

# THE FINANCIAL SERVICES ROUNDTABLE

*Financing America's Economy*



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**RICHARD M. WHITING**  
EXECUTIVE DIRECTOR  
AND GENERAL COUNSEL

February 24, 2011

The Honorable Timothy F. Geithner  
Secretary  
U. S. Department of the Treasury  
1500 Pennsylvania Avenue, NW, Room 3421  
Washington, DC 20220

Dear Secretary Geithner:

The Financial Stability Oversight Council has proposed a rule to implement the process the Council will following in determining if a nonbank financial company may pose a threat to the financial stability of the United States and should be subject to supervision by the Federal Reserve Board. As proposed, the rule provides little insight into the determination process beyond the terms of section 113 of the Dodd-Frank Act. Yet, according to recent press reports and Congressional testimony it appears that the Council has given much more detailed consideration to the determination process.

Specifically, Bloomberg News has reported that the Council's staff has prepared an 80-page document addressing the determination process. Also, in recent testimony to the Senate Banking, Housing and Urban Affairs, FDIC Chairman Bair noted that the Council was looking at industry segments in order to develop measures of potential risk posed by firms and categories of firms.

We believe it is incumbent upon the Council to make these documents public so the process governing determination is more transparent. Indeed, the current rule stands in sharp contrast to President Obama's recent Executive Order on Improving Regulation and Regulatory Review, which states that regulations issued by federal agencies should "promote predictability and reduce uncertainty."

I have attached formal FOIA requests for this information, but would hope that the Council would realize the benefit of transparency for all parties and make this information public as soon as possible.

Sincerely,

*Richard M. Whiting*

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Executive Director & General Counsel

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February 24, 2011

FOIA Officer  
Department of the Treasury  
Washington, DC 20220

Re: Freedom Of Information Act Request, 5 USC 552

To Whom It May Concern:

This is a request under the Freedom of Information Act.

I request that a copy of the following documents be provided to me:

I. Any staff reports or memoranda that were produced or used by staff in arriving at segmentation of the nonbank sector into various categories such as (1) hedge fund, private equity firm and asset management industries; (2) the insurance industry; (3) specialty lenders; and (4) broker-dealers and futures commission merchants.

II. Any reports or memoranda describing or commenting upon methods used or adopted by the Council to measure the potential risk posed by these categories of firms or the firms themselves, and any calculation of the potential risk of either or both the categories or firms whether a preliminary or final calculation.

This segmentation and the commencement of development of measures of potential risk posed by the firms and categories were referenced by a member of the Council, FDIC Chairman Bair, in her testimony before the Senate committee on Banking Housing and Urban Affairs on February 17, 2011. Chairman Bair's comments were not lengthy and detailed, and served more to stimulate curiosity about the methodology and metrics than to fully inform. For a full understanding that can lead to more useful comments, the public needs to have access to the documents we have requested.

I am willing to pay reasonable fees for this request, although disclosure of the information to me is in the public interest because it is likely to contribute significantly to public understanding of the decisions to be made by the Oversight Council. It is my intention to disseminate this information among the members of the Financial Services Roundtable, a trade organization comprising many of the largest members of the financial services sector in the country. Such dissemination will provide important information about this methodology and the

metrics which will permit our members to make comments to the recently published proposed rule RIN 4030-AA00 that are more informed and therefore more useful to the Council than would be comments made without the benefit of a review of the information.

I ask that my request receive expedited processing because dissemination of the information and assimilation of its content will require some time by the members of our organization, and the comment period for the proposed rule terminates on February 25, 2011.

I can be reached at 202-589-2424 to discuss any aspect of my request.

Thank you for consideration of this request.

Sincerely,

*Richard M. Whiting*

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RE: Freedom of Information Act Request, 5 USC 552

To Whom It May Concern:

This is a request under the Freedom of Information Act.

I request that a copy of the following document be provided to me:

The 80 page report prepared by staff of the Financial Stability Oversight Council referred to in the attached story from Bloomberg News in which staff presents information about various sectors of the financial system.

I am willing to pay reasonable fees for this request, although disclosure of the report to me is in the public interest because it is likely to contribute significantly to public understanding of the decisions to be made by the Oversight Council. It is my intention to disseminate this report among the members of The Financial Services Roundtable, a trade organization comprising many of the largest members of the financial services sector in the country. Such dissemination will provide important information about these sectors which will permit our members to make comments to the recently published proposed rule RIN 4030-AA00 that are more informed and therefore more useful to the Council than would be comments made without the benefit of a review of the report.

Since the report has already received some dissemination in the form of the Bloomberg story, a story by a widely read business news source, broader dissemination and publication of the ideas in depth is even more essential to avoid use by our members of a third party interpretation of the staff report. While we respect the Bloomberg reputation, it is a brief story summarizing what appears to be a much more detailed and lengthy staff report. For a full understanding that can lead to more useful comments, the public needs to have access to the full report.

I request that my request receive expedited processing because dissemination of the report and assimilation of its content will require some time by the members of the public, and the comment period for the proposed rule terminates on February 25, 2011.

I can be reached at 202-589-2424 to discuss any aspect of my request.

Thank you for consideration of this request.

Sincerely,

*Richard M. Whiting*

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Attachment: Bloomberg News Article 2-17-11

# Bloomberg

## Hedge Funds May Pose Systemic Risk in Crisis, U.S. Report Says

*By Rebecca Christie and Ian Katz - Feb 17, 2011*

Hedge funds and insurers might threaten U.S. economic stability in a time of crisis, according to a report aimed at helping regulators decide which non-bank financial companies warrant Federal Reserve supervision.

An exodus of hedge-fund investors could “cause activity in some markets to freeze,” said the Feb. 3 report by staff of the Financial Stability Oversight Council. The report, obtained by Bloomberg News, also said the failure of a large insurance company could “result in dramatic and destabilizing actions being taken by investors.”

The 80-page report is a preliminary draft that, without making recommendations, offers a glimpse of issues regulators, including Federal Reserve Chairman Ben S. Bernanke and Treasury Secretary Timothy F. Geithner, will consider when deciding which firms should be designated “systemically important” and warrant central bank scrutiny. The council, created by last year’s Dodd-Frank financial overhaul law to prevent another financial crisis, may begin making those rulings by midyear.

Companies including Blackrock Inc., the world’s largest money manager, and lobbyists for the hedge-fund and mutual-fund industries have made the case to regulators they aren’t important enough to the financial system to merit the designation. Financial executives have said the costs of more regulation would put them at a disadvantage to their competitors.

### Possible Criteria

The report also details possible criteria, marked “confidential,” that regulators could use to monitor risks related to firms’ market share and portfolio holdings. Some of the information is already available through public filings. In other cases, the companies would have to document financial information never before released to regulators.

For example, regulators could require hedge funds to provide information on value-at-risk, a measure of risk relative to investor capital. A ratio that’s too high “can make a fund more vulnerable to runs,” the report said.

The oversight council has authority to make companies under its jurisdiction raise capital, increase liquidity and sell assets deemed too concentrated in one segment of the economy. The staff report’s considerations “are meant to provide context and an initial filter” for regulators as they consider individual firms, the document said.

AIG, GE Capital

Geithner, the council's chairman, suggested in September that such a list could encompass New York-based American International Group Inc., the bailed-out insurer, and GE Capital, a unit of Fairfield, Connecticut-based General Electric Co. that benefited from a government backstop for financial- company debt.

Steven Adamske, a Geithner spokesman, declined to comment on the document.

The FSOC report describes a \$40 trillion investment management industry that includes retirement programs, private equity firms and \$2.4 trillion in specialty funds that banks use to manage their assets. It also discusses the role of real estate lenders, broker-dealers and futures commission merchants.

Futures dealers who handle swaps, commodities and foreign exchange agreements could have a systemic impact if a "large default" set off a chain reaction within the industry, the report said. Such an event "could have devastating ramifications," and regulators should assess a firm's ability to cause such an event, the report said.

## **Insurance Failure**

In the case of insurance, a big company's failure could "reduce overall investor sentiment," the report said. It noted relationships between the life insurance and corporate bond sector, and between municipal bond markets and property/casualty insurers.

"Insurance itself is essential for many day-to-day activities, such as shipping goods, purchasing cars or extending mortgages," the report said. "A sector-wide crisis may have an adverse macroeconomic effect due to its role in the general conduct of economic activity."

The report said regulators historically had "little reliable information" on the "opaque" hedge fund industry, which plays "a significant role in U.S. financial markets." It said the industry has the potential for systemic impact and noted that about 200 advisers manage 80 percent of industry assets.

The Managed Funds Association, a Washington-based lobbying group whose members include D.E. Shaw & Co., Citadel LLC and SAC Capital Advisors LP, argued in a November letter to Geithner that hedge funds are too small to be systemically important, noting that the mutual-fund and banking sectors are much bigger.

## **Private-Equity Firms**

Private-equity firms could be a source of risk because of the "highly leveraged nature of their portfolio companies and their use of bridge loans," according to the staff report. It noted that out of the industry's roughly 2,000 managers, about 250 oversee more than \$1 billion in assets each.

The report also discussed retirement plans sponsored by non-profit organizations and state and local governments. “Many retirement plans are very large,” the document said. “Therefore, they could pose potential systemic risk.”

Money market funds, or MMFs, have systemic impact when they incur losses because the industry can be susceptible to runs, the report said.

In 2008, the \$62.5 billion Reserve Primary Fund became the biggest money-market fund and the first in 14 years to “break the buck,” meaning the value of a share fell below \$1 and investors faced losses. Reserve failed after investing in debt issued by Lehman Brothers Holdings Inc., the investment bank that declared the biggest-ever U.S. bankruptcy.

## **Money-Market Funds**

“Even a modest-sized MMF breaking the buck could, in principle, trigger a broad and damaging run,” the report said. “However, no individual MMF may warrant designation applying the factors” laid out in the Dodd-Frank financial overhaul law.

So-called liquidity funds, or unregistered money-market funds, suffered large investor withdrawals in 2007, the report said. “Although these runs may have been disruptive, they do not appear to have become systemic.” If the funds grow rapidly there could be “greater potential to pose systemic risk in the future.”

The staff report says some types of firms, such as venture capital funds and community development financial institutions, aren’t likely to pose risks because they generally don’t make leveraged bets. Closed-end funds, a type of investment company that issues equity securities, don’t offer investors redemption rights and therefore “primarily raise investor-protection concerns rather than potential systemic consequences,” the report said.

Thrift holding companies may warrant further study, the report said.

In addition to Geithner and Bernanke, the council’s 10 voting members include the chairmen of the Federal Deposit Insurance Corp., the Securities and Exchange Commission and the Commodity Futures Trading Commission.

To contact the reporters on this story: Rebecca Christie in Washington at [rchristie4@bloomberg.net](mailto:rchristie4@bloomberg.net); Ian Katz in Washington at [ikatz2@bloomberg.net](mailto:ikatz2@bloomberg.net)

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