United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, DC 20510–6075

May 23, 2016

The Honorable Jacob J. Lew
Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Dear Secretary Lew:

As you are aware, a major cause of the global financial crisis of 2008 was the failure, or near-failure, of nonbank financial institutions. Many nonbanks took unacceptable risks prior to 2008 that resulted in catastrophic losses during the crisis, including creating dangerous exposures for the regulated banking system. American taxpayers were subsequently forced to fund bailouts to, or acquisitions of, several nonbanks and their counterparties, including the investment bank Bear Stearns and the insurance conglomerate American International Group, because their potential failures threatened the entire financial system, and with it the rest of the economy.

With some exceptions, nonbank institutions are not subject to robust prudential regulation. The nonbank financial system developed, in part, because lightly regulated or unregulated institutions sought to engage in profitable, but risky, financial activity while, at the same time, avoiding comparable regulations and limitations associated with traditional banking. The Dodd-Frank Wall Street Reform and Consumer Protection Act (Wall Street Reform) created the Financial Stability Oversight Council (FSOC) to monitor the risks posed by nonbank financial companies, and to address these risks through enhanced supervision and regulation. In order to evaluate the effectiveness of Wall Street Reform, regulators must properly monitor the behaviors and activities that result from its regulations, and ensure that there are no significant oversight gaps.

FSOC's efforts to date, in both examining financial activities and designating financial firms, have been analytical and thorough. However, I am concerned that recent legislative efforts and legal developments could jeopardize our ability to address these risks in the future, leaving our economy vulnerable to another financial crisis. To that end, I would appreciate your responses to the following questions related to your efforts, as the Chair of the FSOC, to monitor and address the risks posed by nonbank financial companies:

1. What processes does FSOC have in place to systematically identify and monitor potential threats to financial stability, including potential threats arising from the migration of financial activities to less-regulated entities?

2. Are there any current legislative proposals or legal actions that may impair the FSOC's ability to effectively respond to threats to financial stability?

3. Are there additional authorities that would improve the ability of FSOC to respond to threats to financial stability?

4. FSOC recently highlighted a number of potential risks that may arise from asset management products and activities, including potential risks related to the use of leverage by hedge funds. What tools do FSOC and/or its member agencies have to analyze and address any potential threat to financial stability here?

Thank you for your attention to this important issue. The financial crisis demonstrated that financial stability is crucial to promoting a healthy economy and helping working-class Americans. I commend your efforts to monitor the nonbank financial sector and encourage you to continue working to ensure that the migration of risks to nonbank financial companies does not weaken the effectiveness of Wall Street Reform.

Sincerely,

Sherrod Brown

Sherrod Brown
United States Senator

Cc: The Honorable Janet L. Yellen
The Honorable Thomas J. Curry
The Honorable Richard Cordray
The Honorable Mary Jo White
The Honorable Martin J. Gruenberg
The Honorable Timothy G. Massad
The Honorable Melvin L. Watt
The Honorable Deborah Matz
The Honorable S. Roy Woodwall, Jr.
The Honorable Richard Berner