NOSSAMAN LLP | Memorandum

TO: Susan Wyderko

FROM: Shelby Hagenauer

DATE: January 30, 2014

RE: Senate Banking Hearing with Office of Financial Research

Please find below a summary of the January 29, 2014 Senate Banking Subcommittee on Economic Policy hearing on "Monitoring Systemic Risk: The Annual Report and Oversight of the Office of Financial Research (OFR)," which lasted about an hour, with two rounds of questioning of the only witness – Richard Berner, Director of OFR.

Senators in attendance: Chairman Jeff Merkley (D-OR), Ranking Member Dean Heller (R-NV), Elizabeth Warren (D-MA), David Vitter (R-LA), Pat Toomey (R-PA).

The September 2013 OFR report (http://www.treasury.gov/initiatives/ofr/research/Documents/OFR_AMFS_FINAL.pdf) was the primary topic of discussion; secondary was the issue of the US repo market. This memo will exclusively discuss the hearing's focus on the report.

Senator Heller first asked if Berner believes the OFR study should be solely relied upon as the Financial Stability Oversight Council (FSOC) considers the issue of whether asset management firms should be considered Systemically Important Financial Institutions (SIFIs). Berner said no, and repeated what was his theme throughout the hearing – the report is one ingredient in FSOC deliberations, I am a non-voting member of the council, and our report is designed to provide them with information. Heller also asked about SIFI designation as it relates to the size of a firm versus the activities of the firm, and Berner agreed that activity should be the focus. Heller also pushed on the issue of the report's admission that significant gaps in data prohibited full analysis, asking if it is responsible to publish a report without all the data. Berner commented that the report indicated some metrics are estimates because of data gaps, and they wanted to focus on areas like separately managed accounts and securities lending transactions where data is scarce and transactions could be potential problems. In response to questions, Berner also said they did not ask asset management firms to provide data, but they engaged with trade groups and different asset management firms to talk about the nature of their business, as well as talking with the Securities and Exchange Commission (SEC) since almost the start of the research since they are the primary regulator.

Senator Warren focused her remarks on the importance of data collection and whether OFR is able to get the data they need from the prudential regulators they work with. Berner said that thus far, there are MOUs in place with the regulators related to information and procedures in place for dealing with what is often confidential data. Berner also told Warren that OFR has not used its subpoena power to obtain data from financial institutions.

Senator Vitter stated his concerns about a possible push to designate asset management firms as SIFIs. He thought it was interesting that in this case, the normally very divergent views of both Peter Wallison of the American Enterprise Institute and former Chairman Barney Frank merged in saying that it does not make sense. Vitter also expressed concern that the study is the prelude to a potential SIFI decision. Berner repeated his earlier comments that OFR's job is to identify risks, and FSOC's job is also to work on identifying risk, but to propose and implement any remedies. The study focused on activities, not firms, so it could not be used as the sole basis for any decision. Additionally, an analysis of a particular firm would need to be done before a designation could be considered, since this report was just on activities. They are concerned about opacity in separately managed accounts, which they think are about 40% of assets under management.

Vitter also took Berner to task about the process of gathering information and putting together the report, sharing that firms involved and others including Members of Congress have been frustrated with what they consider to be OFR's "black box approach" to the report. He has heard complaints that meeting participants got no reaction from OFR during meetings. Berner pushed back, saying they engaged with 10 large asset management firms during the study and sent teams to the firms, and he personally visited with 5-6 of them. He found the meetings constructive, and welcomed continued engagement with the industry.

Senator Toomey, who is not on the subcommittee, followed up on the issue. He commented that systemic risk by nature is transmittable throughout other institutions, and asked what those transmission mechanisms would be with respect to asset management. Berner said that is why OFR is focused on activities, because if an asset manager would be hit by an external shock, it could transmit or amplify to the rest of the system because of activities it has undertaken. And if multiple asset managers are doing similar things, that could create a potential systemic threat. He also responded that many activities may be regulated by ERISA or the SEC, but the regulation of activities in separately managed accounts differs from the regulation of 40 Act accounts, potentially creating more risk.

Senator Heller followed up on this theme as the second round of questions started, asking if one asset management firm is designated as a SIFI, whether clients would just move from that firm to another. Berner returned to his earlier comments that they are looking at activities taken by a variety of firms, so they are widespread.

Heller also pushed Berner about whether he is willing to commit that future OFR research on this would be made public. Berner said that if FSOC asks them to do work, it is their property, so FSOC would have to make the judgment if a work product is predecisional or has confidential data. He was very clear, however, that if it is appropriate for OFR to release information, data, or analysis that bears on the question of financial stability that they will do so.

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