr. Watt. You can explain to me why your side is doing that later on. It has to do with guns, I am told, believe it or not. Anyway, not my—

Mr. WATT. I generally couldn't explain it when I was here, so I certainly can't explain it now.

Mr. MULVANEY. I hear you. I want to go back to something that Mr. Green said early on in the hearing today. He mentioned the MetLife lawsuit, talked a little about the jurors, and said those folks don't have to have any particular insurance experience, do they? And of course, they don't. That is not the way our legal system works.

Then he looked at you and asked you if you agreed with that, and everybody sort of agreed the jurors don't need to have that. But that is not really the standard for the members of this group, right?

Does anybody really think that 12 good persons and true could serve in this role, or is it a good idea to have—everybody agrees we should have some expertise, right, in this?

That is why you are there, and that you couldn't do this job if we just randomly picked you off the street. So I didn't want people walking out of there thinking the standard for you folks is the same as the standard for a juror.

And I want to go into something that I believe Ms. Matz said to the chairman early on about the process you went through in your decision-making regarding MetLife. You said you were briefed extensively, which I want to talk about a little bit. You said it was done by the FSOC staffers. Let's talk about that. Was this to you individually? Was it to you and your staff? Was it to you as a group? Tell me how you were briefed on this, Ms. Matz?

Ms. MATZ. I was briefed by my staff, who participate actively with the FSOC staff, and the FSOC Deputies Council. Then we were briefed extensively as a Council, and we also received a great deal of briefing material.

Mr. MULVANEY. Okay. The final determination was made on June 30th. Do you remember the first time you were briefed on MetLife?

Ms. MATZ. I don't.

Mr. MULVANEY. Was it days in advance, weeks, months?

Ms. MATZ. Oh, no. It was longer. It had been in the works for probably a year or more, more than a year. So no, we were briefed on progress being made so I couldn't tell you when it was. But the staff worked on that designation for quite a long time.

Mr. MULVANEY. So the staff worked on it. I get that. We do that here as well, as Mr. Watt would say. We rely on our staff. How much time did you spend on it yourself?

Ms. MATZ. I spent a long time because of the tremendous amount of information both to get in briefings and reading material. The basis was I believe 300 or some-odd pages.

Mr. MULVANEY. Did you block off time during the day for reading those materials?

Ms. MATZ. I brought them home. I read them at night and on weekends.

Mr. MULVANEY. I do the same thing. Let me ask you this then. The reason I am focusing on you is you mentioned it during your opening statement. I think you also mentioned it to Mr. Hultgren in response to some of his questions.

Given your extensive briefing on the material, and the understanding that the statute requires you to look at 11 different factors, I want to go through them very, very briefly.

For example, you mentioned in your opening testimony—or response to the chairman—that one of the things that stood out in your mind was the derivatives. But that was one of the things that stood out in your mind as to the MetLife, in making the MetLife decision, or voting for the designation. So tell me, what it was about the derivatives that you thought was important?

Ms. MATZ. We just can't discuss that right now, because it is in litigation. We have public information on the FSOC website, but we are not at liberty to discuss the details of the deliberation.

Mr. MULVANEY. Okay, I will ask it this way, then. I disagree with that, by the way. We get that a lot. Mr. Watt didn't allow it when he was here, and I don't like it now that I am here, because you can tell us stuff. But we will skip it then. You made the same determination for Prudential, right?

Ms. MATZ. Yes.

Mr. MULVANEY. And you voted to designate them. And they are not in the lawsuit right now. So what was it—I take it you did the same level of preparation in making your decisions for Prudential that you did for MetLife?

Ms. MATZ. Correct.

Mr. MULVANEY. So what was it about the derivatives decision that Prudential had that made you inclined to vote for the designation?

Ms. MATZ. Well, it wasn't just one item. It was the totality of—

Mr. MULVANEY. I get that. Tell me one thing about the derivatives position?

Ms. MATZ. The size of it. I can't remember off the top of my head. It was a huge amount of derivatives and exposures—

Mr. MULVANEY. Huge in relation to what?

Ms. MATZ. In relation to other institutions, how they were exposed to other institutions, and exposed other institutions—

Mr. MULVANEY. No, that is not my question. Huge in relation to what? The size of their assets? The size of the—

Ms. MATZ. No, their exposure. It wasn't in relation to the size of their assets. We view it in relation to their exposure to the financial system of the United States.

Mr. MULVANEY. Within a billion dollars, what was the size of their derivatives?

Ms. MATZ. I don't recall.

Mr. MULVANEY. Thank you.

Mr. MESSER [presiding]. The gentleman's time has expired. The Chair now recognizes himself for 5 minutes for questions.

It is a fundamental American principle that in America we follow the rule of law. And for the rule of law to be meaningful, of course it has to be transparent.

It has to be written down. People have to have the ability to understand the law and see whether they are complying with it. But we want to talk about that principle in the context of the FSOC's current approach and designated non-bank financial institutions, particularly insurance companies, under that designation.

Under the rule of law, folks first ought to understand why they are being regulated, what are the standards we are applying to determine whether you will be regulated, and then how they will be regulated.

What are the standards you will be held accountable to if you are designated a non-bank SIFI? Mr. Woodall, you have been very patient today, I have to concede, for all this Kentucky Phi Beta Kappa this is of course, a panel full of Phi Beta Kappas and Ivy League decorated folks. I will admit something I rarely admit in public, which is I am a Phi Beta Kappa.

But I will tell you, for this complex world of acronyms and initials and regulatory structure and laws, I think, like most Americans, we are just—it is all Greek to us and we are trying to figure it out.

In the construct of the rule of law that I talked about, Mr. Woodall, I have offered legislation that I think is really a modest proposal. It is H.R. 3857. And here is what it does very simply.

I will read it here to make sure I am getting it accurate. The bill would simply prevent FSOC from designating any further nonbank financial institutions for heightened Fed supervision until 90 days after.

First, the Federal Reserve establishes prudential standards for non-bank financial companies as required by Section 165(a) and (b) of Dodd-Frank.

Second, the Federal Reserve promulgates regulations, setting forth criteria for exempting certain types of classes of U.S. non-bank financial companies or foreign non-bank financial companies from supervision, as required by Section 170 of Dodd-Frank.

And third, the FSOC re-evaluates within calendar year 2016, each previous SIFI designation and rescinds any such designation if it determines that the non-bank financial company no longer meets the standards for designation that have been brought forward. I would just like to get your reaction. Would that legislation prevent FSOC from doing its job?

Mr. WOODALL. I was waiting to see what the question was going to be. Would it prevent what now?

Mr. MESSER. Would it prevent FSOC from doing its job? Again, would that seem like a reasonable proposal? That the companies that will be designated or the entities that are designated, non-bank SIFIs, have some way of understanding why it is they are designated that way and of course the, an off-ramp that would allow them to determine their—

Mr. WOODALL. That was your third point and it seems to me that is what we are working for right now, is to try to get more clarity in what that exit ramp is. I have just recently submitted a list of 17 different options for the FSOC to consider. It is now being considered by their deputies.

And it is ways to clarify that where it can be much more clear to the company what it needs to do. As I have said several times before, the company says to the regulator, tell us what we are doing wrong and we will fix it.

Mr. MESSER. Yes. Is there any way you can provide that list of 17 options to the committee?

Mr. WOODALL. Yes.

Mr. MESSER. Thank you. I guess I will open it up to the rest of the panel. Could someone give me the rationale for designating non-bank entities as SIFIs before establishing any public standard for doing so?

And question two, before establishing the criteria that they will be held to?

Mr. MASSAD. I think, Congressman, the criteria by which we designate were set forth in the statute. And they were further spelled out as far as the procedures in our rules, which were subject to notice—

Mr. MESSER. So you are telling me you believe that the entities that are being designated SIFIs understand the standards by which they are being evaluated?

Mr. MASSAD. They are—

Mr. MESSER. Every entity I talk to says they are not.

Mr. MASSAD. —publicly available, and I think we also provide memoranda to the company prior to the designation.

Mr. MESSER. Any others?

Thank you.

Seeing no one else in the queue and no further questions, I thank the panel for their stamina and for their testimony today.

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.

The hearing is now adjourned.

[Whereupon, at 2:26 p.m., the hearing was adjourned.]

A P P E N D I X

December 8, 2015

Testimony of Richard Cordray
Director, Consumer Financial Protection Bureau
Before the House Financial Services Committee
December 8, 2015

Chairman Hensarling, Ranking Member Waters, and Members of the Committee, thank you for the opportunity to testify today. I am glad to work with you to strengthen our financial system.

As we are all aware, just a few years ago disruptions in the housing market preceded a financial crisis that caused significant damage to our people and our economy. The ensuing deep recession caused millions of Americans to lose their jobs and millions of families to lose their homes. Many saw their retirement savings diminished as Americans lost trillions of dollars in household wealth. Severe deficiencies in the loans supporting mortgage-backed securities, in particular, shocked and upended the financial system.

In the aftermath of the crisis, Congress passed financial reform legislation to address the problems that led to the crisis and help ensure they would not happen again. Among the steps taken were the creation of the Financial Stability Oversight Council and the Consumer Financial Protection Bureau.

The creation of the FSOC provides, for the first time, a means of comprehensively monitoring the stability of our nation's financial system. Prior to the crisis, the U.S. financial regulatory framework focused more on individual institutions and markets in isolation from one another. No one regulatory body was responsible for monitoring and addressing overall risks to financial stability, which too often involve different types of financial firms operating in complex and intertwined ways across multiple markets. The potential for supervisory and regulatory gaps were viewed as creating blind spots in important parts of the financial system.

After the crisis, Congress recognized the need for a mechanism to bring financial regulators together to monitor the financial system, share information and expertise, and coordinate their regulatory efforts to respond effectively to emerging threats to financial stability. One approach that Congress specified to address these issues was to designate certain financial institutions and financial market utilities as systemically important to the stability of the U.S. financial system, for the purposes of applying enhanced prudential standards and supervision.

As you know, the FSOC includes the Consumer Bureau, which is the first federal agency solely focused on protecting consumers in the financial marketplace. Products such as mortgages and credit cards are involved in some of the most important financial transactions in people's lives. These products are often funded through complex financial markets, and they may constitute the underlying assets for more complex and highly leveraged securities. As the crisis made clear, financial stability, market discipline, and consumer protections are closely interrelated.

Part of the mission of the Consumer Bureau therefore is to help ensure that the recent economic meltdown is not repeated. The practices that led to the financial crisis are inconsistent with the principles of fairness, transparency, and competitiveness in markets. We are exercising the authority Congress gave us to ensure balanced oversight and prevent harmful practices in consumer financial markets. When honest and innovative businesses can succeed on their merits, fair competition drives growth and progress and the entire financial system rests on stronger and sturdier foundations.

As the Director of the Consumer Bureau, I look forward to continuing to fulfill Congress's vision for our agency and my role on the FSOC. All of us here today are working together to identify risks to financial stability, promote market discipline, and respond to emerging threats to the stability of the financial system. All of this work should help us better avoid the problems that so nearly caused this country to face economic collapse.

Thank you for the opportunity to testify today. I look forward to your questions.

TESTIMONY OF

THOMAS J. CURRY
COMPTROLLER OF THE CURRENCY

before the

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

December 8, 2015

Statement Required by 12 U.S.C. § 250:

The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

I. Introduction

Chairman Hensarling, Ranking Member Waters, and members of the Committee, thank you for the opportunity to testify today. I am pleased to provide the views of the Office of the Comptroller of the Currency (OCC) on the functions and operations of the Financial Stability Oversight Council (FSOC or Council).

The OCC charters, regulates, and supervises national banks and federal savings associations (collectively, banks). These banks range from small community banks to multi-trillion dollar institutions that are among the world's largest financial companies. The OCC's mission is to ensure that these banks operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations. As the only federal financial regulator with prudential regulation as its primary focus, the OCC has specialized knowledge about the safe and sound operations of banks.

As one of the FSOC's ten voting members, the OCC brings considerable expertise to the Council. Many of the areas of financial risk on which the OCC focuses as part of its bank supervision – for example, credit, liquidity, interest rate, and operational risk – are the same risks that the FSOC evaluates with respect to nonbank financial companies. Furthermore, the OCC has staff experts with in-depth knowledge in areas such as asset management who support the OCC's FSOC work.[1]

Congress established the Council to identify, monitor, and respond to systemic risk. The FSOC brings together its member agencies to fulfill this critical mission. Through its committees and staff, the FSOC provides a formal, structured process for communicating, coordinating, and

[1] Approximately 44% of national banks and 27% of federal savings associations, including a number of limited purpose trust institutions, are engaged in asset management activities. To supervise these institutions, the OCC has over 170 examiners specializing in asset management activities and risks.

responding to emerging market, industry, and regulatory developments, as well as to unforeseen events.[2] In addition, the FSOC identifies and designates nonbank financial companies and financial market utilities (FMUs) for heightened supervision.

My testimony will provide a brief summary of specific mandates Congress has given to the FSOC and a discussion of recent, important actions of the Council.

II. The FSOC's Statutory Mandates

The FSOC's Purposes

In section 112 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act or Act), Congress described the purposes of the FSOC as follows: (1) to identify risks to the financial stability of the United States that could arise from the material financial distress or failure, or from ongoing activities, of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace; (2) to promote market discipline by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the U.S. government will shield them from losses in the event of failure; and (3) to respond to emerging threats to the stability of the U.S. financial system. As described below, Congress provided the FSOC with tools to carry out these purposes.

Nonbank Financial Company Designations

In section 113 of the Act, Congress gave the FSOC the authority to designate, on a case-by-case basis, certain nonbank financial companies for supervision by the Board of Governors of the Federal Reserve System (Board) and to be subject to heightened prudential standards, if the Council determines that material financial distress at any such company would pose a threat to

[2] Current committees include: the Deputies Committee; Data Committee; Financial Market Utilities and Payment, Clearing, and Settlement Activities Committee; Nonbank Financial Companies Designations Committee; Regulation and Resolution Committee; and Systemic Risk Committee.

the financial stability of the United States. A number of additional provisions apply to nonbank financial companies that are designated for supervision by the Board. For example, designated companies become subject to the Board's examination authority, enforcement actions under 12 U.S.C. § 1818, and assessments by the Board and the Office of Financial Research. To date, the FSOC has used this authority to designate four nonbank financial companies.[3]

The FSOC uses a three-stage process to identify, evaluate, and engage with nonbank financial companies under review. In stage one of the process, the FSOC applies six quantitative thresholds to a broad group of nonbank financial companies to identify companies that merit further evaluation. In stage two, the FSOC notifies a company when it comes under active review and considers existing public and regulatory information, as well as information submitted by the company. If the Council decides to evaluate the company further, it notifies the company and begins stage three. In this stage, the Council conducts a detailed, in-depth analysis of the company, including a review of confidential information provided by the company. Throughout the stage two and stage three processes, the Council engages extensively with the company, and in stage three, prior to a designation, the company has the opportunity to make a presentation before the FSOC principals. Following this robust process, the FSOC may designate the company pursuant to a supermajority vote.

By contrast, in accordance with section 165 of the Act, bank holding companies with total consolidated assets equal to or greater than $50 billion are automatically subject to the Board's heightened prudential standards. While the Act permits the Board to tailor these standards, including by considering a company's capital structure, riskiness, complexity,

[3] These companies are: American International Group, Inc.; General Electric Capital Corporation, Inc.; Prudential Financial, Inc.; and MetLife, Inc.

financial activities, size, and any other risk factors the Board deems appropriate, the Act does not provide these companies with the opportunity to contest the application of these standards.

Financial Market Utility Designations

Title VIII of the Act charges the FSOC with the responsibility for identifying and designating systemically important FMUs. The Act subjects designated FMUs to heightened supervision by one of three agencies: (1) the Securities and Exchange Commission (SEC) in the case of clearing agencies; (2) the Commodity Futures Trading Commission (CFTC) in the case of derivatives clearing organizations; and (3) the Board for all other FMUs (on either a direct or back-up basis). The FSOC determines whether to designate an FMU as systemically important on a case-by-case basis, after assessing the FMU's market activities and the effect its failure or disruption would have on critical markets, financial institutions, or the broader financial system. Once designated, an FMU is subject to periodic examination by the SEC, CFTC, or Board, as appropriate. Designated FMUs also are subject to operating rules issued by these agencies and must give advance notice to their supervising agency of any material changes to their operations. Designated FMUs are subject to enforcement proceedings by their supervising agency for breach of these requirements, unsafe or unsound practices, or other violations of law, in accordance with 12 U.S.C. § 1818(b). Pursuant to a final rule and interpretive guidance issued by the FSOC in 2011, the FSOC designated eight entities as systemically important FMUs in 2012.[4] The FSOC monitors the financial markets and periodically determines whether designation status should remain in place for each FMU and whether it should designate additional FMUs.

[4] These entities are: The Clearing House Payments Company, L.L.C., on the basis of its role as operator of The Clearing House Interbank Payments System; CLS Bank International; Chicago Mercantile Exchange, Inc.; Depository Trust Company; Fixed Income Clearing Corporation; ICE Clear Credit LLC; National Securities Clearing Corporation; and Options Clearing Corporation.

Other Authority of the FSOC

In addition to the authority to designate nonbank financial companies and FMUs as systemically important, Congress gave the FSOC other tools to address systemic risk. For example, under section 120 of the Act, the FSOC has the authority to issue recommendations to the primary financial regulatory agencies to apply new or heightened standards and safeguards for a financial activity or practice conducted by the firms under the agencies' respective jurisdictions. The FSOC may issue such recommendations if it determines that the conduct of such activity or practice could create or increase the risk of significant liquidity, credit, or other problems spreading among such firms, the U.S. financial markets, or low-income, minority, or underserved communities. Pursuant to section 120, in 2012, the FSOC published for public comment proposed recommendations with respect to money market mutual funds.

III. Recent Actions

The Council has demonstrated a sustained commitment to working collaboratively to fulfill its statutory mission in a transparent and accountable manner. Council members and their staffs have developed strong working relationships, and the Council, its committees, and working groups provide a forum to have candid conversations; share confidential, market-sensitive information; and ask tough questions that help make the U.S. financial system safer.

The Council convenes regularly to monitor market developments, consider a wide range of potential risks to financial stability, and, when necessary, take action to protect the United States against potential threats to the financial system. As part of this work, the Council regularly examines significant market developments and structural issues within the financial system. Examples of such issues include short-term wholesale funding, cybersecurity, volatility in fixed income markets, equity market structure, high frequency and automated trading activities, leveraged lending, reference rate reform, and interest rate risk at a variety of financial institutions.

Nonbank Financial Company Designation Supplemental Procedures. In February of this year, the FSOC adopted supplemental procedures to the nonbank financial company designation process to address stakeholder concerns and to formalize a number of existing Council practices regarding engagement with companies. For example, the Council now will notify a nonbank financial company within 30 days of forming an analytical team to commence an active review of the company in stage two. As a result, companies will know their status earlier in the process, which in turn will provide them with more opportunities to engage with and provide input to the Council. Additionally, under the supplemental procedures, the Council is providing companies with a clearer and more robust annual review process and an opportunity for an oral hearing every five years to contest a designation.

The supplemental procedures also provide greater transparency while still allowing the Council to protect sensitive, nonpublic information. For example, the Council will continue its recent practice of including more information in its public bases for designations in an effort to provide a deeper understanding of the Council's analysis. In addition, the Council has started to publish more information in its annual reports about its designation work. Together, these procedural changes to the FSOC's nonbank designations process make it a more interactive and transparent process that permits the Council to continue its important work while also addressing concerns of stakeholders.

Asset Management Analysis. The Council has conducted extensive analysis and public outreach regarding potential risks to U.S. financial stability posed by asset management products and activities. In May 2014, the Council's Deputies Committee hosted a conference on the asset management industry and its activities during which practitioners, academics, and other stakeholders discussed a variety of topics related to the industry. In July 2014, the Council directed staff to undertake a more focused analysis of industry-wide products and activities to assess risks associated with this industry. In order to inform that analysis, in December 2014, the Council voted unanimously to release a notice seeking public comment on aspects of the asset management industry. In particular, the Council sought input from the public about risks to the U.S. financial system associated with liquidity and redemptions, leverage, operational functions, and resolution in the asset management industry. The notice provided another important mechanism to solicit input from the public and build upon the Council's prior public engagement in this area. The public comment period closed in March 2015. The FSOC is now evaluating, through a series of working groups, whether asset management products or activities pose a threat to the financial stability of the United States.

IV. Conclusion

The Dodd-Frank Act provided the FSOC with important duties and responsibilities to promote the stability of the U.S. financial system. The issues that the Council confronts in carrying out these duties are, by their nature, complex and far-reaching. Developing appropriate and measured responses to these issues requires thoughtful deliberation and debate among the Council's members. The OCC remains committed to helping the Council achieve its mission.

STATEMENT OF

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on

OVERSIGHT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

December 8, 2015

2128 Rayburn House Office Building

Chairman Hensarling, Ranking Member Waters, and members of the Committee, thank you for the opportunity to testify today on the work being undertaken by the Financial Stability Oversight Council (FSOC). My testimony will discuss the FSOC's efforts to identify and address systemic risk, and the designation of entities as systemically important financial institutions (SIFIs).

Background and Mission of the FSOC

The financial crisis that began in 2007 exposed a number of serious vulnerabilities in the U.S. financial system. In the years leading up to the crisis, misaligned incentives, excessive leverage and risk taking, and gaps in regulation all contributed to a serious and, at the time, unrecognized increase in systemic risk. The crisis that followed resulted in the most severe economic downturn since the Great Depression. While some risks affecting individual products and institutions had been recognized, neither the financial markets nor the regulatory community was able to see the whole picture.

The FSOC was established in 2010 by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) to address this gap in the regulatory framework. Its key functions are to facilitate information sharing among its member agencies, to identify and respond to emerging risks to financial stability, and to promote market discipline. The FSOC is also responsible for designating nonbank SIFIs for heightened supervision by the Board of Governors of the Federal Reserve System (FRB). By statute, the FSOC is composed of 10 voting members and 5 nonvoting members, and its structure allows the member agencies to work together while preserving the ability of the independent regulators to fulfill their statutory mandates.

Specific Authorities

Identification of emerging risks that can have a systemic impact is among the key responsibilities of the FSOC. This work is carried out and documented primarily through the development of the FSOC's Annual Reports. This year the FSOC issued its fifth such report, and as in previous years, a significant portion of the report is devoted to describing emerging risks to financial stability.

The FSOC is also responsible for determining whether a nonbank financial company should be designated as a SIFI based on the statutory factors in Section 113 of the Dodd-Frank Act. A firm that is designated as systemic is subject to FRB supervision and enhanced prudential standards, including the requirement to file a resolution plan to demonstrate how the company would be resolved in a rapid and orderly manner under the Bankruptcy Code in the event of its material financial distress or failure.

FDIC's Role

The FDIC has as its primary mission the maintenance of public confidence in our nation's financial system, which is the foundation of financial stability. It performs that mission in three important ways. First, it insures deposits held in our nation's banking system. Second, it examines and supervises banks for safety and soundness and compliance with laws and regulations. Finally, it is responsible for the resolution of failed banks and, under the Dodd-Frank Act, for the resolvability of large and complex financial institutions. These authorities give the FDIC a valuable perspective on markets and market participants that it brings to bear on FSOC deliberations and actions.

Systemic Risk Identification and Monitoring

One of the primary responsibilities of the FSOC is to identify risks to the financial stability of the United States financial system and to respond to these risks. Through the work of its standing committees and its principal-level meetings, the FSOC monitors: the U.S. macroeconomic environment; developments in financial markets, firms and products; the regulatory environment; and international trends and other potential exogenous shocks to financial stability. This is a continuous process the FSOC engages in throughout the year, culminating in the assessment of potential threats to the financial system published in the FSOC Annual Report.

The FSOC Annual Report provides an evaluation of the current macroeconomic environment and financial developments and a progress report on regulatory developments that form the basis of an analysis of potential emerging risks to U.S. financial stability. Moreover, the FSOC Annual Report contains a set of recommendations intended to address those potential threats. We now have the benefit of five annual reports, which together outline the key systemic risks facing the financial system – and how they have evolved over time - and provide a framework to formulate policies to address these risks.

The first Annual Report, published in 2011, described a still fragile financial system recovering slowly from the deepest financial crisis since the Great Depression. At that time, much of the regulatory agenda intended to improve the resilience of the financial system as a whole — and of the financial institutions that make up the financial system — had yet to be completed. Rulemakings and reforms in areas like capital, liquidity, resolution planning, derivatives, tri-party repos, and money market funds, among others, were not complete, and in some cases, not yet underway. In contrast, the most recent 2015 FSOC Annual Report describes a more stable, though still recovering macro economy and broad-based improvement in most financial markets and market participants. Three broad areas of risk which the FSOC has been following closely, and which are of particular consequence to the FDIC, are interest rate risk, credit risk, and cybersecurity.

The five annual reports have been prepared against the backdrop of prolonged low interest rates and have accordingly addressed potential risks to market participants and the financial system of a sharp rise in interest rates as well as the implications of increased risk taking in a low-rate environment (so-called "reach for yield" behavior). We have identified industry trends that highlight the importance of careful management of sensitivity to interest rate risk. Nationally, a number of institutions report a significantly liability- sensitive balance sheet position, meaning that a rise in short-term interest rates may cause funding costs to rise at a faster rate than long-term asset yields. For a number of institutions, the potential exists for material securities depreciation relative to capital in a rising interest rate environment. Significant, unmitigated levels of interest rate or market risk can lead to losses and liquidity constraints when prevailing rates change significantly. Effectively managing interest rate risk is part of the business of banking, and many institutions have effectively measured, monitored, and controlled exposures to achieve earnings goals. However, we expect the FSOC will continue to closely review interest rate risk in the industry.

In addition to problems related to maturity mismatch, we have seen an increase in credit risk caused by easing of lending standards, and other forms of increased risk-taking. The past two annual reports describe a sharp increase in high-yield and leveraged lending markets as some market participants reach for yield, and accordingly, strong activity in the secondary markets for these credits. The FDIC, along with the other banking agencies, issued guidance in 2013 to the institutions we supervise that sets forth prudent underwriting and risk management standards for these types of credits. The banking agencies published results of the 2015 SNC review on November 5th. The review found that the level of risk in the SNC portfolio is increasing, with elevated levels of credit risk centered mainly in loans to leveraged borrowers as well as weaknesses in leveraged loan underwriting practices and oil and gas sector credit exposures. The agencies will continue to closely monitor the leveraged lending activities of insured depository institutions and will continue to stress the need to conform to 2013 leveraged lending guidance.

Cybersecurity has been cited as a risk in each of the five FSOC annual reports, and in 2015, rose to the top of the list of potential emerging threats and vulnerabilities as a result of the increase in the number and severity of cyber incidents and the real costs this issue presents in terms of risk assessment and mitigation. Given the deliberate and increasingly sophisticated attempts to disrupt institutions and markets, and given the increasing reliance on complex and interconnected technologies, it is clear these incidents will continue and will require heightened attention in the years to come. This year's report addresses the importance of the public/private partnership in information sharing, developing strong best practices to enhance the security and resilience of the nation's critical infrastructure – including the portions that are not within the financial system, but upon which financial companies rely, and solid plans for response and recovery.

The FSOC Annual Report recommends enhancements to existing information sharing between government and industry, including increasing the speed of information exchange by automating the sharing of technical data where possible. The FSOC has been supportive of the ongoing work done through the Federal Financial Institutions Examination Council (FFIEC), which includes release of a Cybersecurity Assessment Tool to help institutions identify their risks and level of cybersecurity preparedness. If there is a significant cyber incident, a coordinated, nationwide response will be essential. The FSOC encourages the establishment of a national plan for cyber incident response for the financial sector that includes identifying and articulating the role of law enforcement, the Department of Homeland Security, and financial regulators.

In the coming year, the FSOC will continue its ongoing process of monitoring these risks and others as we begin to prepare our sixth annual report in 2016.

Nonbank Designation

As previously noted, Section 113 of the Dodd-Frank Act authorizes the FSOC to designate a nonbank financial company if the FSOC determines that material financial distress at the company, or the nature, scope, size, scale, concentration, interconnectedness, or mix of the activities of the company, could pose a threat to the financial stability of the United States. Rather than relying on any one specific factor, or using a strictly quantitative approach, the Dodd-Frank Act requires the FSOC to evaluate both quantitative measures and qualitative factors. It also ensures significant engagement between FSOC staff and representatives of the companies being evaluated and provides due process rights to financial companies being considered for designation. Designated companies are subject to enhanced supervision by the FRB and are required to develop and submit resolution plans as noted above.

The Designation Process

After three opportunities for public comment, the FSOC issued a Final Rule and Interpretive Guidance (Rule and Guidance) outlining the process it uses in carrying out the requirements of section 113 of the Dodd-Frank Act. The FSOC received significant feedback on the procedures from a wide range of commenters, and considered their recommendations. The Guidance lays out a 3-stage process, with each stage involving a more in-depth evaluation and analysis of the financial company. This approach allows the FSOC to engage in a flexible company-specific analysis that reflects the unique risks posed by each company and is appropriate for the company's size, scope, and complexity.

In the first stage of the nonbank financial company designation process, FSOC compares all nonbank financial companies to public "threshold" quantitative standards. The Stage 1 thresholds are based on public information and are readily calculable by nonbank financial companies and market participants. They are:

- $50 billion in total consolidated assets;
- $30 billion in gross notional credit default swaps (CDS) outstanding for which a nonbank financial company is the reference entity;
- $3.5 billion of derivative liabilities;
- $20 billion in total debt outstanding;
- 15 to 1 leverage ratio; and
- 10 percent short-term debt ratio.

Generally, in order to be further evaluated, a company would have to meet or exceed at least 2 of these thresholds. Only a small subset of nonbank financial companies will exceed the threshold standards and receive additional analysis. These thresholds, adopted by notice and comment as part of the Rule and Guidance, add significant transparency to the designation process. Earlier this year, FSOC staff published guidance on its website that provides additional details explaining how the Stage 1 thresholds are calculated. Publication of these thresholds and the related guidance allows nonbank financial companies to assess, from the outset of the process, whether they would likely be subject to additional FSOC review.

In stages 2 and 3 of the process, the FSOC considers all the statutory factors set forth in Section 113 of the Dodd-Frank Act. These factors include the following:

- leverage, off-balance sheet exposures, and financial assets;

- transactions/relationships with other significant nonbank financial companies and significant bank holding companies;
- importance as a credit source for households, businesses, State/local governments, and U.S. financial system, and as a credit source for low-income, minority, or underserved communities, and impact failure would have on credit for such communities;
- extent to which it manages rather than owns assets, and whether ownership of assets under management is diffuse;
- nature, scope, size, scale, concentration, interconnectedness, and mix of activities;
- degree to which it is already regulated by 1 or more primary financial regulatory agencies;
- liabilities, including reliance on short-term funding; and
- any other risk-related factors the FSOC deems appropriate.

In the second stage of review, FSOC analyzes each nonbank financial company using public information, and nonpublic information from regulators, if provided, to determine whether the company could pose a threat to U.S. financial stability. An analytical team, made up of staff members from the FSOC and FSOC member agencies, reviews these information sources to analyze these risk factors and to consider the mechanisms through which risk can be transmitted to the rest of the financial system. After the analysis in Stage 2, the Council votes on whether to conduct additional analysis in Stage 3. As was noted in this year's Annual Report, to date, four nonbank financial companies have been subject to final designation by the FSOC, and the FSOC has voted not to advance five nonbank financial companies beyond Stage 2 because the analyses indicated that the firms were unlikely to be systemic.

In the third stage, FSOC notifies in writing each nonbank financial company that the FSOC believes merits further review to collect directly from the company information that was not available in prior stages. Each nonbank financial company reviewed at this stage is provided an opportunity to submit written materials related to the FSOC's analysis.

During this time, a company may have extensive contact with FSOC staff and the analytical team. Although not required by the statute, the FSOC encourages meetings between company representatives and members of the analytical team to discuss details of the company's operations and financing and to hear the company's views. Based on the results of the analyses conducted in Stage 3, the FSOC may make a proposed determination regarding designation of the nonbank financial company, which requires a vote of at least two-thirds of the FSOC's voting members then serving, including an affirmative vote by the FSOC Chairperson. If a proposed designation determination is made, the FSOC will provide the nonbank financial company with a written explanation of the basis of the proposed determination. Any company that receives a proposed designation may submit a written response and request an oral hearing before the FSOC. The FSOC has adopted hearing procedures, clarified in response to industry comment, to ensure that any company that wishes to contest a proposed designation can fully and fairly present its views before the FSOC principals.

After a hearing, or if none is requested, the FSOC will vote on a final determination with respect to the designation of the nonbank financial company. If two-thirds of the members then serving, including the FSOC Chairperson, vote in favor of the determination to subject the company to FRB supervision, the firm is designated. The FSOC provides any nonbank financial company that receives such a vote with written notice of its final determination, including a detailed explanation of the basis of its decision. Ultimately, the FSOC's close adherence to the requirements of the statute and the Rule and Guidance is intended to ensure a consistent, fair, and transparent designation process for nonbank financial companies.

The FSOC annually reevaluates each designation and will rescind a designation if it determines that the company no longer meets the statutory standards. In connection with this annual reevaluation, the company has the opportunity to meet with FSOC staff to discuss the review and to present information regarding changes that may be relevant to the threat the company could pose to financial stability, such as restructuring efforts, regulatory developments, or market changes. A company also has the opportunity to contest its designation at an oral hearing before the FSOC once every five years.

Companies designated by the FSOC for FRB supervision are subject to a number of authorities designed to reduce systemic risk. The Dodd-Frank Act requires the FRB to apply enhanced prudential standards and early remediation requirements to these companies and authorizes the FRB to tailor the application of these standards and requirements to different companies on an individual basis or by category. Prudential standards include capital standards, stress testing requirements, and the submission of resolution plans to the FDIC and the FRB.

Designated companies, as well as large bank holding companies, are required to submit resolution plans identifying how the company could be resolved in a rapid and orderly manner under the Bankruptcy Code in the event of its material financial distress or failure. The FDIC and the FRB review each resolution plan. Under Section 165(d) of the Dodd-Frank Act, if the FDIC and the FRB jointly determine that the resolution plan is not credible or would not facilitate an orderly resolution of the firm under the Bankruptcy Code, then the company must resubmit the plan with revisions, including, if necessary, proposed changes in business operations or corporate structure. If the company fails to resubmit a credible plan that would result in orderly resolution under the Bankruptcy Code, the FDIC and the FRB may jointly impose more stringent capital, leverage, or liquidity requirements; as well as growth, activities, or operations restrictions. In addition, if the company fails to resubmit a credible plan after two years, the FDIC and FRB, in consultation with the FSOC, may impose divestiture requirements.

FSOC transparency and process

FSOC policies and procedures were crafted to ensure a robust exchange of information throughout the designation process. As the process has evolved, opportunities for additional transparency both within the operations and the designation process were identified by the FSOC and in comments by external parties. As a result, the FSOC undertook several initiatives over the past year and a half to improve both transparency and engagement with financial companies.

These include:

- providing no less than seven days' advance notice of regularly scheduled meetings, including information about the agenda for both open and closed meetings;
- publication of minutes of Council meetings, including all votes of Council members;
- publication of answers to frequently asked questions about designation;
- publication of guidance that provides additional details explaining the calculation of Stage 1 thresholds; and
- the adoption of supplemental procedures related to its nonbank designations process.

The supplemental procedures, adopted in February of 2015, address a number of suggestions made by industry stakeholders as well as members of Congress. These supplemental procedures require, among other things, notification to companies that they have been advanced to Stage 2 and that they are being evaluated by the FSOC, opportunities for the company to submit information to the FSOC for review by the analytical team, opportunities in Stage 2 for the company to meet with the analytical team, notice if the Council votes not to advance to Stage 3, and if the Council votes to advance a company to Stage 3, notification if specific aspects of the company's operations or activities were identified as the primary focus for the evaluation. Additionally, the supplemental procedures provide clarification that the FSOC intends to grant any timely request for an oral hearing from a company subject to a proposed designation and for any such hearing to be conducted by the FSOC members. If a company is designated, the designation must be reevaluated annually and the supplemental procedures provide that the company may submit new information, meet with FSOC staff, and get feedback on the review as part of the reevaluation process. The procedures provide an opportunity for a designated company to have an oral hearing before the FSOC once every five years. These steps reflect an ongoing commitment to good governance and transparency, and the FSOC will continue to look for opportunities to improve both.

Conclusion

Thank you for the opportunity to share with the Committee some details of the work that the FDIC has done with the FSOC to identify and address systemic risk in the financial system. The FSOC fills a significant gap in the regulatory framework that existed prior to its creation. The FDIC is committed to the ongoing work of the FSOC and supports the cooperative approach to identifying and responding to risks along with other FSOC members.

Testimony of Chairman Timothy G. Massad before the
U.S. House Committee on Financial Services
Washington, DC
December 8, 2015

Thank you Chairman Hensarling, Ranking Member Waters and distinguished members of this Committee. I appreciate the opportunity to testify today.

You have asked me to set forth my views on the agenda, operations and structure of the Financial Stability Oversight Council (FSOC), and to discuss the perspective I bring to its deliberations as one of ten voting members.

Therefore, today I would like to talk about how my role as Chairman of the Commodity Futures Trading Commission (CFTC) informs my approach to the FSOC. I would also like to highlight a few issues that are common priorities for the Commission and for the Council.

The CFTC is responsible for overseeing the U.S. derivatives markets. This includes the commodity futures and related options markets and, as a result of the Dodd-Frank Act, the vast majority of the swaps market. Although most Americans do not participate in these markets directly, they are vital to our economy, affecting the prices we all pay for food, energy, and other goods and services. They do this by enabling businesses of all kinds to hedge commercial risk, whether a farmer hedging the price of his crop, a manufacturer hedging the price of supplies, or an exporter hedging foreign exchange risk.

For these markets to work well, sensible regulation is essential. This is a lesson we learned in 2008, when a lack of oversight of the swaps market led to a buildup of excessive risk that contributed to the intensity of the worst global financial crisis since the Great Depression. That crisis, which had many causes, cost our economy more than 8 million jobs, wiped out the savings of millions of Americans and led to a foreclosure crisis that cost millions of families their homes.

My perspective as a member of the FSOC is shaped by my responsibilities as CFTC Chairman. The laws we implement are intended to deter and prevent fraud and manipulation in our markets, to promote financial integrity in transactions and the institutions we oversee, to avoid systemic risk, to protect customers, and to encourage innovation and competition.

I would like to highlight a few of the CFTC's priorities that are particularly relevant to the FSOC. The first area is the implementation of a regulatory framework for over-the-counter swaps. The Dodd-Frank Act codified the four basic reforms agreed to by the leaders of the G-20 nations—central clearing of standardized swaps, transparent trading on regulated platforms, oversight of major market players and regular reporting. We have made great progress in implementing these reforms. In particular, with respect to central clearing, today approximately 75 percent of swap transactions in our markets are being cleared, as compared to only about 15 percent in 2007. Other financial regulators also have responsibilities in the area of swaps reform, and the FSOC provides a useful way for us to communicate and coordinate.

A second area is the regulation of central clearinghouses. While central clearing mitigates risk, it does not eliminate it. So we're focused on making sure clearinghouses are strong and resilient. This is another focus for FSOC, as highlighted in its recent annual report.

While we remain the primary supervisor of the clearinghouses in the derivatives markets, the Federal Reserve and the FDIC have responsibilities as well. We work collaboratively on these important issues – and we also work with the Securities and Exchange Commission (SEC), which has primary oversight of clearing agencies in its markets.

Domestically, the CFTC has undertaken a major overhaul of our clearinghouse oversight, substantially strengthened risk management, and increased transparency. We are also leading important work that is taking place on clearinghouse resiliency efforts internationally -- working with foreign regulators and other FSOC members.

Another priority of CFTC is strong, sound and resilient markets. Here, the FSOC also plays an important role in bringing agencies together. For example, following the volatility in the Treasury market on October 15, 2014, the FSOC served as a good forum to share information. Shortly thereafter, CFTC staff presented our analysis of what took place in the Treasury futures market to the Council. And Commission staff subsequently worked with the Department of Treasury, the Board of Governors of the Federal Reserve, the SEC and the Federal Reserve Bank of New York to prepare a report analyzing what happened on that day and its relation to the recent evolution of the Treasury market. We are continuing to work together to look at issues pertaining to volatility, liquidity and the oversight of these markets, including the availability of data and the growth of automated trading.

In addition, cybersecurity is one of our agency's top priorities. I believe it is one of the greatest risks to our financial system today. The FSOC plays an important role in facilitating dialogue and cooperation among regulators in addressing this very important issue.

Another area of focus for the CFTC over the last few years that is important to FSOC is the oversight of benchmarks. Benchmark integrity is vital to our financial system, which is why we have made this a priority issue in our enforcement efforts. We brought the first case against a global bank concerning LIBOR manipulation in 2012, and we have imposed penalties on many of the world's largest banking institutions for similar actions. We have also actively supported the development of voluntary principles for the administration of benchmarks to ensure integrity and transparency.

I believe that one of the most valuable functions of the FSOC is simply to bring together the regulators and agencies that have responsibilities for our financial markets and institutions on a regular basis. By sharing information and ideas, I believe we are in a better position to identify and address potential systemic risks – and better serve the American people.

Mr. Chairman, thank you very much for the opportunity to share my views before this Committee today.

NCUA
National Credit Union Administration

Embargoed until Delivery
10:00 a.m.
December 8, 2015

Congressional Testimony

Debbie Matz
Board Chairman
National Credit Union Administration

House Committee on Financial Services

Hearing on Oversight of the
Financial Stability Oversight Council

NCUA is the independent federal agency created by the U.S. Congress to regulate, charter, and supervise federal credit unions. With the backing of the full faith and credit of the United States, NCUA operates and manages the National Credit Union Share Insurance Fund, insuring the deposits of more than 102 million account holders in all federal credit unions and the overwhelming majority of state-chartered credit unions.

At MyCreditUnion.gov and Pocket Cents, NCUA also educates the public on consumer protection and financial literacy issues.

NCUA
National Credit Union Administration

Congressional Testimony

Thank you, Chairman Hensarling, Ranking Member Waters, and Members of the Committee. I am Debbie Matz, Board Chairman of the National Credit Union Administration. I appreciate this opportunity to discuss the structure, operations, and agenda of the Financial Stability Oversight Council, as well as the expertise I bring and the views I have on these matters.

Before I address the topics outlined in the invitation letter, it's important to briefly review the history behind the Council's creation. The decision to establish FSOC came in response to the 2008–2009 financial crisis. This decision was driven by the recognition that financial crises are enormously costly—not only to individual financial services companies, but also the general economy and the financial well-being of our nation's citizens and their families. In all, the American economy lost 9 million jobs, major stock market indexes declined by more than 50 percent, and household net worth plunged by $12 trillion.[1]

The sudden failures of several large, interconnected financial companies during the crisis triggered a cascade of more failures and near-failures of financial companies previously thought invulnerable. As the crisis deepened, many of our nation's largest financial companies were left holding toxic assets on their balance sheets without sufficient capital to absorb the losses. To prevent further failures and greater losses, the federal government provided previously unthinkable amounts of support and took a number of unprecedented actions.

The interconnections within the financial system laid bare by the financial crisis meant that no sector was immune to the fallout. Even the consumer-oriented, member-owned credit union system suffered sizable losses. In all, 90 retail credit unions that were holding insufficient capital to cover their risks failed as a result of the crisis.[2]

Compounding those failures, five corporate credit unions with investments in faulty mortgage-backed securities had to be liquidated, which led to near-catastrophic consequences for all surviving credit unions.[3] Recognizing the instability those costs would cause throughout the credit union system, Congress created the Temporary Corporate Credit

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[1] The total jobs lost figure was calculated from data provided by the Bureau of Labor Statistics from December 2007 through June 2009. Declines in stock market indexes were calculated using information from Moody's Analytics using data from the *Wall Street Journal* for the period of December 27, 2007, to March 5, 2009. The change in household net worth was calculated using the Federal Reserve's Financial Accounts of the U.S. for the second quarter of 2007 through the first quarter of 2009.

[2] The number of failed federally insured credit unions is calculated for the period beginning January 1, 2008, through December 31, 2011.

[3] Corporate credit unions exist primarily to provide retail credit unions with banking, liquidity, and investment services. To date, federally insured credit unions have paid $4.8 billion in assessments and experienced $5.6 billion in losses in the form of contributed capital to cover the losses associated with the corporate crisis.

Union Stabilization Fund.[4] NCUA also infused more than $120 billion of emergency liquidity and guarantees to stabilize the credit union system.[5]

FSOC's Creation and Mission

Ultimately, the 2008–2009 financial crisis made clear that financial distress at interconnected financial firms cannot be easily isolated, and the broader financial market cannot quickly absorb the collapse of very large financial companies. The crisis also highlighted vulnerabilities in the U.S. financial system, including gaps in regulators' jurisdiction over large, complex nonbank financial companies that play a significant role in our financial system. The complex, evolving financial system needed some form of broader oversight. Establishing the Council was one of the core reforms of the Dodd-Frank Wall Street Reform and Consumer Protection Act.[6]

Congress created FSOC to serve as an early warning system to detect and address emerging threats to our nation's financial stability and the economy. The primary goal is to prevent system-wide financial crises or at least mitigate their effects.

Specifically, the Council's statutory mandate has three elements. They are to:

- Identify risks to the financial stability of the United States posed by the material financial distress or failure, or ongoing activities, of large, interconnected financial companies.
- Promote market discipline by eliminating expectations on the part of shareholders, creditors, and counterparties of these large, interconnected financial companies that the government will shield them from losses in the event of their failure.
- Respond to emerging threats to the stability of the U.S. financial system.

These principles have guided FSOC from its inception, when the organizational framework was designed, to the present as the processes and procedures have evolved.

FSOC's Structure and Operations

The Council brings together federal and state regulators with responsibility for the major sectors of the U.S. financial system to share their diverse expertise and to identify and address potential risks to financial stability. As designed by Congress, the Council has ten voting members and five non-voting members, who serve in an advisory capacity.[7] The

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[4] *See* 12 U.S.C. § 1790e.
[5] NCUA provided more than $20 billion in liquidity assistance through the Central Liquidity Facility and over $100 billion in guarantees. NCUA also had to borrow $5 billion from the U.S. Treasury to support the credit union system.
[6] *See* 12 U.S.C. §§ 5301-5641.
[7] *See* 12 U.S.C. § 5321(b).

Council's voting members comprise the Treasury Secretary, an independent insurance expert, and the lead official of every major federal financial regulatory agency, including NCUA.[8]

Each FSOC member has deep experience in financial market analysis and specialized knowledge within a particular sector. The Council's multi-agency structure ensures that a diverse array of views, research, and emerging risks in each sector are considered when examining the financial system and making decisions. In my view, the quality of the decisions FSOC makes is enhanced by the diversity of viewpoints of the principals at the table.

The Council's principals meet almost monthly; to date, we have met 54 times. These meetings cover a wide range of topics, including international financial and regulatory developments, unusual geopolitical developments that affect financial markets, emerging changes to financial market infrastructure, general economic trends, and emerging issues like cyber threats.

The meetings of FSOC principals represent the culmination of a thorough process of review and analysis. FSOC and agency staff provide research and recommendations after deliberations in committees and working groups. For example, the Council's Deputies Committee, composed of senior staff from each principal's agency, meets twice each month to evaluate and discuss possible approaches to mitigate threats to our nation's financial stability before these matters are presented to the Council.

At the working level, there are five committees meeting regularly on critical issues such as monitoring systemic risk, examining developments related to the accumulation and standardization of data across financial institutions, and reviewing developments related to the designation of systemically important nonbank financial companies. The committees consist of staff from FSOC member agencies, as well as the Office of Financial Research, another entity created by the Dodd-Frank Act.[9] Through the committees, staff are engaged in sharing information, conducting research, and monitoring market developments.

The committees often create working groups to examine specific issues. For example, the Systemic Risk Committee formed a working group to examine the interest rate risk exposures in the financial system. The findings of the working group were presented to the Systemic Risk Committee, the Deputies Committee, and the Council. Thus, the information about the working group's findings flowed up through FSOC's reporting structure to the principals.

From the beginning, the Council has recognized the importance of public transparency and participation. Stakeholder feedback has helped the Council clarify its procedures, enhance

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[8] *See id.*
[9] *See* 12 U.S.C. §§ 5341-5346.

its analysis, and improve its decision-making. FSOC also is committed to publicly disseminating timely information about the Council's decisions, while balancing the need to protect proprietary corporate information and avoid moving markets.

In developing its procedures, the Council is mindful of statutory requirements. In some cases, the Dodd-Frank Act was prescriptive, such as providing the factors to consider when designating a nonbank financial company as systemically important. In other instances, the law was flexible, permitting the Council to determine how to make the designation.

The evolving process for designating nonbank financial companies offers a prime example of how FSOC looks to the law and develops the complementary procedures. Within the first few months of establishment, the Council published in the *Federal Register* for comment an advance notice of proposed rulemaking on the process for designating nonbank financial companies.[10] Based on feedback, the Council made revisions to the process and issued a notice of proposed rulemaking at the start of 2011.[11] These procedures were further revised before the rule was finalized in 2012.[12]

Then, in February of this year, the Council made further revisions based on additional public comments and congressional suggestions.[13] The revised procedures allow more communication and interaction with companies earlier in the determination process, enhance transparency to the broader public about the designation process, and improve engagement during the Council's annual reevaluations of designations.[14]

As an FSOC principal, I am committed to continuing to explore how we can further refine and improve the Council's operations and structure.

Expertise and Perspective

Each Council member brings a unique perspective to the table, informed by our particular areas of professional expertise and experiences. In my case, that is a multi-decade career working on economic and financial services issues. Early on, I served on the staff of the congressional Joint Economic Committee where I advised lawmakers on a host of domestic policy issues, including the fiscal conditions of cities and municipalities during the financial crises of the late 1970s and early 1980s, housing policy, and infrastructure finance. Subsequently, I served as an NCUA Board Member and a credit union executive.

More recently, I have led NCUA through the aftermath of the Great Recession. When I assumed the role of NCUA Board Chairman, five corporate credit unions were on the brink

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[10] *See* 75 FR 61653 (Oct. 6, 2010).
[11] *See* 76 FR 4555 (Jan. 26, 2011).
[12] *See* 77 FR 21637 (Apr. 11, 2012).
[13] *See, for example,* The Honorable Carolyn B. Maloney, Member of Congress, letter to The Honorable Jacob Lew, Chairman, Financial Stability Oversight Council, July 29, 2014.
[14] *See* https://www.treasury.gov/press-center/press-releases/Pages/jl9766.aspx.

of failure. These failures could have led to the collapse of the credit union system. To prevent this, NCUA developed a mechanism to securitize more than $40 billion in toxic assets once held by the failed corporate credit unions.

To protect retail credit unions from the repercussions of the crisis, NCUA strengthened safety and soundness regulation and supervision. The agency also reallocated resources toward credit unions that posed the largest risks to the National Credit Union Share Insurance Fund. In the process, NCUA replenished the Share Insurance Fund, which now insures the deposits of more than 102 million members.

As a federal financial regulator for almost 10 years, I oversee an agency that now supervises more than 6,000 financial institutions with total assets exceeding $1.1 trillion. Each of these institutions must manage the assets and liabilities on their balance sheets. Asset-liability management is critical to institutions of all sizes. In fact, major elements of FSOC's designation of a systemically important financial institution include the composition of the firm's balance sheet, off-balance sheet exposure, and interconnectedness with the entire financial services sector. As such, these experiences have prepared me for working with FSOC in analyzing the performance of financial markets and operations of individual companies.

Through the Council's structure, NCUA is able to regularly meet with federal and state financial regulators to discuss and identify emerging risks and consider the financial system as a whole, rather than just in constituent parts. FSOC's member agencies share information, ideas, and expertise in a way that previously did not occur, and this information has given NCUA and other FSOC members a greater perspective on the entire financial system.

In addition to FSOC's collective decisions aimed at enhancing and protecting U.S. financial stability, the institutions regulated by the individual prudential regulators benefit, as well. From NCUA's perspective, the Council's emphasis on enhancing financial stability and mitigating potential risks is another form of protection, both for credit unions as financial institutions and for their members. This complements NCUA's supervision of credit unions and share insurance coverage of members' accounts up to $250,000 if a credit union fails. The missions of the two organizations, therefore, are interrelated and important to promoting confidence in the U.S. financial system.

FSOC's Agenda and Work

By law, the Council must remain alert to emerging issues that concern the financial system as a whole.[15] FSOC also takes action by "closing loopholes, improving consolidated supervision, and establishing robust regulatory oversight."[16]

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[15] *See* 12 U.S.C. § 5322.
[16] 155 Cong. Rec. H. 14409 (daily ed. Dec. 9, 2009) (statement of Rep. Ed Perlmutter).

In carrying out FSOC's responsibilities, the Council has taken advantage of the multi-agency structure to draw on experts from the individual agencies and FSOC staff to collectively review potential threats as they unfold for Council members. For example, Council members have been briefed on the potential consequences of instability in Eurozone financial markets from a default on Greek debt and work on reference rates, among others. In addition, the Council is immediately briefed on unusual market developments such as sizable, sudden, short-term swings in our securities markets, with an eye on developing an understanding of their systemic importance.

A recent concern for financial markets, including the credit union system, is the ongoing challenges related to the low interest-rate environment and the likely transition to a higher rate environment, potentially with a flatter yield curve. Additionally, cybersecurity risks are an evolving threat that affect all financial institutions. In this interconnected environment, cyberattacks continue to evolve in sophistication and coordination, which reinforces the need of financial regulators and their regulated entities to remain vigilant, evolve with the changing environment, and maintain effective resilience. FSOC has closely studied both of these issues and raised public awareness about them to better protect the financial system.

FSOC's work related to asset managers has received considerable public attention, as well. To better understand the complex role of asset managers in the financial system, the Deputies Committee has held a major conference and convened numerous other meetings and discussions with asset managers and other knowledgeable individuals. In addition, the Council has requested public comments seeking responses to a number of questions about asset managers. This resulted in more than 1,000 pages of material, which has helped to define the Council's path forward. As a result of these interactions, the staff work on asset managers has been focused on industry-wide products and activities to better assess potential risks associated with the asset management industry. FSOC staff continues to work on this critical area.

Another important aspect of FSOC's work is its annual report. As required by law, this report summarizes the work of the Council, significant financial market and regulatory developments, potential emerging threats to U.S. financial stability, and all determinations of systemically important financial institutions.[17] The report also makes recommendations to enhance the integrity, efficiency, competitiveness, and stability of U.S. financial markets, to promote market discipline, and to maintain investor confidence.[18] The 2015 report highlighted the need for heightened risk management and supervisory attention in the areas of cybersecurity, increased risk taking in a low-yield market, and financial innovation activities, among others.[19]

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[17] *See* 12 U.S.C. § 5322(a)(2)(N).
[18] *See id.* § 5322(a)(2)(N)(vi).
[19] *See* https://www.treasury.gov/initiatives/fsoc/studies-reports/Documents/2015%20FSOC%20Annual%20Report.pdf.

The statutory duty that has received the most public attention is FSOC's responsibility to identify large, nonbank financial firms that, if they were to fail, would transmit that distress through the rest of the financial system and cause a threat to financial stability. Under the Dodd-Frank Act, financial companies identified for this designation are subject to consolidated oversight by the Federal Reserve and enhanced prudential standards.[20] The Federal Reserve can tailor such standards so they are appropriate to the nonbank financial company, but a designated firm is required to develop a living will to demonstrate how it could reach a quick and orderly resolution should it fail.[21]

As noted earlier, since its inception, FSOC has moved deliberately as it has created its process for identifying and designating nonbank financial companies for enhanced supervision. In all, FSOC has identified four large, interconnected financial companies for this oversight.[22] After extensive review and consideration, a majority of the Council voted in favor of designating each of these complex nonbank financial companies. The Council determined that should these institutions experience financial distress, their financial problems could threaten the stability of other systemically important institutions and therefore the financial stability of the United States. FSOC has reviewed and will continue to review these designations annually.[23] If significant changes occur within a designated firm that might impact the designation, FSOC has the authority to remove the designation.

Going forward, I am committed to continuing to move deliberately on any further designations of nonbank financial firms. As the financial system evolves, I also believe so too must the Council's policies and procedures for designating nonbank financial companies.

Conclusion

In conclusion, the Financial Stability Oversight Council at the five-year mark should be seen as a dynamic, evolving organization. For the first time, the Council has formally brought together all of the regulators charged with oversight of critical segments of the financial system. The Council has stood up an effective, responsive organization, with a unique charge from Congress: to safeguard the financial stability of the United States.

To that end, FSOC has thus far promoted collaboration across financial regulators, established appropriate rules and procedures which reflect public input, identified four systemically important nonbank financial companies, and furthered greater public awareness of threats to our financial system. The Council is therefore performing a valuable service for the American people by identifying risks, promoting market discipline, and responding to emerging threats to the U.S. financial system on critical issues such as the

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[20] *See* 12 U.S.C. §§ 5361, 5365.
[21] *See id.* §§ 5365(i), 5365(d).
[22] The four nonbank financial companies designated as systemically important are American International Group, General Electric Capital Corporation, Prudential Financial, and MetLife.
[23] *See id.* § 5323(d).

oversight of key financial market utilities, data standards infrastructure, and cybersecurity threats.

Speaking for NCUA, participation on FSOC has expanded our perspective, helped the agency understand the broader context for some of the emerging risks to credit unions, and improved access to critical financial and market information. FSOC also has positioned NCUA to receive and share best practices with other financial regulators. As a result, NCUA is better able to fulfill its mission of providing, through regulation and supervision, a safe and sound credit union system which promotes confidence in the national system of cooperative credit.

Furthermore, I find NCUA's inclusion on FSOC to be mutually beneficial. The Council benefits from NCUA's inclusion in the process by having a multitude of views and a broader perspective in its discussions of systemic risk.

Thank you for your consideration of my thoughts on these matters. I look forward to answering any questions you may have.

Statement of Melvin L. Watt
Director, Federal Housing Finance Agency

Before the U.S. House of Representatives Committee on Financial Services

Oversight of the Financial Stability Oversight Council

December 8, 2015

Chairman Hensarling, Ranking Member Waters, and members of the Committee, thank you for the opportunity to testify today about the Financial Stability Oversight Council (FSOC).

Next month will mark the two year anniversary of my participation in FSOC. During that time, FSOC has designated one nonbank financial company for supervision by the Board of Governors of the Federal Reserve System subject to enhanced prudential standards, supplemented its designation procedures, launched a comprehensive analysis of the asset management industry, revised its transparency policy, and released two annual reports. I have found that FSOC is an important forum for consultation, information sharing, and decision-making related to risk in the financial system and its impact on U.S. financial stability.

As an independent regulator, FHFA is responsible for supervision, regulation, and housing mission oversight of Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System. In addition, since 2008 FHFA has served as conservator of Fannie Mae and Freddie Mac. FHFA's housing finance market expertise contributes to FSOC's ability to understand and better assess broad systemic risks. Through FHFA's active participation in all FSOC committees, including the Deputies Committee and all standing committees, FHFA engages regularly with other members on information sharing, policy matters and risk assessments of the entities subject to FSOC jurisdiction and the markets in which they operate.

Participation in FSOC provides FHFA and other regulators with opportunities to raise and discuss potential issues that are broader than the horizons and jurisdictions of individual members. This forum for raising issues serves as a valuable tool for improving coordination among regulators and eliminating duplications, as well as identifying and addressing regulatory and oversight gaps.

FHFA's engagement with FSOC enhances the Agency's ability to carry out its mission by providing another venue for consulting with other regulators. On FSOC committees, members of FHFA's staff work closely with the staffs of other members and gather information that strengthens FHFA as the regulator of Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. Through its annual report, FSOC has also supported several of FHFA's regulatory initiatives and has identified and discussed important issues that affect the mortgage and housing finance markets in the United States that are beyond FHFA's jurisdiction to regulate directly. FHFA appreciates the support of FSOC members in some of its most important initiatives, including development of a Single Security, credit risk transfer transactions undertaken by Fannie Mae and Freddie Mac, reform of their representations and warranties framework, and development of standards for their non-bank mortgage servicers. FSOC has also supported granting FHFA express authority to examine and, where appropriate, exercise enforcement authority over Enterprise contractual counterparties.

Beyond these regulatory coordination roles, the evaluation of whether to designate nonbank financial companies for supervision by the Board of Governors of the Federal Reserve System and subject them to enhanced prudential standards continues to be a significant and important FSOC function. A vote to designate a nonbank financial company for supervision by the Board of Governors of the Federal Reserve System subject to enhanced prudential standards is a decision that I take seriously. A designation has many consequences for each such financial company, and each decision is arrived at only after extensive engagement with the company, a thorough analysis of the facts, and careful deliberation.

Transparency in the designations process and in FSOC's other work is crucial to the Council's ability to maintain the public's trust. On the other hand, much of the information we consider in making the assessments FSOC is required by statute to make is sensitive, nonpublic information. We spend a lot of time considering how to appropriately balance these interests. FSOC has enhanced its official transparency policies, increased the information shared through meeting minutes, hosted public outreach meetings on the nonbank designations process, and solicited public comment on the asset management industry.

I look forward to continuing to engage with my fellow FSOC members to meet our duties and responsibilities in a manner that fosters transparency, is fair and analytical, and contributes to appropriate risk management and risk reduction.

Thank you, and I look forward to answering your questions.

Testimony on "Oversight of the Financial Stability Oversight Council"
by
Chair Mary Jo White
U.S. Securities and Exchange Commission

Before the
Committee on Financial Services
United States House of Representatives
December 8, 2015

Chairman Hensarling, Ranking Member Waters, and Members of the Committee:

Thank you for inviting me to testify regarding the Financial Stability Oversight Council (Council).[1] Below I highlight my perspective on the Council and my role on it.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) established the Council to provide comprehensive monitoring of the stability of our nation's financial system. Specifically, the Council is responsible for:

- Identifying risks to the financial stability of the United States that could arise from the material financial distress or failure – or ongoing activities – of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace;

- Promoting market discipline by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the government will shield them from losses in the event of failure; and

- Responding to emerging threats to the stability of the United States financial system.[2]

In addition, the Council provides a formal forum for coordination among the various financial regulators, a structure that, during my tenure, has resulted in at least monthly meetings or teleconferences among members. This kind of collaborative sharing of information and concerns is, in my view, very important to safeguarding the U.S. financial system.

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[1] The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the full Commission, or any Commissioner.

[2] *See* Dodd-Frank Act § 112(a)(1).

Pursuant to the Dodd-Frank Act, the Chair of the Commission serves as a voting member of the Council, along with the heads of eight other federal financial authorities and an independent member with insurance expertise.[3] In addition to the ten voting members of the Council, there are five nonvoting members that serve in an advisory capacity.[4] Pursuant to this statutory construct, I, together with certain SEC staff as needed, participate in the activities of the Council, which include: determining if certain nonbank financial companies' material financial distress could pose a threat to the financial stability of the United States and should be subject to heightened prudential supervision by the Board of Governors of the Federal Reserve System;[5] preparing an Annual Report, which analyzes potential emerging threats to financial stability and makes certain recommendations; and studying areas identified in the Annual Report, as well as other issues that arise that could potentially impact the financial stability of the U.S. In addition, staff-level activities of the Council, as well as meetings of the principals, provide a new and important avenue for regulators to share information, discuss approaches, and foster cooperation.

As you know, the Dodd-Frank Act gave the SEC significant new responsibilities for, among other things, over-the-counter derivatives, hedge fund and other private fund advisers, municipal advisors, and clearing agencies. These are measures designed in part to promote financial stability and strengthen our financial system. They are also important areas implicating the SEC's mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation. Tackling systemic risk in most areas, of course, requires a broader

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[3] *See* Dodd-Frank Act § 111(b)(1). By statute, the Secretary of the Treasury serves as Chairperson of the Council. *Id.*

[4] See Dodd-Frank Act § 111(b)(2)

[5] *See* Dodd-Frank Act §§ 112(a)(2)(H) and 113. *See also* Financial Stability Oversight Council Makes First Nonbank Financial Company Designations to Address Potential Threats to Financial Stability (July 9, 2013), *available at* http://www.treasury.gov/press-center/press-releases/Pages/jl2004.aspx

program beyond any particular agency's jurisdiction and authority. Risks that could cascade through our financial system could impact a range of market participants, many of whom, for example, the SEC does not oversee. The Council provides an important forum for studying and identifying systemic risks across different markets and market participants.

As one of two capital markets regulators on the Council – the other being the Chairman of the Commodity Futures Trading Commission – the market perspective that I and SEC staff bring to the Council is essential. In particular, the SEC's historical tripartite mission necessarily gives the SEC unique insight into many areas on which the Council is focused, such as the potential financial stability risks of asset management activities and products, the ongoing changes to market structure, and the role of central counterparties. SEC engagement with the Council on these issues helps to ensure that relevant expertise is brought to bear on these important subjects.

As discussed above, each year, as required by the Dodd-Frank Act, the Council is required to report to Congress on, among other things, the activities of the Council, significant financial market and regulatory developments, and potential emerging threats to the financial stability of the United States.[6] Each of the Council's five reports has been approved unanimously, the most recent one in May of this year.[7] In that most recent report, the Council identified a need for continued attention and/or action with respect to certain key potential emerging threats and vulnerabilities, including the need for:

[6] *See* Dodd-Frank Act § 112(a)(2)(N).

[7] The 2015 Annual Report is available at http://www.treasury.gov/initiatives/fsoc/studies-reports/Documents/2015%20FSOC%20Annual%20Report.pdf. Links to prior year annual reports are available at http://www.treasury.gov/initiatives/fsoc/studies-reports/Pages/2015-Annual-Report.aspx.

- Financial sector companies to continue to mitigate risks associated with cyberattacks, and the need for strong collaboration and data sharing among financial service companies and government agencies;

- Market participants and regulators to continue to monitor how financial market structure changes may affect liquidity and market functioning in all sectors including Treasuries and other fixed income, equities, and futures;

- Regulators to continue evaluating whether existing standards are sufficiently robust to mitigate the risk that central counterparties could transmit credit and liquidity problems among financial institutions and markets during periods of market stress; and

- Regulators to continue to address gaps in the scope and quality of available data on financial markets and institutions, as well as to continue improving data sharing that may enhance risk identification and monitoring efforts.

Since 2012, the Council has also focused on, among other areas, potential risks to financial stability associated with the asset management industry.[8] In May 2014, Council staff hosted a Public Asset Manager Conference that permitted the staffs of the member agencies to hear directly from the asset management industry and other stakeholders. In July 2014, the Council directed staff to undertake a focused analysis of industry-wide products and activities to assess potential risks to financial stability. To inform that analysis, in December 2014, the Council voted unanimously to release a notice seeking public comment on aspects of the asset management industry, in particular seeking input from the public about potential risks to the U.S. financial system associated with liquidity and redemptions, leverage, operational functions, and resolutions in the asset management industry. The public comment period closed in March 2015, and the staff's analytical work in this area continues. Throughout, SEC staff has been actively engaging with representatives of other Council members in the analysis of potential financial

[8] Independently, at my direction, SEC staff has been developing recommendations for enhancing the asset management industry's risk monitoring and regulatory safeguards. I publicly outlined those initiatives last December. *See* http://www.sec.gov/News/Speech/Detail/Speech/1370543677722. To date, the Commission has proposed: (1) new rules and forms, as well as amendments to its rules and forms, to modernize the reporting and disclosure of information by registered investment companies; and (2) a new rule that would require open-end mutual funds to adopt and implement liquidity management programs.

stability risks posed by asset management activities and has been sharing its expertise on asset management, including the ways in which asset management activities differ from banking activities.

With respect to designations of any nonbank financial companies as systemically important pursuant to the Council's authority under section 113 of the Dodd-Frank Act, I believe it is important to be data-driven and to conduct rigorous analysis throughout the process. The framework for the analysis is provided by the Dodd-Frank Act and the guidance adopted by the Council after notice and comment. In connection with each firm that is analyzed in the designation process, SEC staff including economists in our Division of Economic and Risk Analysis assist my review of the data and analysis provided by both the Council staff and the company under consideration.

Another area of focus by the Council is on enhancing the transparency of its functions, which I consider to be an important focus. Toward that end, in February 2015, the Council unanimously adopted changes to the designation process, including: (1) increased and earlier engagement with companies under review; (2) increased public transparency concerning, for example, the designation factors and the metrics assessed in stage one of the process; and (3) an annual opportunity for designated firms to meet with Council staff to discuss and present relevant information as part of the annual review process. While any changes to the process must be cognizant of the sensitive, company-specific information that is being assessed and required to be kept confidential, it is important for the Council to be mindful of calls for greater transparency and to provide ways for the public and other interested parties to have greater insight and input into issues concerning U.S. financial stability. I fully supported the Council's efforts to increase transparency, and look forward to our continued study of possible further enhancements.

Thank you again for the opportunity to testify today, and I would be pleased to take your questions.

TESTIMONY OF
S. ROY WOODALL, JR.
INDEPENDENT MEMBER HAVING INSURANCE EXPERTISE

BEFORE THE U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES

"OVERSIGHT OF THE FINANCIAL STABILITY OVERSIGHT COUNCIL"

DECEMBER 8, 2015

Thank you, Chairman Hensarling, Ranking Member Waters, and members of the Committee for inviting me to appear before you today, alongside my colleagues.

This past September, I began the fifth year of my six-year term as a voting member of the Financial Stability Oversight Council (Council or FSOC). I am now the second-longest serving voting member of the Council, exceeded only by National Credit Union Administration Chair Matz.

As provided in the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), I serve as "*an independent member appointed by the President, by and with the advice and consent of the Senate, having insurance expertise*."[1] As you know, in the U.S., insurance is generally regulated by the States, and not by the Federal government. Thus, the Independent Member serves in effect as a "proxy" in the absence of a Federal insurance regulator, and as the sole voting member of the Council with an insurance-focused perspective. This complements the expertise brought to the Council by the nine other voting members: five Federal regulators of depository institutions, two Federal market regulators, one Federal housing regulator, and a Cabinet member.

The Council's Chairman, Treasury Secretary Lew, has often said that the Council is a young institution; and, as one would hope with any young institution, it is improving as it matures. I agree with him. That evolution of improvement is reflected in the Council's recent enhancement to its procedural transparency, its process for identifying and designating *systemically important financial institutions* (SIFIs), and its new emphasis

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203 (July 21, 2010), §111(b)(J).

on studying systemically risky activities that cut across several types of financial institutions. I believe the Council and its work can continue to benefit from further reforms as its members gain experience in carrying out its charges.

Accordingly, I think it is timely and beneficial for Congress to be examining the early work of the Council and to be exploring additional ways to improve the Council's procedures and structure. Secretary Lew noted recently that the Administration is open to conversations about technical changes or improvements to Dodd-Frank. This Committee's success in having Congress clarify Section 171 of Dodd-Frank, colloquially known as the *Collins' Amendment*, is but one example of the kind of important technical improvements with which Congress can assist.

Mr. Chairman, your letter of invitation states that the focus of today's hearing is broadly on the Council's agenda, operations, and structure. As to its structure, an area in need of attention by Congress, in my view, is a technical clarification of the scope of authority and responsibilities assigned to the position I now hold.

"Three Lines" in the Statute

Other than a few lines in Dodd-Frank,[2] the law does not set out specific duties and authorities for the position of the Independent Member, other than being a voting member of the Council. Unlike my colleagues who run Federal agencies, I have no other statute setting forth my duties and authorities. Dodd-Frank does not provide the Independent Member a source of funding, a budget process, or an office or staff. Accordingly, since being confirmed, I have had to resolve whether the position is meant to be full time, overcome hurdles to the efficient operation of my office's day-to-day operations, and struggle for resources. Beyond these operational distractions, and more significantly, I have had to endeavor to define and establish my evolving role relative to those of my fellow Council members and others by relying primarily on the Council's general authorities and

[2] Section 111(b)(1) of Dodd-Frank lists the voting members of the Council and includes "(J) an independent member appointed by the President, by and with the advice and consent of the Senate, having insurance expertise." Section 111(c)(1) sets the Independent Member's term: "The independent member of the Council shall serve for a term of 6 years … ." Section 111(i)(2) sets the level of the Independent Member's compensation.

mandates in a manner consistent with the overall intent of Congress and the relevant provisions of Dodd-Frank.

Some have pointed to the law's absence of specific duties and authorities for the Independent Member as a limitation and justification for their attempts to marginalize the position. For example, my role in staying abreast and lending expertise on insurance matters internationally – where developments are occurring at a rapid pace – has been in constant dispute. This dispute has continued in spite the provisions of Section 112 of Dodd-Frank which specifically entrust the Council with the duty of monitoring international financial regulatory proposals and developments involving insurance issues.

International Developments

In June of 2013, I initially testified before your Subcommittee on Housing and Insurance that I had been prevented from even being "in the room" with international insurance policymakers at the International Association of Insurance Supervisors (IAIS) in their discussions concerning possible systemic risks related to insurers and the insurance sector.[3] Despite the expressed desire of Subcommittee members from both sides of the aisle for the necessary collaboration that would allow the Independent Member to participate in insurance-related international discussions, obstacles persist. As noted in my subsequent September 29, 2015 testimony before the same Subcommittee, no progress had been made on this issue since my initial testimony.[4] Today, I continue to be thwarted from engaging in any meaningful non-public or consultative role at the international level.

The Government Accountability Office (GAO) touched on this ongoing dispute when it noted in a recent report to Congress that "…*U.S. IAIS members disagreed on whether the FSOC independent member with insurance expertise would be a relevant participant in the U.S. collaborative*

[3] Testimony of S. Roy Woodall, Jr., before the U.S. House Committee on Financial Services Subcommittee on Housing and Insurance, Hearing entitled: "*The Impact of International Regulatory Standards on the Competitiveness of U.S. Insurers*," (June 13, 2013).

[4] Testimony of S. Roy Woodall, Jr., before the U.S. House Committee on Financial Services Subcommittee on Housing and Insurance, Hearing entitled: "*The Impact of Domestic Regulatory Standards on the U.S. Insurance Market*," (September 29, 2015).

efforts...."[5] I am grateful that the representatives from two of the three U.S. IAIS members (the Board of Governors of the Federal Reserve System and the National Association of Insurance Commissioners) support allowing for the participation of the Independent Member at IAIS fora. Unfortunately, the third U.S. IAIS member maintains the position that Dodd-Frank does not specifically provide for the Independent Member to have any international role.

Just last month, the Bipartisan Policy Center and its Insurance Task Force issued a report that recommended that Congress should step in, if necessary, to resolve this ongoing dispute if the three U.S. IAIS members, referred to as "Team USA," continue to be unable to reach consensus:

> *"The independent member has expertise in the business of insurance and also authority in matters of systemic risk and insurance. Therefore, the independent member should be included on 'Team USA' and consulted by its other members on all issues in which systemic risk overlaps with insurance.*
>
> *"In addition, the independent member should have the opportunity to be fully informed on global debates on insurance oversight related to systemic risk and to offer his or her opinion on such issues in global forums. To that end, the Treasury Department, FIO, the Federal Reserve, and the NAIC should support giving the independent member formal access to any IAIS and FSB materials, meetings, and discussions related to insurance and systemic risk.*
>
> *"The task force sees real benefits, and no downside, to implementing this recommendation. It can be implemented without legislation, but Congress should step in if progress is not made to do so."*[6]

[5] United States Government Accountability Office, "International Insurance Capital Standards, Collaboration among U.S. Stakeholders Has Improved but Could Be Enhanced," p. 46 (GAO Report 15-534, June 2015).
[6] Bipartisan Policy Center, "Global Insurance Regulatory Issues: Implications for U.S. Policy and Regulation, p. 21 (November 2015).

It appears to me that after over three years of this continuing dispute, there is general agreement that the Council would benefit from the Independent Member's being a part of "Team USA." Indeed, I believe that to allow the Independent Member to continue to be blocked from participation in discussions regarding international insurance matters acts to interfere with Congress' overall intent that there should be an independent perspective within the Council in the carrying out of the Council's stated duties to monitor international financial regulatory proposals and developments involving insurance. Despite ongoing bipartisan calls for cooperation and my own best efforts, it appears that the current state of affairs can only be resolved by Congress.

Other Technical Corrections Needed

In addition to a possible clarification as to the Independent Member's participation in monitoring international insurance developments, other technical corrections to Dodd-Frank could further clarify Congressional intent as to the overall duties the Independent Member should perform, as well as confirm the contours of the authorities inherent in this unique, independent position. Technical corrections could bolster the independence of the Independent Member with clear statutory authorities that would guard against the possibility that employment, budgetary, staffing, and other pressures could be used to try to influence the effectiveness of the Independent Member. Finally, there are several other technical fixes or corrections that would address certain gaps in the *good government* functioning of this Federal position, such as who, if anyone, would fill the position in an acting capacity should the position become vacant, and whether the previously-confirmed occupant can continue to serve beyond an expired term until a new appointee is confirmed by the Senate. At present, in either situation, the seat for the insurance Independent Member would remain vacant.

That there are only "three lines" in Dodd-Frank is understandable, given that the Independent Member position was not proposed until near the end of the Conference Committee's deliberations, and the main purpose of the position was to fill the recognized insurance gap among the voting members of the Council. Now, however, Congress has the opportunity at this relatively early stage of the Council's operations, to consider clarifying specific duties and authorities for the position of the Independent Member. Doing so would ensure that expertise about the insurance sector of our economy has a true independent voice at the Council table and that the person in this position can more meaningfully and effectively contribute to the fulfillment of the important goals and best ensure success of the Council in carrying out its statutory responsibilities.

Conclusion

I appreciate this Committee's efforts and interest in considering reforms to the structure and operations of the Council. I suggest that the role of the Independent Member is worthy of attention. I do have a set of specific, concrete proposals for additional legislative technical corrections relating to the position of the Independent Member, which I would be happy to share with you. I look forward to continuing to work with this Committee and Congress on this and other matters.

Thank you and I look forward to answering any questions you may have.

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Questions for the Honorable Richard Cordray, Director, Consumer Financial Protection Bureau, from Congressman Patrick E. Murphy:

Question:

As you know, a very important part of the Bureau's authority is to work in particular on consumer financial challenges affecting military servicemembers and veterans through the Office of Servicemember Affairs. It is vital that we have an aspect of the Bureau working specifically on giving military families the education they need to make the soundest possible financial decisions, to monitor and respond to consumer complaints from military families, and to see that federal and state authorities coordinate their activities to improve servicemember consumer protection.

What steps have been taken to date to serve this uniquely important purpose of the Bureau in the area of consumer financial protection?

Response:

The Consumer Financial Protection Bureau is committed to ensuring that servicemembers, veterans, and their families receive a strong financial education in order to make better informed decisions regarding financial products and services. The Bureau's Office of Servicemember Affairs engages the military community, brings the issues and perspectives of military consumers into the Bureau, and works to improve consumer financial protection for servicemembers, veterans, and their families in a number of ways, including partnering with the Department of Defense and the Department of Veterans Affairs to provide opportunities for servicemembers to receive financial education relevant to their needs, monitoring complaints submitted by servicemembers, and coordinating consumer protection efforts among federal and state agencies related to consumer financial products and services offered to, or used by, military families. The Office also has a dedicated Veteran's Outreach Specialist, who works closely with Veteran Service Organizations and other stakeholders to disseminate information to the veteran community. Servicemembers, veterans and their families have made enormous sacrifices for our nation and deserve information on all the options available to them.

The Assistant Director for the Office is Holly Petraeus. Mrs. Petraeus routinely travels to military installations and speaks about the housing challenges faced by the military community. The Office of Servicemember Affairs conducts activities designed to reach servicemembers at the places where they live and work to make them aware of Bureau resources, including the Bureau complaint system, and to hear about their challenges and concerns. Between June 1, 2014 and December 31, 2015, the Office delivered consumer financial educational information and materials to more than 23,000 servicemembers, veterans, military families, and other stakeholders through live events. This effort included interacting with more than 5,300 active-duty servicemembers and National Guard personnel through leadership roundtables and town hall style listening sessions at 59 military installations. These sessions provided a forum for military personnel and their families to relay their financial challenges, and for the Bureau to

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provide educational information and materials to help them make better-informed financial decisions. In addition, Bureau staff have provided instruction at military consumer legal protection briefings at Judge Advocate General (JAG) schools for the Army, Air Force, and Marine Corps. The Bureau also provides training to legal assistance attorneys on military installations. These efforts help extend the Bureau's educational reach by leveraging the extensive consumer law mission of the JAG Corps, and ensuring that JAG legal assistance attorneys have up-to-date information on federal laws and policies affecting servicemembers in the consumer marketplace. The installations visited were representative of all five service branches of the armed forces and included regional commands, senior leadership development schools, wounded warrior care centers, military recruit training stations, and Unified Combatant Commands.

The Office of Servicemember Affairs is also working to reach veterans by building channels with veteran-support organizations that promote consumer protection. This channel-building effort has included providing briefings about Bureau resources and particular consumer financial protection issues to veterans service organizations; engaging with public policy groups to identify consumer issues for older veterans; and establishing relationships with groups looking for resources to address financial risk factors for veterans, including local veterans' courts, faith-based service providers, neighborhood organizations, and women's groups. It has included working with veterans' authorities to create distribution networks at the state and local levels for Bureau educational materials addressing veteran-specific issues as well as more general Bureau resources.

In 2013, the Office of Servicemember Affairs began hosting an ongoing series of virtual Military financial educator forums on consumer financial topics for service providers who deliver financial, educational, or legal counseling to servicemembers and their families worldwide. In January 2014, the Bureau began making the forums available as on-demand video trainings on the Bureau's website.[1] The Bureau has continued to expand its catalog of online courses, which now includes issues in debt collection, credit reporting and the military, veteran consumer issues, the consumer complaint process, and solutions for a troubled mortgage.

The Bureau has created a number of tools and resources to assist servicemembers and their families in making financial decisions on the Bureau's website, consumerfinance.gov.[2] For example, as part of the Bureau's interactive online tool, *Ask CFPB*,[3] the agency has developed "when you need it" answers to financial questions affecting consumers, including questions about financial products and services including credit cards, mortgages, student loans, bank accounts, credit reports, payday loans, and debt collection, and including answers to financial questions specifically affecting servicemembers.[4]

[1] *See* http://www.consumerfinance.gov/servicemembers/on-demand-forums-and-tools/.
[2] *See* http://www.consumerfinance.gov/servicemembers/.
[3] *See* http://www.consumerfinance.gov/askcfpb/.
[4] *See* http://www.consumerfinance.gov/askcfpb/search/?q=&selected_facets=audience_exact%3AServicemembers.

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From July 2011 through December 2015 the Bureau received over 48,000 complaints from servicemembers, veterans, and their family members, with mortgages and debt collection topping the cumulative volume of complaints for military consumers. Military consumers have received more than $1.5 million in monetary relief as a result of bringing their complaints to the Bureau, and we have helped many to obtain non-monetary relief. In addition, the Bureau has published four reports on complaints received from servicemembers, veterans, and their families.[5] Monitoring these complaints has allowed us to spot trends and make referrals that have resulted in enforcement actions, which have returned well over $100 million to servicemembers and veterans.[6]

The Bureau understands that military life has some extra challenges, such as deployment and frequent moves, and that those challenges can have powerful financial repercussions. Those who serve, or have served, our country should not have to worry about falling victim to unfair, deceptive, or abusive financial practices. The Bureau will continue to promote financial markets that work better for servicemembers, veterans, and their families.

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[5] *See* http://files.consumerfinance.gov/reports/servicemembers-2015-a-year-in-review/; http://files.consumerfinance.gov/f/201511_cfpb_snapshot-of-servicemember-complaints.pdf; http://files.consumerfinance.gov/f/201504_cfpb_snapshot-of-complaints-received-from-servicemembers-veterans-and-their-families.pdf; **and** http://files.consumerfinance.gov/f/201403_cfpb_snapshot-report_complaints-received-servicemembers.pdf.

[6] **For information on all of the Bureau's enforcement actions against companies targeting servicemembers, see** http://www.consumerfinance.gov/newsroom/?topic=enforcement+servicemembers.

Questions for the Record Submitted by Representative Patrick Murphy from the hearing entitled: "Oversight of the Financial Stability Oversight Council"

What is the status of the OCC's work on a rulemaking in this regard?

Following the publication of the initial proposal, a number of comments were received that raised complex and important issues regarding private flood insurance provisions included in the Biggert-Waters Act. The Agencies have been engaged in discussions to address these issues and likely will re-propose the rule. It is the Agencies' goal to have a rule issued in 2016.

How and to what extent specifically could a private flood insurance policy accepted by a regulated lending institution be substantively different than a standard flood insurance policy under the National Flood Insurance Program?

National banks and federal savings associations are currently able to accept private flood insurance policies. These policies may vary from a Standard Flood Insurance Policy (SFIP) in a variety of ways. For example, a policy might have different deductibles or cancellation provisions. However, OCC guidance provides that, to the extent a private policy differs from the SFIP, the differences should be carefully examined before a national bank or federal savings association accepts the policy as sufficient protection for a loan under the law.[1]

Why was implementation of the private flood insurance provisions in Biggert-Waters left out of the rulemaking, issued in July of 2015, to implement other provisions of the law?

The Agencies believed it was important to publish the escrow rule as soon as possible so that industry had adequate time to prepare for the escrow provision's statutory effective date of January 1, 2016. Because the comments on the proposed private flood insurance provisions raised many policy issues that required further review and analysis, the Agencies decided to issue the escrow rule separately from the private flood insurance proposal so that the escrow rule could be finalized without delay.

[1] See Q&A 63, *Interagency Questions and Answers Regarding Flood Insurance* in 2009 (74 FR 35914, July 21, 2009).

Representative Murphy (D-FL)

The failure of Freddie Mac to exercise clean-up call options on the issuance of mortgage-backed securities designated as Real Estate Mortgage Investment Conduits (REMICs) is a matter of concern to me. Although it retains one-percent clean-up call rights on nearly 2,700 REMIC contracts, Freddie has chosen not to exercise these call rights. If Freddie were to exercise these call options, revenue in the hundreds of millions could be generated in shared profit for taxpayers. With currently low interest rates, Freddie is leaving money on the table and foregoing an opportunity to return substantial revenue to taxpayers.

The failure of Freddie to exercise clean-up call options where it would benefit the taxpayers has led me to co-sponsor legislation (H.R. 1224) to require these options called where profit sharing would yield a return for taxpayers, and to preclude further clean-up call options in future contracts for sale of REMIC securities to investors.

Investors should not be surprised if a call is made where the call option is clearly articulated in the purchasing contract. In addition, with the amount of collateral that remains tied to these REMIC securities, the exercise of such calls would be consistent with the desire of the Federal Housing Finance Agency (FHFA) to transition Freddie Mac and Fannie Mae to a single security. Furthermore, the potential value of these calls to the taxpayer diminishes with each passing fiscal quarter.

With this in mind, why is Freddie Mac favoring certain investors over the taxpayer in its persistent failure to exercise these clean-up call options? Does FHFA plan to have Freddie exercise these call options in the near future? If not, why?

Freddie Mac's position in the creation of a REMIC is that of a trustee. As a trustee, Freddie Mac owes a fiduciary duty to all REMIC interest holders. Therefore, Freddie Mac is not permitted to act to the detriment of any interest holders for the purpose of Freddie Mac's own economic gain. As such, exercising the clean-up call as you proposed would require Freddie Mac to breach its duty as a fiduciary. The only economic gain permitted for Freddie Mac in this instance is to charge a nominal fee to offset its cost of exercising the clean-up call.

Freddie Mac also would not profit from a clean-up call because the Internal Revenue Code (IRC) at 26 USC 860D(a)(3) provides that in order to qualify for REMIC tax advantages, a security must have only one residual interest holder. If Freddie Mac, in exercising the clean-up call, were to participate in residual interest holder profits, Freddie Mac effectively would be a second residual interest holder. The tax consequences of disqualification from REMIC treatment to both Freddie Mac and its investors would be significant.

Finally, Freddie Mac would not profit from a clean-up call because a clean-up call would disrupt the market and incent investors to move away from Freddie Mac securities. Exercising the option could exacerbate the trading differences that already exist between Fannie Mae and Freddie Mac's securities, would be inconsistent with enterprise alignment initiatives (especially the Single Security initiative that is well along toward a target conclusion in 2018), and, ultimately, would run contrary to FHFA's mission to ensure market liquidity.

For the reasons stated above, FHFA, as conservator, cannot support Freddie Mac exercising the clean-up call options referenced in your question.