



## FSOC OPEN SESSION

### OVERVIEW

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

Yesterday, the Financial Stability Oversight Council (FSOC or Council) held an [open session](#) that included: 1) an update on the work of the Alternative Reference Rates Committee (ARRC); 2) an update on the Council's review of asset management products and activities; and 3) revisions to the Council's regulations under the Freedom of Information Act (FOIA), in accordance with the FOIA Improvement Act of 2016.

### Key Takeaways

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- The ARRC is working to identify one or more alternatives rates, develop a plan to implement the selected rate, and make a recommendation on an alternative to LIBOR sometime next year.
- Staff from the Council's hedge fund (HF) working group described the risks HFs may pose to the financial system, including the disruption caused by forced selling and transferring risk to counterparties. The group made several recommendations regarding data collection, such as improving data sharing among agencies and collecting bilateral repo data.
- Several Council members agreed that the FSOC needs to continue to study HF activities and to collect additional data of their activities.

### SUMMARY

#### Update on the Work of the Alternative Reference Rates Committee (ARRC)

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##### *Jerome Powell, Federal Reserve (Fed)*

ARRC has focused on two tasks: 1) strengthening LIBOR; and 2) identifying alternatives to LIBOR. FSOC has recognized that banks could leave the LIBOR panel, which would adversely impact U.S. dollar LIBOR.

Most contracts that use LIBOR do not specify the consequences if there is no alternative to LIBOR. ARRC is working to identify one or more alternative reference rates, to develop a plan to adopt a rate, and to select a backup rate.

ARRC expects to make a recommendation on an alternative reference rate next year. ISDA has agreed to work with ARRC on implementing a backup reference rate.

#### Comments by FSOC Members

*Jacob J. Lew, Secretary of the Treasury (Treasury) & Chair of FSOC:* LIBOR plays a critical role in our financial system. Questions about the integrity of LIBOR can have significant, adverse effects on the financial system. Any transition from LIBOR to a new rate will be complex and will take time.

### **Update on the Council's Review of Asset Management Products and Activities**

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#### ***Jonah Crane, Senior Advisor, Treasury***

No single regulator has the data to evaluate overall risk posed by HFs. The relationship between leverage and risk is not simple. On average, most HFs do not employ much leverage, but the leverage employed is focused in a small number of funds. The working group has focused on two particular effects of HFs: 1) disruption caused by forced selling; and 2) the transferring risk to counterparties.

Leverage means small price changes can lead to margin calls and require HFs to rapidly liquidate positions. These forced sales could cause a price change in asset prices and impact trading or funding in markets. Market risk has been mitigated by central clearing and minimal margin requirements, but some of the largest banking institutions have large exposure to HFs.

The working group made several recommendations regarding data, including: improved data collection and sharing among agencies and the need to collect more granular exposure data and bilateral repo data.

#### **Comments by FSOC Members**

*Lew:* FSOC established the working group so that the Council could better understand HF activities and the risks they pose to financial stability. FSOC member agencies must continue to work together to implement suggestions made by the HF working group, so that should risks develop to where action is required, we can identify them together and respond in a timely fashion.

*Janet Yellen, Chair, Fed:* We need to develop more risk-sensitive metrics so that we can better assess risks posed by HFs – especially HFs holding less-liquid assets. Permanent data collection on bilateral repo markets and amendments to Form PF are important steps to address risk posed by HFs.

*Martin J. Gruenberg, Chair, FDIC:* Leverage appears to be concentrated in a small number of HFs.

*Mary Jo White, Chair, SEC:* Leverage can be a useful component of a HF's investment strategy, but it is only one of many factors to measure its risk. The relationship between leverage and risk cannot be simplified to a single metric or data point.

*Timothy Massad, Chair, CFTC:* Agencies need to develop better metrics for data collection and continue to address gaps in data, particularly in regard to the lack of repo data. It is also important to distinguish between simple, cleared instruments versus complex, uncleared instruments.

### **Revisions to the Council's Regulations under FOIA**

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FSOC unanimously approved revisions to its regulations under FOIA, in accordance with the FOIA Improvement Act of 2016.