



HOUSE FINANCIAL SERVICES COMMITTEE HEARING

OVERVIEW

For questions on the note below, please contact [Kwon Park](#) at (202) 547-3035.

Yesterday, the House Financial Services Committee held a [Full Committee hearing](#) entitled "[The Annual Report of the Financial Stability Oversight Council.](#)"

Key Takeaways

- Jacob Lew, Secretary of the Treasury, said that GE Capital's decision to de-designate itself from being a systemically important financial institution (SIFI) as determined by the Financial Stability Oversight Council (FSOC or Council) was a strategic business plan. He also indicated that the court decision to overturn MetLife's designation is flawed.
- Lew opposed the Financial CHOICE Act (legislation sponsored by Chairman Hensarling), declaring that rolling back Dodd-Frank would be harmful to financial stability. He specifically opposed the provisions to restructure the Consumer Financial Protection Bureau (CFPB), and to replace risk weighted capital ratios.
- Many Republican members claimed that the cash payment to Iran by the Obama administration was a ransom payment and questioned Lew about whether he could trace the funds so Iran does not fund terrorist activities. Many Democratic members asserted that the Republicans are making another politicized attempt to undermine the President and his administration.

SUMMARY

Opening Statements and Testimony

[Committee Chairman Jeb Hensarling \(R-TX\)](#)

- FSOC's 2016 annual report is basically identical to its 2015 annual report, breaking little new ground and adding little value.
- Since the passage of Dodd-Frank, America is losing, on average, one community financial institution a day as they are crushed by the federal regulatory burden, and the big banks have only grown bigger.
- Since President Obama took office, the national debt has increased by 84%. The Congressional Budget Office noted that the President's 2017 budget would add nearly \$7.5 trillion to the national debt, and warned that such high and rising amounts of debt have serious, negative, long-term consequences for the economy and would constrain future budget policy – yet, FSOC remains silent, and thus, loses credibility.

- FSOC's annual report is disappointing and the Committee's focus should be on its frightening and unconstitutional powers. The Council's SIFI designation authority is taking our financial system one step closer to a government-controlled utility model – this must change.
- FSOC's highly-politicized structure and penchant for secrecy are emblematic of a shadow regulatory system that is antithetical to American democratic principles.
- The Financial CHOICE Act will bring economic growth for all and bailouts for none. It ends bailouts by removing bailouts for bankruptcy, and holds FSOC accountable to its sole task of monitoring emerging threats to our financial system. The bill is undoubtedly a better way forward.

Ranking Member Maxine Waters (D-CA)

- The U.S. Census reported that median household income increased by more than 5% last year, and that the poverty rate declined by 1.3 percentage points.
- We need to be doing more, especially to address the wealth gap, particularly for African American and Hispanic households whose economic security was devastated by the financial crisis.
- The Wells Fargo scandal begs the question of what further reforms may be needed, and yet, this Committee advocates deregulation and wants to give Wall Street more opportunities to write the rules of the game.
- FSOC is effective in preventing companies from growing too large or risky. For example, GE Capital voluntarily agreed to shrink itself and sell much of its consumer financial business – making it smaller, safer, and less likely to cause systemic risk.
- The Financial CHOICE Act would put Wall Street back in the driver's seat and leave consumers and investors to fend for themselves. Rather than harmful roll-backs, we should support further reforms and explore how we can do more to prevent scandals like the one at Wells Fargo.

Randy Neugebauer (R-TX)

- FSOC has failed to exercise its authority to ensure that heightened prudential standards are applied fairly to bank holding companies, failed to implement a fair and transparent process for designating non-banks, and failed to identify real market concerns (i.e. reduction of bond market liquidity).

Scott Garrett (R-NJ)

- FSOC's legacy will be remembered by secrecy and its continued refusal to answer the most basic and simple questions that would provide transparency to this Committee, Congress, and the American public. The MetLife court decision confirms this statement.

The Honorable Jacob J. Lew, Secretary, Department of Treasury (Treasury)

- Dodd-Frank has addressed serious weaknesses that contributed to the financial crisis and has restored confidence in the financial markets. Since its enactment, there has been sustainable economic recovery – the poverty rate is down and household incomes are rising.
- The recent enforcement actions against Wells Fargo by the OCC and the CFPB remind us of the ongoing need for robust regulatory protections. The CFPB ensures fair, transparent, and

competitive markets. The agency is fulfilling its statutory mission. As for the SEC, it is critical to have a strong executive compensation rule.

- FSOC's annual report focuses on 12 key areas, such as cybersecurity and risks associated with asset management products and activities.
 - Cybersecurity: government agencies and the private sector should continue to work to improve and enhance information sharing, baseline protections, and implement response and recovery planning.
 - Risks associated with asset management products and activities: we should continue to evaluate implications to financial stability and update the review of potential risks in this area, particularly liquidity redemption and leverage risks.
- Congress should not support legislation (Financial CHOICE Act) that rolls back Dodd-Frank.

Discussion

Merchant Banking Authority

Neugebauer (R-TX): The Fed made a recommendation to repeal banks' merchant banking authority – did the Fed consult Treasury on the recommendation? Do you agree with the recommendation - is merchant banking too risky? *Lew*: The Fed made an independent recommendation. Dodd-Frank made distinctions between different types of activity, and we will evaluate the recommendation for inconsistencies. This repeal requires legislative action. We recently received the report and are still analyzing it.

SIFI Designation

Luettkemeyer (R-MO): Many critics claim the \$50 billion threshold is arbitrary – do you agree that size should not be the only factor to determine SIFI designation? What is the cost of SIFI designation (or de-designation)? *Lew*: The process of SIFI designation via a firm by firm review requires a completely different process than the current practice. The real issue is risk and size is a big indicia of risk.

Meeks (D-NY) and Maloney (D-NY): Does FSOC need to provide greater transparency in the designation process? Is the only way to de-designate to divest and gut one's business? *Lew*: GE Capital de-designated because it wanted to focus on its industrial business rather than its financial business. GE made this business decision due to its strategic business plan moving forward – it had little to do with designation.

Lynch (D-MA): How has the MetLife court decision changed FSOC's analysis? *Lew*: We believe the court decision is flawed.

Liquidity

Pearce (R-NM): What is the impact of monetary policy on bond liquidity (i.e. Virtu revealed it will not trade in bond markets because the market is too unstable)? Why is monetary policy not included in the annual report? *Lew*: I speak to Fed Chair Yellen about monetary policy.

Money Market Funds

Rothfus (R-PA): Are you aware of the flow of capital from money market funds into government funds due to the new proposal? *Lew*: The impacts from the proposal are not as dramatic as reported.

Cybersecurity

Maloney (D-NY): Can cyber threats to the SWIFT system undermine international payments and pose systemic risk? *Lew:* Cyber threats exist and we need coordinated efforts to implement best practices, share information, and update systems.

Lynch (D-MA): Given the volume of transactions between central banks and banks via SWIFT, does the theft of \$81 million cause concerns? *Lew:* We must focus on efforts to enhance cybersecurity.

Financial CHOICE Act

Hinojosa (D-TX): Discuss how replacing more complex risk weights with other measures will make sense for community banks engaged in traditional banking activities? What is the impact of the Financial CHOICE Act on financial stability? *Lew:* We are looking for ways to simplify reporting for smaller banks. Rolling back Dodd-Frank would be a mistake for the financial system and economic stability.

Luetkemeyer (R-MO): What are your feelings about smaller institutions being acquired because they cannot comply with regulations? *Lew:* We continue to craft/revise regulations so they are not as burdensome on smaller institutions.

Huizenga (R-MI): According to a report by Lawrence Summers, Dodd-Frank has not worked - agree? *Lew:* No, we have to look at the entire picture of the financial system.

Financial Stability Board

Royce (R-CA) and Love (R-UT): Why utilize FSB recommendations when it lacks due process? Why are U.S. regulators deferring to FSB's agenda? *Lew:* FSB simply shapes policy and makes recommendations. They are not binding but help bring other countries in line with U.S. standards. The U.S. drives the FSB's agenda to improve financial stability around the world.

CFPB

Velazquez (D-NY): The Financial CHOICE Act politicizes CFPB's appropriations process, repeals the single director structure, and brings significant roadblocks to its ability to write rules and enforce them – what will these proposed changes do to American economic security? *Lew:* The proposed changes can pose a threat to financial stability. The CFPB should remain independent so abusive practices by financial institutions can be dealt with.

Barr (R-KY) and Stutzman (R-IN): Are small community banks and credit unions competitive with large banks like Wells Fargo? It seems the CFPB failed to do its job in detecting the Wells Fargo's fraudulent activities. *Lew:* Competition is good. The CFPB reacted correctly to the Wells Fargo situation - but for the agency, there would have been no penalties.

Tax Reforms

Schweikert (R-AZ) and Perlmutter (D-CO): The 385 proposal deals with corporate inversions – what is its status, and will firms have a way to grandfather deals once the rule is final? *Lew:* The rule makes it harder for U.S. companies to avoid U.S. tax liability, and the best way to deal with inversions is through tax reforms. The proposal has a broader impact than intended so we are working to address the consequences.

Poliquin (R-ME): The Obama administration introduced taxing college savings plans and withdrew them after public outcry – do you plan to tax retirement savings? *Lew:* No.

Excessive Compensation Rule

Garret (R-NJ): You were senior officer of a group at Citi bank that later collapsed and was charged with defrauding consumers – has your pay been clawed back from your time as COO? Were you paid for joining the government through your bureaucratic parachute? *Lew:* I was not subject to any action and no one asked any questions. My job was focused on administrative activities and not risk-based products – you have no idea what my job was and there was nothing wrong with my compensation.

Housing Reform

Heck (D-WA): What is unstable about the status quo of housing markets? *Lew:* We continue to have a housing system where most mortgages are government backed. It would be good to have a venue for private capital to flow into the housing market and bear the risks, rather than being fully dependent on a government backstop. The challenge is passing legislation permitting the development of a structure that would meet these criteria.

Iran Settlement

Hensarling (R-TX): The recent \$1.7 billion payment made by the Obama administration to Iran – can you trace the money so it is not used for terrorist activities? Who authorized the cash payment and did you object to the payment? Were two wire transfers made to Iran? *Lew:* The payment to Iran was related to a Hague tribunal settlement. The facts are included in a report provided to Congress, and we complied with U.S. laws. This was not a ransom payment, but a settlement from a contractual agreement. The payment went to the central bank of Iran, and since it was made, we have not seen increased terrorist funding in Iran. Two wire transfers were made before and after the cash payment to a European bank account held by the Iranian government.

Waters (D-CA): The ransom story is another political attempt to undermine the President. Trump engages in business deals with Putin and is absolutely ridiculous. Shame on the Republican party.

Neugebauer (R-TX) Barr (R-KY), and Duffy (R-WI): Are there serial numbers on cash given to Iranians for tracking purposes? Are wire transfers to Iran possible? Can you guarantee that these funds will not be used to fund terror? *Lew:* Not sure - will get back to you. The wire transfers went to a European bank account, not to Iran directly. We will try our best to track those funds.

Huizenga (R-MI): Did you support the license to finance aircrafts to Iran? *Lew:* The license was a joint comprehensive action. The U.S. financial system remains closed to Iran, and this is the only exception.

Meeks (D-NY): Do you believe this was a smart deal by the administration (as they leveraged the payment in exchange for hostages)? *Lew:* Yes. The U.S. was at risk of more than \$5 billion taxpayer dollars to settle this claim.

Scott (D-GA): The President should work with Congress on negotiations as we have a close relationship with Israel. *Lew:* Israeli aid is important. Some in the Israeli government might disagree with you that this deal was bad.

Pittenger (R-NC): Did the Treasury's Office of Financial Intelligence raise concerns about the method of payment to Iran? *Lew:* Treasury acted according to law. I will not describe who told me what.

Poliquin (R-ME): Agree with the State Department that Iran sponsors terrorism? Agree that untraceable cash is the currency of terrorism? *Lew:* Yes, cash in the private economy is a big problem.

Brexit

Maloney (D-NY): Does Brexit potentially bring risks to the financial system? *Lew:* We are better equipped to deal with issues due to financial reforms (Dodd-Frank).

U.S. Armenian Tax Treaty

Sherman (D-CA): Will you make the U.S. Armenian tax treaty a priority? *Lew:* We look at tax treaties through an economic tax policy lens and ask whether we can avoid double taxation. There is no evidence of double taxation.