



BANKING REPORT



REGULATORY REFORM

Systemic Risk

The Financial Stability Oversight Council: Completely New or Deja Vu?



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Amid the swirl of news stories reporting on financial regulatory reform developments, one increasingly sees references to the new Financial Stability Oversight Council (“FSOC”), but there has been little attention paid to what it is, what it is not, and what it can be expected to do. The FSOC was established by the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”). This is but the latest instance in which Congress acted in the aftermath of a financial crisis by creating a new government agency.¹

¹ The Office of the Comptroller of the Currency (“OCC”) was created as a bureau within the Treasury Department by the National Currency Act of 1863 to create a national currency and help fund the Civil War. The Board of Governors of the Federal Reserve System (“Federal Reserve”) was created

Like its predecessor, the President’s Working Group on Financial Markets (“PWG”), the FSOC is a grouping of federal financial institution regulators. Like the PWG, the FSOC’s mission is to implement the lessons learned from the crisis that gave rise to it. Unlike the PWG, the FSOC is a more formalized entity designed to be more transparent and accountable, and its membership more inclusive and representative of the full spectrum of financial regulators. It remains to be seen whether this new structure will allow the FSOC to be more effective than the PWG in anticipating and avoiding financial crises, or whether its rigid, yet more transparent and inclusive structure makes it less likely to replicate the PWG’s largely unnoticed successes.

A Basis for Comparison: What is the PWG?

When considering the role that the FSOC can play in the future, it is helpful to examine the role that the PWG has played until now.² The PWG is a forum where federal financial regulatory agency heads may confer periodically as a group and agency staffs may interact and produce studies and recommended legislative changes, often in response to Congressional requests.

The PWG was established by an Executive Order of President Ronald Reagan, in response to the “Black Monday” stock market crash of October 19, 1987.³ The membership of the PWG includes the Secretary of the

by the Federal Reserve Act of 1913, following the banking panic of 1907. The Federal Deposit Insurance Corporation (“FDIC”) and the Securities and Exchange Commission (“SEC”) were established following the crash of 1929 by the Banking Act of 1933 and the Securities Exchange Act of 1934, respectively. The Office of Thrift Supervision (“OTS”) was created by the Financial Institutions Reform, Recovery and Enforcement Act of 1989, following the savings and loan crisis.

² Notwithstanding its apparent demise, in this article we refer to the PWG in the present tense, as no official action has yet been taken to abolish it.

³ Executive Order 12631 – Working Group on Financial Markets (March 18, 1988) (“Executive Order”).

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Treasury (“**Secretary**”) (who acts as chairman), and the Chairmen of the Federal Reserve, the SEC, and the Commodity Futures Trading Commission (“**CFTC**”).

The Executive Order provides only the following brief description of the PWG’s purpose and functions, so brief that we can repeat it in full:

Sec. 2. Purposes and Functions.

(a) *Recognizing the goals of enhancing the integrity, efficiency, orderliness, and competitiveness of our Nation’s financial markets and maintaining investor confidence, the Working Group shall identify and consider:*

(1) *the major issues raised by the numerous studies on the events in the financial markets surrounding October 19, 1987, and any of those recommendations that have the potential to achieve the goals noted above; and*

(2) *the actions, including governmental actions under existing laws and regulations (such as policy coordination and contingency planning), that are appropriate to carry out these recommendations.*

(b) *The Working Group shall consult, as appropriate, with representatives of the various exchanges, clearinghouses, self-regulatory bodies, and with major market participants to determine private sector solutions wherever possible.*

(c) *The Working Group shall report to the President initially within 60 days (and periodically thereafter) on its progress and, if appropriate, its views on any recommended legislative changes.*

The lack of detail in its mandate provides the PWG considerable flexibility. The PWG is not required to report to Congress or otherwise formally account for its actions. As a result, the PWG, like most federal financial regulators, has traditionally operated out of public sight, perhaps encouraging its members to share confidential information with little fear that the information could become public.⁴

At the same time, the PWG also faces certain constraints. The PWG is not a creation of Congress. There is no statute detailing its powers or authorizing its activities. The PWG has no explicit authority that is independent of its members. The PWG has no formal staff, funding or offices, but depends on the charity of the Treasury Department for its operations.⁵

Over time, the PWG has evolved beyond the boundaries of the Executive Order. The PWG now informally includes the heads of the FDIC, the OCC, and the OTS in its deliberations. The PWG also covers a broader range of financial sector topics than its financial markets brief implies, issuing “reports, principles, and draft legislative language on terrorism risk insurance, hedge funds and other private pools of capital, over-the-

⁴ PWG staff reports, however, often have been made public. See, e.g., “Hedge Funds, Leverage, and the Lessons of Long-Term Capital Management: Report of the President’s Working Group on Financial Markets” (April 1999), available at <http://www.treasury.gov/resource-center/fin-mkts/Documents/hedfund.pdf>; and “Over-the-Counter Derivatives Markets and the Commodity Exchange Act: Report of the President’s Working Group on Financial Markets” (November 1999), available at <http://www.treasury.gov/resource-center/fin-mkts/Documents/otcact.pdf>.

⁵ “To the extent permitted by law and subject to the availability of funds therefore, the Department of the Treasury shall provide the Working Group with such administrative and support services as may be necessary for the performance of its functions.” Section 3(c) of the Executive Order.

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counter derivatives, the Commodity Exchange Act, and financial contract netting.”⁶

The Bush Administration recommended updating the Executive Order to recognize and reflect accurately what the PWG actually does:

- The PWG focuses on the financial sector generally, rather than being restricted to the financial markets.

- The PWG is a forum to facilitate better inter-agency communication regarding the mitigation of systemic risk, the improvement of market integrity, efficiency and competitiveness, and the promotion of consumer and investor protection.

- The OCC, FDIC, and OTS can act as members of the PWG.

- The PWG has authority to issue reports and other documents.⁷

This modernization effort was abandoned by the incoming Obama Administration, which issued a White Paper containing a diametrically opposed message, proposing that the FSOC be created to replace the PWG.⁸ Without reaching explicit conclusions about the role played by the PWG in the run-up to the financial crisis, the report of the Financial Crisis Inquiry Commission (“**FCIC**”) offers clues as to the basis for this turnabout. The FCIC noted that the PWG has historically taken a deregulatory approach, such as in its report on over-the-counter derivatives, recommending against the regulation of those products, and in its report on hedge funds and leverage, where it cautioned that regulation of hedge funds could disrupt trading activity and financial intermediation that supported economic activity.⁹ It is not clear, however, that a newly reconstituted version of the PWG would hold different views.

Perhaps because it operated in the shadows, some have ascribed to the PWG far more power than it actu-

⁶ Department of Treasury, “Blueprint for a Modernized Financial Regulatory Structure” (March 2008) (“**Bush Blueprint**”), p. 76.

⁷ *Id.*, pp. 76-77.

⁸ Department of Treasury, “Financial Regulatory Reform: A New Foundation,” (June 17, 2009) (“**White Paper**”), p. 20.

⁹ Financial Crisis Inquiry Report, Final Report of the National Commission on the Causes of the Financial and Economic Crisis in the United States (Jan. 27, 2011) (“**FCIC Report**”), pp. 48 and 58.

ally has and complained that on occasion the PWG has abused this perceived authority. Some even have alleged that the PWG may have manipulated the stock market.¹⁰ Some share an expectation that the PWG can and will prop up the market in the event of a financial crisis.¹¹ Taken together, these assumptions and allegations have transformed the PWG into a source of moral hazard, notwithstanding the fact that it exists to champion private sector solutions over government intervention. It is not clear, however, whether the blame for such excesses, if true, should be borne collectively by the PWG or only certain of its members.

The PWG's flexibility and opaque operating style allow it some agility, but simultaneously preclude it from advertising its successes. We cannot determine how many crises the PWG successfully averted since its creation. All can agree, however, that the PWG did not succeed in staving off the most recent financial crisis. This lack of success may have discredited the PWG, and while there has been no official act dissolving the PWG, its role essentially has been subsumed within the FSOC.¹²

What is the FSOC; How Does It Function?

Mandate

The FSOC has a broad mandate. The FSOC is responsible to:

- *Identify risks to the financial stability of the United States that could arise from the material financial distress or failure, or ongoing activities, of large, interconnected bank holding companies or non bank financial companies, or that could arise outside the financial services marketplace;*

- *Promote market discipline, by eliminating expectations on the part of shareholders, creditors and counterparties of such companies that the Government will shield them from losses in the event of failure; and*

- *Respond to emerging threats to the stability of the United States financial system.*¹³

These purposes appear consistent with those of the PWG, with some refinements. First, the PWG was created to identify and repair the defects giving rise to the 1987 crash, but over time its mission expanded to deal with evolving conditions in the markets. The first prong of the FSOC mandate, to identify future risks, is ostensibly more forward-looking than the PWG mandate, and covers the whole financial system, not just the markets. Nevertheless, like the PWG, the FSOC also is addressing the problems associated with a past crisis.

¹⁰ See, e.g., Testimony of Federal Reserve Chairman Ben Bernanke, Hearings on Monetary Policy and the State of the Economy, Committee on Financial Services, U.S. House of Representatives (July 20, 2006) (questioning by Rep. Ron Paul), transcript available at <http://www.lewrockwell.com/paul/paul340.html>.

¹¹ See Brett D. Fromson, *Plunge Protection Team*, Washington Post, Feb. 23, 1997.

¹² The PWG's most recent report on money markets may have been its swan song. See Report of the President's Working Group on Financial Markets: Money Market Fund Reform Options (October 2010), available at <http://www.treasury.gov/press-center/press-releases/Documents/10.21%20PWG%20Report%20Final.pdf>.

¹³ Dodd-Frank Section 112(a)(1).

Second, there is a new mandate to respond to emerging threats to the financial system. Prongs two and three of the FSOC mandate raise an internal inconsistency that also applies to the PWG. Both the PWG and the FSOC are charged with discouraging the expectation of government intervention, but that mandate is at odds with the obligation to maintain financial stability and avert threats, which implies the ability to intervene. Thus the mandates of the PWG and FSOC differ only to the extent that the FSOC standards state an obvious, inherent inconsistency that the Executive Order ignores.

Activities

While the PWG and the FSOC appear to share similar mandates, the PWG has no express regulatory authority. In contrast, Dodd-Frank assigns the FSOC a wider range of activities, the most important of which involve substantive supervision and arbitration of disputes among member agencies.¹⁴

Supervision. The role of the FSOC in supervision is extensive and includes:

- subjecting a U.S. or foreign non bank financial company to prudential standards and supervision by the Federal Reserve;

- recommendations concerning the prudential standards applicable to non bank financial companies and large, interconnected bank holding companies;

- recommendations that a primary financial regulatory agency apply new or heightened standards;

- review of actions to be taken by the Federal Reserve with regard to systemically important financial companies;

- determinations to prevent access by swaps entities to federal assistance;

- designations of financial market utilities or payment, clearing, or settlement activities that are systemically important; and

- authorizing or requiring examinations of or enforcement actions against designated financial market utilities.¹⁵

Interagency Dispute Resolution. The FSOC has authority to make recommendations for resolving supervisory jurisdictional disputes among two or more member agencies. It may resolve disputes between the SEC and the CFTC regarding joint rulemakings under Title VII,¹⁶ and stay or set aside a regulation of the Bureau of Consumer Financial Protection ("CFPB").¹⁷

OFR Oversight. The Office of Financial Research ("OFR") will be central in permitting the FSOC to accomplish its mission. Housed in the Treasury Department, the OFR may collect reports from a bank holding company with total consolidated assets of more than \$50 billion or a non bank financial company supervised by the Federal Reserve. The OFR also may collect information from any bank holding company or non bank financial company for determining whether the company should be designated as systemically important.¹⁸ This information can help FSOC anticipate and react to emerging financial crises and identify entities to be sub-

¹⁴ See Dodd-Frank Sections 112 and 119.

¹⁵ Dodd-Frank Sections 113, 115, 120, 121, 716, 804, and 807.

¹⁶ Dodd-Frank Section 712(d)(3).

¹⁷ Dodd-Frank Section 1023.

¹⁸ Dodd-Frank Sections 112(d)(3) and 116.

jected to enhanced prudential regulation by the Federal Reserve.¹⁹

Possibly Conflicting Goals. To accomplish its assigned tasks, the FSOC must foster the cooperation of its members. However, rather than make regulators more likely to communicate with each other, it is possible that Dodd-Frank's emphasis on more formal means of communication between agencies may in fact inhibit the exchange of ideas and information. While those with less access to market information may crave greater transparency, the probability that two regulators would first share meaningful ideas with each other at a public meeting rather than behind closed doors is remote. It is more likely that regulators may use public FSOC meetings as a forum to announce refined and negotiated joint views or, more cynically, to advertise views that are well known and perhaps unaccepted among their colleagues, but more popular among the public at large. If members do not find the FSOC a convenient forum for discourse, the risk of fragmented regulatory oversight that some see as a contributing factor in the last financial crisis could be greater still.

The FSOC's mission of enhanced cooperation and communication also could be undercut by its role as arbiter of disputes among members. Member agencies are "independent" and jealous of their authority. Resolving a dispute between two members could polarize the FSOC, effectively dividing it into two or more camps and making progress on other issues more difficult. The losing agency could feel resentful, prove less reliable a partner in facing new problems, and even be less likely to share information with the "winning" side.

The process for the FSOC to make recommendations to a member for heightened regulatory standards for systemically risky financial activities also will be delicate and ideally should never be used. An informal, rather than a formal recommendation is more likely to gain a better reception from any member. A formal recommendation risks comparison to a public rebuke and resentment at what the receiving member might perceive as an unwarranted intrusion. Fear that a member could react adversely or in retaliation to even an informal recommendation might prompt other members to refrain from speaking up.

The FSOC has another responsibility that it has not yet publicly discussed. The FSOC may recommend heightened supervisory standards for activities that could increase the risk of problems spreading among low-income, minority or underserved communities.²⁰ Although there has been little discussion about this provision, it could prove controversial.²¹ The focus on consumer issues is complementary to Dodd-Frank's emphasis on consumer protection in Title X but it may not be directly relevant to the macroprudential concerns that are the focus of Title I.²²

¹⁹ See also Dodd-Frank Sections 153-156.

²⁰ Dodd-Frank Section 120(a).

²¹ While some argue that it is appropriate to place greater emphasis on the enforcement of consumer laws with respect to financial institutions, others have argued that the focus on increased lending to low-income, minority and underserved communities was one of the causes of the recent crisis. See, e.g., FCIC Report, Dissenting Statement of Peter J. Wallison, pp. 524-532.

²² Further, it may be inconsistent to transfer the authority over consumer laws from the financial regulators to the CFPB through Title X on the one hand, in part because those regula-

Membership

The FSOC is a collection of 10 voting and five non voting advisory members, formally headquartered in the Treasury Department building. The voting members are the Secretary (who serves as chairperson), the current members of the PWG, plus the heads of the OCC, CFPB, FDIC, Federal Housing Finance Agency, and National Credit Union Administration Board.²³ Dodd-Frank also provides a vote to an independent member with insurance expertise, appointed by the President for a term of six years and confirmed by the Senate.²⁴

The non voting members of the FSOC are the Director of the OFR, the Director of the Federal Insurance Office ("FIO"), a state insurance commissioner, a state banking supervisor, and a state securities commissioner, the latter three each serving a term of two years.²⁵

Forging consensus can be challenging for the head of any collegial body, and the membership structure of the FSOC poses subtle challenges for its chairperson. Primary among those challenges is creating a sense of equality among two classes of FSOC participants, voting and non voting. Dodd-Frank permits the FSOC to exclude non voting members from its deliberations, when necessary to safeguard and promote the exchange of confidential information.²⁶ The fact that certain participants can be excluded from discussions of confidential, and therefore important, matters adds to this tension. Even in circumstances where non voting members participate, their right to speak is simply that.

Another challenge is coordinating the views of state and federal officials. Three of the five non voting members represent state regulatory interests, and states recently have been more aggressive in enforcement actions (especially in the area of consumer protection) than the federal regulatory agencies. If the non voting, state members are sidelined, then the FSOC may look

tors have been accused of neglecting their responsibilities, and then indirectly charge those same agencies with responsibility to recommend heightened standards to protect consumers. For a discussion of the jurisdiction of the CFPB generally, see Donald N. Lamson and Hilary Allen, *Consumer Financial Protection: It's a Smaller World After All*, 96 Banking Rep. (BNA) 552, 03/22/2011 (96 BBR 552, 3/22/11). There also has been controversy concerning the authority of Elizabeth Warren, Special Advisor to the Secretary of the Treasury, to lead the CFPB on an interim basis. See Donald N. Lamson and Hilary Allen, *The Consumer Financial Protection Bureau: Stand-Up or Stand-Off?*, 96 Banking Rep. (BNA) 693, 04/12/2011 (96 BBR 693, 4/12/11).

²³ Dodd-Frank Section 111(b)(1).

²⁴ Dodd-Frank Section 111(b)(1)(J). Despite the fact that the FSOC has been operating for nine months, the seat for the insurance expert is still vacant. The appointment of a non-voting Director of the FIO has only recently been announced. John Huff, the director of the Missouri Department of Insurance, holds the non-voting seat for a state insurance commissioner, and currently is the only insurance voice on the FSOC. As the FSOC is now devising rules for the designation of systemically-important non-bank financial institutions, some of which may be insurance companies, the lack of insurance industry representation may be a cause for concern. See Phil Mattingly, "Vacant Insurance Seats Hinder Stability Council, Lawmakers Say," Feb. 11, 2011, available at <http://www.bloomberg.com/news/2011-02-11/vacant-insurance-seats-hinder-stability-council-lawmakers-say.html>.

²⁵ Dodd-Frank Section 111(b)(2).

²⁶ Dodd-Frank Section 111(b)(3).

and behave more like the PWG. Even so, the new voices of the CFPB and the insurance representative will have a vote and may change the dynamic. It remains to be seen whether the FSOC can take advantage of these different inputs to spot and react to coming crises.

As most voting members also head independent agencies, the assumption of responsibilities relating to FSOC may represent a significant additional burden. While required to meet at least quarterly,²⁷ the FSOC could require more frequent meetings to properly discharge its functions. Agency heads cannot afford to ignore their new FSOC duties, however, due to the requirement that each voting member personally sign an annual statement to Congress to the effect that “such member believes that the [FSOC], the Government and the private sector are taking all reasonable steps to ensure financial stability and to mitigate systemic risk that would negatively affect the economy” or otherwise explain what further action needs to be taken.²⁸ This is akin to the requirement that CEOs and CFOs of publicly held corporations personally attest to their company’s financial statements, putting their reputations on the line, and encouraging them to more closely monitor the accuracy of financial statements.²⁹

Governance

Unlike the PWG, the FSOC has a formalized structure and governance. Generally, FSOC action will follow an affirmative vote of a majority of the voting members.³⁰ However, it requires the vote of two-thirds of the voting members to designate a non-bank financial company as systemically important and subject to prudential standards and regulation by the Federal Reserve. The Secretary must join in that vote, effectively giving him a veto.³¹ Also, a two-thirds vote is required for the FSOC to provide non binding recommendations regarding the resolution of interagency disputes, or restricting mergers or activities of an institution, although the vote of the Secretary is not required.³²

The FSOC’s bylaws fill 13 pages and comprehensively address its corporate governance, including such matters as delegation of voting authority by its members, duties of the Chairperson and various staff members, budget, information collection and sharing, principal offices, and disqualification of members due to conflicts of interest.³³

Unlike the PWG, the FSOC will have a substantial budget. The Chairperson will propose a budget, subject to a majority vote of the members. The OFR assumes the FSOC’s expenses. The OFR, and by extension the FSOC, will be funded by transfers from the Federal Reserve until 2013. OFR expenses in later years will be funded through assessments on bank holding companies with greater than \$50 billion in assets and non bank financial companies supervised by the Federal Re-

serve.³⁴ FSOC approved a budget for FY 2011 with \$4.4 million allotted for staff salary and expenses and \$2.5 million for IT development, operations and maintenance.³⁵

Staff and Committees. The FSOC’s bylaws provide that the Secretary shall oversee the FSOC staff.³⁶ While the PWG does not have any permanent staff, the FSOC may hire an Executive Director, a Legal Counsel, a Secretary, and other staff members. The FSOC anticipates that its staff may grow to more than 17 this year.³⁷ As with the PWG, member agency and federal government employees also can be detailed to the FSOC.³⁸

In contrast to the PWG’s lack of formal structure, the FSOC has a highly detailed committee system. The FSOC bylaws provide for the creation of a Deputies Committee and Special Advisory, Technical, and Professional Committees. The Advisory Committee will consist of State regulators. The members of other committees may be members of the FSOC, or other persons, or both.³⁹

The Deputies Committee, composed of a senior official from each member agency, will coordinate and oversee the work of the interagency staff committees and coordinate the FSOC’s agenda. The Systemic Risk Committee and two subcommittees will oversee the FSOC’s analysis of emerging threats to financial stability. The Systemic Risk Committee will be accountable for systemic risk monitoring and prioritize the review of sources of systemic risk and overseeing the work of its subcommittees. The Institutions Subcommittee will identify and analyze risk-related issues that affect financial institutions in the medium and longer term. The Markets Subcommittee will perform the same function with respect to financial markets.⁴⁰

Staff from the member agencies will be organized into several additional standing committees responsible for considering the international implications of the FSOC’s work, including coordination with foreign regulators. There will be committees for the designation of non bank financial companies to be supervised by the Federal Reserve, designation of financial market utilities and payment, clearing, and settlement activities, heightened prudential standards, orderly liquidation authority and resolution plans, and data coordination.⁴¹

What is not clear from this highly specific structure are the rules for the assignment of agency staff to these committees. It is possible that some agencies might dominate the committees or exclude the advisory members from committee work. If the committees function opaquely, the benefits of the transparency that Dodd-

²⁷ Dodd-Frank Section 111(e).

²⁸ Dodd-Frank Section 112(b).

²⁹ See Section 302 of the Sarbanes-Oxley Act of 2002.

³⁰ Dodd-Frank Section 111(f).

³¹ Dodd-Frank Sections 113(a)(1), 113(b)(1), 113(d)(2), 113(f)(1), and 117(c)(2)(A).

³² Dodd-Frank Sections 119 and 121.

³³ See Rules of Organization of the Financial Stability Oversight Council (Oct. 1, 2010) (“**FSOC Organization Rules**”), available at <http://www.treasury.gov/initiatives/Documents/FSOCbylaws.pdf>.

³⁴ Sections 118 and 155.

³⁵ Minutes of the Financial Stability Oversight Council Meeting (Oct. 1, 2010) (“**FSOC October Meeting Minutes**”), available at <http://www.treasury.gov/initiatives/Documents/XII%20-%20Minutes%20of%20the%20Financial%20Stability%20Oversight%20Council.%2010%201%2010.%20final.corrected.pdf>.

³⁶ See FSOC Organization Rules.

³⁷ FSOC October Meeting Minutes.

³⁸ Dodd-Frank Section 111(j).

³⁹ Dodd-Frank Section 111(d). See also FSOC Organization Rules.

⁴⁰ Financial Stability Oversight Council Committee Structure (Nov. 23, 2010), available at <http://www.treasury.gov/initiatives/Documents/X%20-%20Committee%20Structure%20111910.pdf>.

⁴¹ *Id.*

Frank mandates for the FSOC could be lost. There also is a danger that the committees may work in isolation from one another or that communication between committee staffs could suffer, thereby negating the benefits of expanding FSOC's membership. The dynamic of permanent staff working with staffs of the member agencies is new and may present issues. Apparently the FSOC also recognizes these issues because the minutes of its Oct. 1, 2010 meeting reveal consideration of a mechanism to facilitate bringing systemic risk issues to the attention of the full FSOC more quickly. Further, the FDIC and SEC staffs are drafting principles to govern consultation among the FSOC members.⁴²

Transparency

Unlike the PWG, the FSOC has been aggressive in making public a great deal of its activity. However, while the FSOC has committed to holding two open meetings each year and to release minutes after each meeting, those minutes are subject to redaction and there is an extensive list of bases on which to withhold information from the public.⁴³ These instances involve information:

- contained in reports prepared by financial regulatory agencies;
- which would lead to significant financial speculation or endanger the stability of markets or financial institutions;
- exempted from disclosure by statute or regulation or required to be kept secret;
- constituting trade secrets or that otherwise is privileged or confidential;
- of a personal nature that would constitute an unwarranted invasion of personal privacy or be inconsistent with Federal privacy laws;
- compiled for law enforcement or supervisory purposes; or
- that would compromise the mission or purposes of the FSOC.⁴⁴

Notwithstanding FSOC's transparency policy, observers may be disappointed in the level of transparency that has been achieved. The minutes released to date reveal that a substantial portion of FSOC meetings are conducted in executive session, away from the public view. Those portions conducted in public indicate deliberations that at times seem scripted. However, the FSOC may regret its commitment to even this limited level of transparency when it is grappling with contentious issues among its members or an impending crisis.

FSOC's Progress To Date

To date, the FSOC has met four times and accomplished a great deal.⁴⁵ The FSOC has issued an advance notice of proposed rulemaking for the designation of

⁴² FSOC October Meeting Minutes.

⁴³ The activities of the FSOC also are subject to audit by the Comptroller General of the United States, which has broad access to FSOC records. Dodd-Frank Section 122.

⁴⁴ See Transparency Policy for the Financial Stability Oversight Council (Oct. 1, 2010), available at <http://www.treasury.gov/initiatives/Documents/FSOCtransparencypolicy.pdf>.

⁴⁵ Meetings were held on Oct. 1, 2010, Nov. 23, 2010, Jan. 18, 2011 and March 17, 2011.

certain market utilities as systemically important⁴⁶ and proposed recommendations regarding modifications to concentration limits on large financial companies.⁴⁷ The FSOC has proposed rules regarding designation of certain non-bank financial companies as subject to increased supervision,⁴⁸ handling Freedom of Information Act requests,⁴⁹ and designation of financial market utilities for heightened supervision.⁵⁰ To date, none of these rules has been adopted. The proposed rule relating to designation of systemically important non-bank financial companies has been particularly controversial – members of Congress from both parties have criticized the lack of specificity in the rule.⁵¹ The FSOC also clarified its governance by publicly releasing its bylaws, transparency policy, and committee structure.

The FSOC has published studies relating to concentration limits on large financial companies, and the implementation of the Volcker Rule.⁵² The FSOC also has published studies on the effects of size and complexity of financial institutions on capital market efficiency and economic growth, and on the macroeconomic effects of risk retention requirements.⁵³ Dodd-Frank requires the FSOC to publish a study on secured creditor haircuts in liquidations by July 2011 and a study addressing the feasibility and benefits of contingent capital requirements by July 2013.⁵⁴ Once these studies are completed, in some cases the FSOC will propose regulations to implement its findings and recommendations.

There are other important tasks that the FSOC has not yet undertaken. Although the FSOC indicated that by April 2011 it would begin designating non bank financial companies as systemically important, to date no such designations have been made.⁵⁵ This delay may be due in part to comments challenging the FSOC's authority to adopt rules governing the designation process,⁵⁶ as well as to the criticism of the FSOC's proposed designation rule. There also has been disagree-

⁴⁶ 75 Fed Reg 79,982 (Dec. 21, 2010).

⁴⁷ 76 Fed Reg 6,756 (Feb. 8, 2011).

⁴⁸ 76 Fed Reg 4,555 (Jan. 26, 2011).

⁴⁹ 76 Fed Reg 17,038 (March 28, 2011).

⁵⁰ 76 Fed Reg 17,047 (March 28, 2011).

⁵¹ See Letter to FSOC from Reps. Randy Neugebauer, chairman, and Michael Capuano, ranking member, House Committee on Oversight and Investigations (May 4, 2011) (requesting that the FSOC repropose rule to give more clarity regarding the criteria and metrics that the FSOC will use in the designation process), available at <http://op.bna.com/bar.nsf/r?Open=jtin-8gzpk4>.

⁵² Section 619 of Dodd-Frank, popularly known as the "Volcker Rule," places limits on the ability of banking entities to engage in proprietary trading activities and hold interests in hedge funds and private equity funds. See "FSOC Study on Implementing the Volcker Rule — A Series of Missed Opportunities and Some Surprises" (Jan. 24, 2011), available at <http://www.shearman.com/fsoc-study-on-implementing-the-volcker-rule—a-series-of-missed-opportunities-and-some-surprises-01-24-2011/>.

⁵³ As required by Dodd-Frank Sections 123 and 946.

⁵⁴ See Dodd-Frank Sections 115(c) and 215.

⁵⁵ See Financial Stability Oversight Council: Dodd-Frank Wall Street Reform and Consumer Protection Act Integrated Implementation Roadmap (Oct. 1, 2010), available at <http://www.treasury.gov/initiatives/Documents/FSOC%20Integrated%20Roadmap%20-%20October%201.pdf>.

⁵⁶ Letter dated Feb. 24, 2011 from Dechert LLP to Treasury Secretary Geithner, available at <http://op.bna.com/bar.nsf/r?Open=jtin-8gzpn6>.

ment as to whether Dodd-Frank requires that all bank holding companies with total consolidated assets in excess of \$50 billion be subject to enhanced measures, or only those financial institutions that could pose a threat to the financial system.⁵⁷ The FSOC has not yet indicated which bank holding companies will be subject to higher prudential standards

Conclusion

The FSOC has a broad array of functions to discharge, but these may be too closely tailored to the per-

⁵⁷ Dodd-Frank Section 115. *See, e.g., Lawyers for Financial Firms Argue FSOC Lacks Legal Power for SIFI Rule*, 96 Banking Rep. (BNA) 373, 3/1/2011 (96 BBR 373, 3/1/11).

ceived causes of the last financial crisis, and not predictive of the next financial crisis. As the FSOC builds up a body of studies, determinations, and rulemakings, we can better discern the contours of its philosophy. All would agree that the FSOC must work to anticipate future crises, but the very features that distinguish it from the PWG may act as constraints rather than virtues. It remains to be seen whether the FSOC will act effectively in the face of a financial meltdown without feeding expectations that the U.S. Government will shield market participants from losses. And ironically, like the PWG, if the FSOC succeeds in averting future crises, we may never know. We hope we do not find out.