DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

May 18, 2020

Hart W. Wood
American Oversight
1030 15th Street NW
Suite B255
Washington, DC 20005

VIA EMAIL

Re: *American Oversight v. United States Department of the Treasury et al*, Case No. 20-cv-00691; Production

Counsel:

This letter describes the May 18, 2020 production from the U.S. Department of the Treasury (Treasury) in the above-referenced Freedom of Information Act litigation.

Treasury has conducted a search in response to American Oversight's October 22, 2019 FOIA Request (2019-10-133). Treasury identified eight documents (totaling twelve pages) as being responsive to this request. Six pages of these documents are being released in full. Portions of the remaining pages are being withheld pursuant to Exemption 6 of the FOIA as the documents contain information the release of which would clearly constitute an unwarranted invasion of personal privacy. The production is numbered UST 000001 – 000012.

If you have any questions concerning this production or a related matter, please contact Assistant United States Attorney Alan Burch at (202) 252-2550 or Alan.Birch@usdoj.gov.

Sincerely,

Digitally signed by Ryan A. Law
Date: 2020.05.18 16:41:26 -04'00'

Ryan Law
Office of Privacy, Transparency, and Records
U.S. Department of the Treasury

cc: Alan Burch, AUSA (via email)

Enclosure

RE: Leveraged Lending Guidance: Follow Up to May 26, 2017 Meeting

From: "Phillips, Craig" <"/o=ustreasury/ou=exchange administrative group (fydibohf23spdlt)/cn=recipients/cn=phillipscr">
To: "Coffey, Meredith" [redacted]@lsta.org>
Cc: "Ganz, Elliot" [redacted]@lsta.org>
Date: Fri, 26 May 2017 16:35:36 -0400

Meredith,

Thanks for following up so quickly. I look forward to further discussion and review on the CLO topic which seemed reasonable to me.

Craig

Craig S. Phillips
Tel: 202-622-2997
craig.phillips@treasury.gov

From: Coffey, Meredith [mailto[redacted]@lsta.org]
Sent: Friday, May 26, 2017 3:35 PM
To: Phillips, Craig <Craig.Phillips@treasury.gov>
Cc: Ganz, Elliot [redacted]@lsta.org>
Subject: Leveraged Lending Guidance: Follow Up to May 26, 2017 Meeting

Mr. Phillips,

It was a pleasure meeting with you. As an initial follow up, we are attaching a description of key tenets of the Leveraged Lending Guidance and its impact on the leveraged loan market.

Do note that we flag two key issues: i) the designation of investment grade companies as leveraged companies, and ii) the prohibition of banks originating or investing in non-pass credits. Both are disruptive.

The attached document is an initial description that we wanted to deliver to you quickly. We will follow up next week with a more formal analysis on how the Leveraged Lending Guidance does or does not conform with the Core Principles.

Kind regards,

Meredith Coffey
Elliot Ganz

Meredith Coffey
LSTA
EVP – Research & Regulation
W: [redacted]
C: [redacted]
[redacted]*@lsta.org*
https://hyperlink.services.treasury.gov/agency.do?origin=www.lsta.org

RE: Followup on Core principles and EO 13772

From: "Phillips, Craig" <"/o=ustreasury/ou=exchange administrative group (fydibohf23spdlt)/cn=recipients/cn=phillipscr">
To: "Seidel, Joseph L." <[redacted]@credit-suisse.com>
Cc: "Hammer, Sarah" <sarah.hammer@treasury.gov>, '[redacted]@treasury.gov>, "Chin, Brian" [redacted]@credit-suisse.com>, "Paul, Douglas" [redacted]@credit-suisse.com>, "Ryan, Peter J." [redacted]@credit-suisse.com>
Date: Fri, 26 May 2017 17:30:47 -0400

Joseph,

Thanks for the input – much appreciated.

Craig

Craig S. Phillips
Tel: 202-622-2997
craig.phillips@treasury.gov

From: Seidel, Joseph L. [mailto:j[redacted]@credit-suisse.com]
Sent: Wednesday, May 24, 2017 6:13 PM
To: Phillips, Craig <Craig.Phillips@treasury.gov>
Cc: Hammer, Sarah <Sarah.Hammer@treasury.gov>; [redacted]treasury.gov>; Chin, Brian [redacted]@credit-suisse.com>; [redacted]@credit-suisse.com>; Ryan, Peter J. [redacted]@credit-suisse.com>
Subject: Followup on Core principles and EO 13772

Hi Craig.

As follow-up to the discussions we have been a part of at Treasury since March, pls find attached a cover letter from Brian Chin as well as CS views & recommendations on a series of financial regulation issues that were covered in the meetings we attended. We are offering a series of issue briefs with our suggestions in a Treasury "Green Book" format that hopefully may still be somewhat timely and helpful to supplement the relatively more voluminous submissions you have received from trade groups and others.

We cover the 9 distinct issue areas below and will send a follow-up on securitizations separately:

- Capital and liquidity ring-fencing associated with the Intermediate Holding Company (IHC) requirement;
- The Comprehensive Capital Analysis and Review (CCAR) process;
- Leverage ratio requirements;
- Total Loss Absorbing Capacity (TLAC) and Long-Term Debt (LTD) rules;
- Recovery and resolution planning/living wills;
- The implications arising from designation as part of the Federal Reserve's Large Institution Supervisory Coordinating Committee (LISCC) portfolio;
- Leveraged lending guidance;
- Derivatives regulation; and
- The Volcker Rule

Please let me know if any questions or we can provide you more info.

Thx. Joe.

Joseph L Seidel
Managing Director & Senior Counsel
CREDIT SUISSE | Head, U.S. Public Policy
(o) [redacted]
(c) [redacted]

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Please access the attached hyperlink for an important electronic communications disclaimer:
https://hyperlink.services.treasury.gov/agency.do?origin=http://www.credit-suisse.com/legal/en/disclaimer_email_ib.html
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RE: (De)Regulation watch: Notes from Treasury's response to POTUS and SIFMA/TCH Prudential Regulation Conference

From: "Phillips, Craig" <"/o=ustreasury/ou=exchange administrative group (fydibohf23spdlt)/cn=recipients/cn=phillipscr">
To: "Seidel, Joseph L." [redacted]@credit-suisse.com>
Date: Fri, 16 Jun 2017 18:41:20 -0400

Joe,

Thanks for sharing these reports.

Craig

Craig S. Phillips
Tel: 202-622-2997
craig.phillips@treasury.gov

From: Seidel, Joseph L. [mailto[redacted]@credit-suisse.com]
Sent: Thursday, June 15, 2017 12:54 PM
To: Phillips, Craig <Craig.Phillips@treasury.gov>
Subject: FW: (De)Regulation watch: Notes from Treasury's response to POTUS and SIFMA/TCH Prudential Regulation Conference

Hi Craig.

Good to talk yesterday. As mentioned yesterday, pls see below the email report our FIG IB Coverage team put out yesterday after the TCH Conference to their external clients (including heavy concentration of Regional Bank CEOs & CFOs). In addition, pls find attached the latest CS Equity Research pieces (Multinational Banks & Specialty Finance sectors) on the Treasury Report. In general, very positive feedback both on the substance and the level of detail.

Good stuff and look forward to talking soon.

Thx. Joe.

Joseph L Seidel
Managing Director & Senior Counsel
CREDIT SUISSE | Head, U.S. Public Policy
(o) [redacted]
(c)

From: MacGown, David W. (BEAI)
Sent: Wednesday, June 14, 2017 3:33 PM
To: MacGown, David W. (BEAI)
Subject: (De)Regulation watch: Notes from Treasury's response to POTUS and SIFMA/TCH Prudential Regulation Conference

Good afternoon,
As promised, the US Treasury on Monday released the first in a series of responses to the POTUS EO seeking an assessment of the post-crisis regulatory structure. In contrast to various muted press reports prior to the report's release, the paper provides a thorough analysis and ambitious set of policy proposals aimed at simplifying, streamlining, and rationalizing the current slate of regulatory agencies, capital and liquidity standards, enhanced prudential standards (EPS) and other more stringent rules governing multiple activities such as mortgage origination and proprietary trading.

Rather than relist all of the pertinent policy proposals in this email, my goal here is to provide you with some perspectives and observations from the paper as well as key takeaways from yesterday's SIFMA/TCH Prudential Regulatory Conference in Washington, where Craig Phillips and Senate Banking Committee Chair Mike Crapo were both speakers. Here's a link to the full paper; note that there's an excellent summary of Treasury's recommendations in Appendix B on p123:
https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf

Treasury Paper Perspectives
Treasury's recommendations are based on the Core Principles in the POTUS EO. To oversimplify, I'd characterize these principles as seeking a transition from the post-crisis singular focus on safety and soundness to a more balanced approach to supporting economic growth without sacrificing the bulk of the more stringent requirements of post-crisis regulation (in particular, protecting taxpayers from future bailout risk). The Core Principles and Treasury's response both couch this in terms of furthering American interests and benefitting America's competitiveness juxtaposed with the US gold-plating of most of the

US's implementation of the Basel 3 standards.

Treasury's recommendations are broad and deep. There's a lot in these recommendations for banks of all sizes, from GSIBs down to community banks, covering capital, liquidity, stress-testing, activities, and regulatory structure and interaction. As Craig Phillips noted at yesterday's conference, these recommendations are aimed at allowing banks to better serve their customers without putting taxpayers at risk. Some of the recommendations (e.g. LCR exemptions and HQLA criteria expansion; SLR denominator reductions) would represent significantly positive developments for SIFI and GSIB banks.

Much of this doesn't need Congressional action. Referring to Appendix B again, there's an excellent accounting for each policy recommendation detailing whether it requires statutory (Congress) or regulatory action (or in some cases both). At yesterday's conference, Mr. Phillips noted that the recommendations run ~2:1 regulatory vs. statutory. That said, some of the most impactful and broadly beneficial reforms need to pass Congress:

- Reg structure: Reducing regulatory overlap and duplication; giving FSOC more authority to coordinate regulation and designate "leads" for specific areas; restructure the leadership, appropriations process, and other aspects of the CFPB; Mr. Phillips noted that regulatory duplication is the largest unnecessary regulatory burden facing banks today, with the lack of sufficient tailoring representing the second largest burden
- Raise the $50B threshold for EPS and other requirements, as well as other thresholds including for FBOs; exempt banks from compliance requirements below certain thresholds
    - Note: Mr. Phillips said Treasury specifically avoided suggesting a new threshold, highlighting Treasury's "slight preference" for a more activities/risk-based structure to be negotiated
- Create an off-ramp for well-capitalized banks (a la CHOICE Act)

Not just about the balance sheet. Treasury's paper calls for a modernization of the Community Reinvestment Act, noting significant changes in the ways banks serve customers (e.g. away from bank branches) and calling for a full reassessment of the examination process and its frequency. Similarly, while the paper did not address the more stringent BSA/AML rules that have affected a number of institutions, in response to Q&A Mr. Phillips noted that there's "room for improvement" in the regulatory approach there as well, suggesting a meaningful gap between the goals of the regulation and how it's enforced, even suggesting that in some cases regulators seem focused on "getting banks in trouble than in finding the bad guys." Other activities-based areas of focus include regulatory expectations for bank Boards (echoing comments from Fed Gov. Powell); improving the process for remediating MRAs/MRIAs; significant changes to the Volcker Rule (importantly, both for large banks involved in market-making and also aimed at reducing the regulatory burden for banks not actively trading); revisiting the 2013 leveraged lending guidance and recalibrating the CRE concentration guidance; and finally a number of recommendations aimed at streamlining and simplifying the origination process for residential mortgages.

Surprising degree of focus on FBOs. Citing the significant presence of and activity in the US bank sector of FBOs, as well as a goal to encourage more foreign investment in the US, Treasury provided four significant recommendations for FBOs, including subjecting their US regulatory requirements to their US (rather than global) footprints (needs Congress); recalibrating the threshold for EPS and other IHC regulatory standards, and also recalibrating the Fed's internal TLAC and LTD requirements for FBOs (including taking into consideration a "foreign parent's ability to provide capital and liquidity resources to the U.S. IHC, provided arrangements are made with home country supervisors for deploying unallocated TLAC from the parent, among other factors." The latter proposals would only need changes to Fed regulations.

Acknowledgement of CECL concerns. Numerous banks have been airing concerns about the pro-cyclical impact of CECL, and in response Treasury suggests that regulators review its impact of bank capital and "formulate recommendations to harmonize the application of the standard with regulators' supervisory efforts."

More papers are coming. This paper is the first of four responses to the POTUS EO, and likely the most sweeping in its recommendations as Mr. Phillips noted that Dodd-Frank has had the most impact on banks in an "existential" way. The other papers will cover:

- Capital markets, including derivatives and clearing
- Insurance and asset management
- Nonbank financial institutions, fintech and financial innovation

Mr. Phillips also noted that Treasury is working on responses to two other Eos requiring reassessment of FSOC nonbank SIFI designation authority and Dodd-Frank Title II resolution authority, pointing towards an October release date.

SIFMA/TCH Prudential Regulation Conference
I'd be remiss in opining on the prospects for Treasury's recommendations to move forward without context from the conference in DC. FI attendees were in high spirits after the release of Treasury's paper the evening prior. That said, I heard some notes of caution from some speakers, the most important of which was Senator Mike Crapo, who as head of the Senate Banking Committee is in the pole position to drive the legislative agenda following the House passage of the CHOICE Act. I'd characterize Senator Crapo's comments as cautiously optimistic, yet determined to produce "significant and robust legislation." On the cautionary front, Sen. Crapo noted while he is working closely on a bipartisan basis with Sen. Sherrod Brown to advance reform, he sees much more likely prospects for bipartisan agreement on community banks, with the probability of agreement diminishing as scale increases (but doesn't completely go away). Sen. Crapo singled out several of the Treasury recommendations for specific mention:

- Change the $50B threshold, support more tailoring
- Exempt $10-50B banks from DFAST
- Exempt <$10B banks from Volcker and Basel 3
- Exempt banks from Volcker if trading assets and liabilities are below the Market Risk Rule threshold
- Raise the Living Will exemption threshold and reduce submission frequency
- Revisit/recalibrate certain US capital requirements (eSLR, GSIB surcharge, etc)

Sen. Crapo also made it clear that he is determined to pursue GSE reform as soon as this year also, and suggested a moderate approach that will retain a government guarantee alongside a number of barriers protecting taxpayers including an "adequately capitalized G-fund." There is likely solid bipartisan support to address the GSEs at least on the Banking Committee. Lastly, Sen. Crapo also suggested that he will push hard to make the independent agencies subject to cost-benefit analysis requirements and the EGRPA, requiring a ten-year review of outdated regulations.

Away from Sen. Crapo, a panel consisting of former regulators threw cold water on the Treasury paper suggestions for less regulatory overlap and more coordination, citing differing statutory missions, incentives, and yes, regulatory creep.

Other conference observations:

- A panel debated the impact of DFAST/CCAR on bank capital allocation, with real-life examples from a GSIB, a TCH representative summarizing research findings that bank lending behavior has been measurably altered by stress-testing, a view challenged by a Fed researcher
- TCH made the case for reform of the CAMELS ratings process, claiming that it has moved from a regulatory focus on safety and soundness to a focus on compliance; a former OCC supervisor offered a somewhat different perspective, but also made the case that some of the factors pressuring CAMELS ratings may be slowly lifting
- Bank board members provided perspectives on regulatory relationships and interaction with bank BoDs

Here's a link to this year's program – happy to provide more color: https://hyperlink.services.treasury.gov/agency.do?origin=http://www.sifma.org/prudential2017/program/

Finally, my views on all of this: I think Treasury has been extremely thorough in the direction and scope of their recommendations and very insightful in detailing the channels through which these changes must be made. There's clearly alignment in some aspects of the proposals between Congress, Treasury, and folks currently sitting in leadership seats at the key regulators, most notably on the $50B threshold, Volcker, CCAR, and tailoring, particularly for small banks. That said, very little of this will advance until we see a Vice Chair for Financial Supervision, new Fed Governors, not to mention a permanent OCC Comptroller and a new FDIC head. The most overused phrase in 2017 might be "personnel is policy" and that's precisely why so much of this ambitious and mostly beneficial reform package is on more than a six-month timeframe.

As always, happy to take your questions. Otherwise we'll talk to you next week after DFAST results.
Best,
Dave

David MacGown
Managing Director
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Re: Thank you

From: "Campbell, Christopher" <"/o=ustreasury/ou=exchange administrative group (fydibohf23spdlt)/cn=recipients/cn=e274cfd215d34ec39a8ebd2fe34454ea-campbell, chr">
To: "Engelhard, Joseph" <[redacted]@metlife.com>
Cc: "Polichene, Briget" [redacted]@metlife.com>, "Chris Cox [redacted]@navigatorsglobal.com)" [redacted]@navigatorsglobal.com>
Date: Fri, 13 Apr 2018 20:14:29 -0400

Thanks very much, Joe. It was great to spend some time with you.

Chris

From: Engelhard, Joseph[redacted]@metlife.com>
Date: April 13, 2018 at 4:56:57 PM PDT
To: Campbell, Christopher <Christopher.Campbell@treasury.gov>
Cc: Polichene, Briget[redacted]@metlife.com>, Chris Cox ([redacted]@navigatorsglobal.com) [redacted]@navigatorsglobal.com>
Subject: Thank you

Chris,

Thank you for taking the time to meet with Briget and me yesterday—and for Chris Cox to make it happen so quickly. I also enjoyed the discussion on a wide range of topics and we would be glad to help on any of the topics discussed, whether cyber or otherwise.

As discussed, MetLife is very supportive of the many recommendations in the Treasury reports on banking, asset management and insurance as well as the capital markets report. We are particularly grateful for the prioritization of recommendations that will improve market efficiency and lessen impediments to greater private sector investment.

MetLife is one of the larger owners of various ABS asset classes, so we were particularly interested in the proposed securitization reforms. We wholeheartedly agree with the proposals to increase liquidity and right-size banks' capital charges. We and a number of other large holders of ABS, did however, want to point out some data indicating that by and large securitization markets are absorbing the new disclosure and risk retention rules (leaving aside the discussion of CLO markets, where the case is less clear). Attached is a slide deck that a group of investors presented to officials at the Fed and SEC earlier this week. We would be glad to discuss with you or any Treasury officials who might be interested in this topic.

Kind regards,
Joe

Joseph L. Engelhard | Senior Vice President | Head, Regulatory Policy Group | Global Government Relations | MetLife
[redacted] Washington, DC 20005 | T. +[redacted] | M. +[redacted] |[redacted]@metlife.com

Financial Research Advisory Committee Summer Meeting Updates

From: Dino Falaschetti <dino.falaschetti@ofr.treasury.gov>
To: [redacted]@chicagobooth.edu, [redacted]@wellsfargo.com, [redacted]@edmcouncil.org, [redacted]@andrew.cmu.edu, [redacted]@lseg.com, [redacted]@dtcc.com, [redacted]@law.columbia.edu, [redacted]@gmail.com, [redacted]@gmail.com, [redacted]@brookings.edu, [redacted]@hotmail.com, [redacted]@jpmorgan.com, [redacted]@bah.com, [redacted]@stern.nyu.edu, [redacted]@osu.edu, [redacted]@wharton.upenn.edu, [redacted]@massmutual.com, [redacted]@gmail.com, [redacted]@umich.edu, [redacted]@bluemountaincapital.com, [redacted]@gs.com, [redacted]@the-cfs.org
Cc: [redacted]@ofr.treasury.gov>, [redacted]@ofr.treasury.gov>, [redacted]@ofr.treasury.gov>
Date: Thu, 27 Jun 2019 10:43:42 -0400
Attachments: FRAC Agenda July 2019.pdf (139.31 kB); FRAC Charges July 2019.pdf (203.48 kB); FRAC Charges Feb. 2020.pdf (162.18 kB)

Good morning, Advisory Committee Members,

I am delighted to contact you as the Senate-confirmed Director of the Office of Financial Research. From the start, I want to express my tremendous gratitude for your commitment to public service and to helping the OFR meet its important mission. I am deeply impressed with the extraordinary credentials and vast expertise you have so generously agreed to share with us.

As we make final preparations for our July 11 Summer Meeting at the Federal Reserve Bank of New York, I'm reaching out to share a few updates. The Welcome Dinner will be held on July 10 at 7 p.m. at VITAE, an Italian restaurant, located at 4 East 46th Street, 212-682-3562. To RSVP for the Welcome Dinner, please respond to a forthcoming Outlook invitation from [redacted] on our Advisory Committee support team. Also, for those members who are unable to attend in person, you can join us via conference call at: [redacted], and enter code: [redacted].

I'm attaching a few documents for your reference, including the final meeting agenda as well as the Leveraged Lending Charge and the Transition from LIBOR to SOFR Charge. I am also attaching a new charge for February 2020 for your consideration.

As detailed in the agenda, we will offer continental breakfast at 8:30 a.m., convene the meeting at 9:00 a.m., and plan to formally adjourn the meeting at 2:30 p.m.

I look forward to working with you and seeing you soon.

With best regards,

Dino

OFR OFFICE OF FINANCIAL RESEARCH FINANCIAL RESEARCH ADVISORY COMMITTEE

AGENDA

Thursday, July, 11, 2019
Federal Reserve Bank of New York

8:30 a.m. **Continental Breakfast in Benjamin Strong Room**

9:00 a.m. **Welcome and Introductions**
Dino Falaschetti, Director, Office of Financial Research
Randy Kroszner, Chairman
Sarah Dahlgren, Vice Chairwoman

9:30 a.m. **Presentation and Discussion of Leveraged Lending Charge**
Susan Wachter & Kate Judge, Co-Chairs

10:30 a.m. **Presentation and Discussion of Transition from LIBOR to SOFR Charge**
Colin Teichholtz, Chair

11:30 a.m. **Break**

12:00 p.m. **Lunch with Guest Speaker James "Jim" Nevels, The Swarthmore Group**

1:00 p.m. **Introduction and Discussion of New Charges**

2:00 p.m. **New Working Group Meetings to Organize and Plan Next Steps**

2:30 p.m. **Adjournment**

OFR FINANCIAL RESEARCH ADVISORY COMMITTEE
OFFICE OF FINANCIAL RESEARCH

Charges to FRAC for July 2019 Meeting

1. **How should the challenges associated with the transition from LIBOR to SOFR be addressed?**

2. **Does leveraged lending pose a risk to financial stability?**

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1. TOPIC: Transitioning from LIBOR to SOFR

SUMMARY

The Office of Financial Research (OFR) is requesting the Financial Research Advisory Committee (FRAC) to consider challenges in building volumes in the industry-identified alternative reference rate, SOFR.

BACKGROUND

Low underlying transaction volumes threaten the long-term stability of the U.S. dollar London Interbank Offered Rate (LIBOR). This situation prompted the Alternative Reference Rates Committee (ARRC), an industry group convened by the Federal Reserve, to identify an alternative reference rate. The rate selected by the ARRC is the Secured Overnight Financing Rate (SOFR), an index reflecting the cost of overnight funding secured by Treasury securities. The SOFR is produced by the Federal Reserve Bank of New York in cooperation with the OFR.

The SOFR has been in production for almost a year, and is used in both cash and derivatives contracts. However, contract volumes need to increase significantly before discontinuing LIBOR if a disruptive transition is to be avoided. To provide additional benchmark options reflecting the cost of SOFR funding over a term, the Federal Reserve Bank of New York is considering the publication of backward-looking term average SOFR rates.

QUESTIONS

1. What are the major impediments to building volume in SOFR-linked contracts?
2. What measures, if any, should the official sector consider to encourage adoption of the SOFR?

OFR FINANCIAL RESEARCH ADVISORY COMMITTEE
OFFICE OF FINANCIAL RESEARCH

TOPIC: Leveraged Lending

SUMMARY

The Office of Financial Research (OFR) is requesting the Financial Research Advisory Committee (FRAC) to consider questions regarding potential systemic vulnerabilities related to the U.S. leveraged loan market, and associated markets such as the market for collateralized loan obligations (CLOs). Further, the OFR seeks input on data gaps that affect monitoring of these markets.

BACKGROUND

Investor demand for leveraged loans has increased significantly in recent years, in part, due to expectations for higher interest rates. Most leveraged loans are floating-rate instruments. These loans are structured and syndicated to accommodate two primary types of lenders: banks and institutional investors. Institutional loans comprise the majority of new issuance. The share of covenant-lite loans has grown along with institutional loan issuance. The OFR has access to data on institutional loans (issuance and outstanding) via Standard & Poor's Leveraged Commentary & Data, but not bank loans. Data on investor exposures to leveraged loans is also incomplete.

QUESTIONS

1. How should the OFR evaluate and monitor risks related to leveraged lending?
2. Does leveraged lending pose any threat to financial stability? If not, what are the mitigants?
3. How are the risks different for bank versus institutional leveraged loans?
4. How do the above risks and mitigants vary and interact with specific risks associated with different types of institutional investors (e.g., liquidity mismatch for loan mutual funds)? Please include comments on CLO managers, hedge funds (including distressed funds), mutual funds, exchange-traded funds, pension funds, and insurers.
5. Are there risks from the securitization of leveraged loans into CLOs? How can the OFR effectively monitor these risks?
6. What are the similarities and differences between leveraged loan markets today versus those pre-crisis? With respect to CLOs, how are these similar or different from subprime mortgage securities in the pre-crisis era?
7. What other sources of data would enhance the OFR's market monitoring efforts?
8. What are the risks from covenant-lite loans? What are the risks from earnings before interest, taxes, depreciation, and amortization adjustments, and other loan document modifications?

OFFICE OF FINANCIAL RESEARCH — FINANCIAL RESEARCH ADVISORY COMMITTEE

Charges to FRAC for July 2019 Meeting

TOPIC: Encouraging Market Discipline to Enhance Financial System Resilience

SUMMARY

The Office of Financial Research (OFR) charges its Financial Research Advisory Committee (FRAC) with identifying promising strategies to increase financial resiliency through greater transparency, more effective incentives, and ultimately more reliable market discipline.

BACKGROUND

The 2007-09 financial crisis was at least partly a product of opaque counterparties and insufficient skin-in-the-game, which fueled systemic risks. Many of these risks were rooted in the housing and derivatives markets, where they were poorly understood or communicated by parties to over-the-counter transactions. Short-term, profit seeking incentives exacerbated the situation, as the financial system levered up on mispriced securities.

Lawmakers and regulators have worked to improve many dimensions of market transparency. For example, the Dodd-Frank Act required that standardized derivatives (largely swaps) be cleared and traded through central counterparties (CCPs). More transparent derivatives data allow for better price discovery, easier acquisition of information on underlying risks, and more effective monitoring by regulators. In addition, securitized financial products now also require greater disclosure throughout the intermediation chain, which increases their price efficiency. However, as with much regulation, there is a flip side to the benefits from CCPs: they concentrate risk in the CCP, another potentially worrying source of systemic risk.

After the crisis, steps also were taken to better incentivize financial markets and institutions to behave in ways that support a resilient financial system. One step was the introduction of margin requirements to incentivize the netting of risk and the use of central clearing. Another was the establishment of single-counterparty credit limits for bank holding companies and foreign banking organizations. These limits were designed to incentivize greater diversification of counterparty risk, yet some researchers still question whether our financial system is sufficiently well capitalized.

QUESTIONS

1. Identify up to three features of the financial system (whether a feature of financial institutions, markets, or activities) where increased transparency can further financial stability, and how that transparency might be achieved.
2. Propose up to three strategies that can (1) better align private-sector incentives with (2) the societal goal of a more resilient financial system through (3) improved market discipline.