



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
INSPECTOR GENERAL

August 24, 2012

OIG-CA-12-006

The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
United States Senate
SD-219 Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Hatch:

This letter and its enclosures respond to your letters of October 18, 2011, and January 18, 2012. In those inquiries, you asked the Council of Inspectors General on Financial Oversight (CIGFO) to review the responses to inquiries that you made to voting members of the Financial Stability Oversight Council (FSOC) in late July and early August of 2011 regarding the debt limit.

Our response to your specific questions is provided as Enclosure 1. Your letters are provided as Enclosure 2.

In preparing our response, we (1) obtained and reviewed relevant information and documentation from the Department of the Treasury (Treasury) and (2) interviewed Treasury officials including the Deputy Assistant Secretary for FSOC, the Deputy General Counsel, senior counsel for the Treasury Office of Banking and Finance, and the Director and Assistant Director of the Office of Fiscal Projections. This work was performed by staff of the Treasury Office of Inspector General under my direction. I shared a draft of this response with the members of CIGFO.

We are also sending a copy of this letter to the Honorable Max Baucus, Chairman, Senate Committee on Finance. We would be pleased to brief you or members of your staff on this response. If you have any questions, you may contact me at

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(202) 622-1090 or a member of your staff may contact Marla Freedman, Assistant Inspector General for Audit, at (202) 927-5400.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric M. Thorson', with a long horizontal flourish extending to the right.

Eric M. Thorson
Chair, Council of the Inspectors General on Financial Oversight
Inspector General, Department of the Treasury

Enclosures

**Response by the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

Request for Information Regarding the Debt Ceiling Issues of 2011

- 1. Determine whether Treasury was internally projecting, using its cash projection models, that it would not have sufficient cash to meet all projected incoming due obligations on July 28, 2011, or any day thereafter, absent an increase to the debt limit.*

We reviewed the Department of the Treasury's (Treasury) daily cash balance projections as of July 21, 2011, for the period July 28 through August 31, 2011. Absent an increase to the debt limit, our analysis of these projections showed that a sufficient cash balance would not be available to meet all incoming due obligations by August 11. Furthermore, we noted that the cash deficit would grow with each day that the debt limit was not raised. The projections assumed that investors would be willing to rollover existing debt that came due during the period. As shown in the August 2, 2011, Daily Treasury Statement, Treasury had an ending cash balance of approximately \$54 billion. According to Treasury officials, had investors not been willing to roll-over debt securities, the cash balance could have been exhausted almost immediately because a payment of \$87 billion would have been needed to pay maturing Treasury securities on August 4, 2011.

Treasury officials stated that prior to August 2, 2011, they were concerned about how investors in Treasury securities might react if the debt limit was not raised by that date. The specific concern was that if the government's borrowing authority were to expire on August 2, investors who ordinarily would roll over maturing Treasury securities (that is, reinvest the proceeds of maturing Treasury securities in new Treasury securities) might choose to invest elsewhere.

Treasury's daily cash balance projections are calculated by the Office of the Fiscal Assistant Secretary (OFAS) and updated on a regular basis. These estimates are based on (1) projected receipts, (2) projected cash outlays for government operations, and (3) projected net cash flows from marketable and non-marketable securities activity.¹ Treasury officials told us that daily

¹ Marketable securities consist of Treasury bills, notes, bonds, and Treasury Inflation-Protected Securities. After original issue by the Treasury, marketable securities can be bought and sold in the

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cash balance projections are inherently imprecise, as there are significant variations in the amount of receipts and expenditures for any given day. According to Treasury officials, the margin of error in these estimates at a 98 percent confidence level is plus or minus \$18 billion for 1 week into the future and plus or minus \$30 billion for 2 weeks into the future.

- 2. Determine what Treasury's daily cash balance projections and daily projections of incoming due obligations were from July 28th through August 30th, 2011.*

We reviewed Treasury's daily cash balance projections and daily projections of incoming due obligations from July 28 through August 31, 2011, as of July 21, 2011. Treasury makes these projections on a daily and monthly basis. We were told that in the days leading up to the debt limit, OFAS ran the daily projections multiple times per day as current information became available. Furthermore, OFAS ran its daily projections under various policy scenarios and finance assumptions. It should be noted that the monthly projection we reviewed, which was run as of July 21, 2011, was predicated on a resumption of borrowing on August 15. With that in mind, some examples of daily cash balance point projections were as follows: \$52.7 billion for July 28; \$20.8 billion for August 4; -\$0.8 billion for August 11; and \$56.5 billion for August 18. As discussed in our response item 1 above, it should also be remembered that there are significant margins of error in these point estimates.

financial marketplace, and ownership is transferable. Non-marketable securities, such as U.S. Savings Bonds, are non-transferable securities issued by the government and registered to the owner. They cannot be sold in the financial market, but they can be redeemed, subject to restrictions. Other types of non-marketable securities include Domestic Series securities, Foreign Series securities, Rural Electrification Authority securities, State and Local Government Securities, and Government Account Series debt.

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3. *On August 1st, was Treasury projecting (point estimate) that its operating cash balance for August 2nd, 2011, would be below its projection of due obligations in the absence of an increase in the statutory debt limit?*

Based on our review of Treasury's daily cash balance projections as of July 21, 2011, for the period July 28 to August 31, 2011, Treasury's operating cash balance for August 2 would not be below its projection of due obligations in the absence of an increase to the statutory debt limit. In fact, based on the document we reviewed, Treasury's estimated daily cash balance was \$69 billion and \$65.6 billion on August 1 and August 2, respectively. Furthermore, a Treasury official told us that Treasury's daily projection produced on August 1 showed that due obligations would not exceed its operating cash balance for August 2. Another Treasury official emphasized to us that Treasury had not stated that the government would be out of cash on August 2, 2011. According to the official, Treasury stated that the government would be out of borrowing authority on that date absent an increase to the statutory debt limit. In this regard, Treasury released statements on June 1 and July 1, 2011, where it announced, and reiterated, that borrowing authority would be exhausted on August 2, 2011. We also noted that Secretary Geithner had publicly emphasized this point as well.

4. *Determine whether there were contingency plans developed by FSOC voting member agencies for disruptions that could have occurred if the debt limit had not been raised and the federal government defaulted or if there was a credit rating downgrade on the U.S.*

According to the Treasury's Deputy Assistant Secretary for FSOC, individual FSOC members recognized the fiscal policy challenge, but there was no collective initiative by FSOC to create an FSOC-directed/coordinated set of contingency plans had the debt limit not been raised. He further stated that although FSOC had conversations regarding the debt limit, creating such contingency plans would be outside of FSOC's authority. FSOC does not interpret its statutory mandate to recommend fiscal policy. According to the Deputy Assistant Secretary for FSOC, FSOC is charged with identifying risks

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and responding to emerging threats to financial stability. In this regard, FSOC did identify and report the threat to financial stability if the debt ceiling was not raised. The Deputy Assistant Secretary for FSOC further stated that it is FSOC's view that Congressional action was the clear response to the debt limit.

Treasury, acting outside of its capacity as a FSOC member, considered a range of options with respect to how Treasury would operate if the U.S. had exhausted its borrowing authority. Treasury considered asset sales; imposing across-the-board payment reductions; various ways of attempting to prioritize payments; and various ways of delaying payments. We were told that similar options had been evaluated by previous administrations during debt limit impasses. That said, Treasury reached the same conclusion that other administrations had reached about these options—none of them could reasonably protect the full faith and credit of the U.S., the American economy, or individual citizens from very serious harm. However, Treasury officials told us that organizationally they viewed the option of delaying payments as the least harmful among the options under review. Ultimately, the decision of how Treasury would have operated if the U.S. had exhausted its borrowing authority would have been made by the President in consultation with the Secretary of the Treasury.

The following describes the various options that were under consideration.

Asset Sales

Treasury officials rejected the option of selling the Nation's gold to meet payment obligations because selling gold would undercut confidence in the U.S. both here and abroad, and would be destabilizing to the world financial system. With respect to the portfolio of mortgage-backed securities owned by Treasury, Treasury officials concluded that a "fire sale" of these assets would be adverse to the interest of taxpayers and could jeopardize the still

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fragile housing market.² Similarly, with respect to investments received in connection with the Troubled Asset Relief Program, Treasury officials determined that a “fire sale” of these investments would not maximize value for the taxpayer and could be detrimental to the economy in general. For both legal and practical reasons, Treasury officials determined that the sale of the government’s portfolio of student loans was not feasible. Moreover, even if Treasury had exercised these options, they would have bought very limited time.

Across-the Board Payment Reductions

After reviewing various ideas for remaining within the debt limit by imposing across-the-board payment reductions (such as cutting all payments by 40 percent or another amount necessary to remain within the debt limit), Treasury officials concluded that such a payment regime would be difficult to implement, as Treasury’s payment systems are not designed to make such across-the-board cuts.

Prioritization of Payments

Treasury officials stated that Treasury also reviewed the idea of attempting to prioritize the many payments made by the federal government each day. Treasury noted that it makes more than 80 million payments per month, all of which have been authorized and appropriated by Congress. According to a

² The Housing and Economic Recovery Act of 2008 (HERA) authorized the Secretary of the Treasury to purchase obligations and securities issued by the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), and the Federal Home Loan Banks. Treasury’s authority to make these purchases ended December 31, 2009. However, Treasury was authorized to sell or otherwise exercise any rights received in connection with these purchases, at any time. Under its HERA authorities, Treasury purchased and sold mortgage backed securities guaranteed by Fannie Mae and Freddie Mac (these securities are referred to as “agency MBS”). In total, before its purchase authority expired, Treasury acquired \$225 billion of agency MBS. Treasury started to sell its agency MBS in March 2011. As of July 2011, Treasury’s reported its agency MBS portfolio holdings were \$82.9 billion. On March 19, 2012, Treasury announced the completion of its sale of remaining agency MBS and reported that overall, cash returns of \$250 billion were received from the agency MBS portfolio through sales, principal, and interest.

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Treasury official, the payments cover a broad spectrum of purposes deemed important by Congress. While Congress enacted these expenditures, it did not prioritize them, nor did it direct the President or the Treasury to pay some expenses and not pay others. As a result, Treasury officials determined that there is no fair or sensible way to pick and choose among the many bills that come due every day. Furthermore, because Congress has never provided guidance to the contrary, Treasury's systems are designed to make each payment in the order it comes due.

Delay of Payments

Treasury officials told us that it was the Department's organizational view that the least harmful option available to the country at the time, of these very bad options, was to implement a delayed payment regime. In other words, no payments would be made until they could all be made on a day-by-day basis. Even under this option, Treasury officials acknowledged that, because the U.S. operates at a deficit, payment delays under such a regime would have quickly worsened each day the debt limit remained at its limit, potentially causing great hardships to millions of Americans and harm to the economy.

5. Provide any contingency plans identified in number 4 above.

As discussed in the response to number 4 above, there was no collective initiative by FSOC to create contingency plans had the debt limit not been raised. That said, Treasury officials did develop various options and scenarios, and seemed to be settling in on a delayed payment regime. However, we were told that there was never a final plan that was presented to the President for approval. Accordingly, based on their description of these documents, we considered them to be pre-decisional, working drafts of options or scenarios, and therefore have no contingency plans to offer.

6. Determine whether the FSOC met its statutory mandate for collective accountability for identifying risks and responding to emerging threats to

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financial stability and whether the FSOC reported on systemic risks surrounding the debt limit impasse.

Based on our review of the applicable sections of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and other relevant documentation, we concluded that FSOC met its statutory mandate for identifying, responding, and reporting on emerging threats and systemic risks to the U.S. with regard to the debt limit impasse.

As mandated by Section 112 of the Dodd-Frank Act, the purpose of FSOC is “to identify risks that could arise from the material financial distress or failure, or ongoing activities, of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace... [and] to respond to emerging threats to the stability of the United States financial system.” Section 112 also requires FSOC to annually report and testify to Congress on, among other things, “potential emerging threats to the financial stability of the United States.”

According to Treasury’s Deputy Assistant Secretary for FSOC, FSOC met its statutory responsibility in its *2011 Annual Report*, where it highlighted the clear need for the debt limit situation to be addressed. The official noted that the risk to financial stability posed by a failure to raise the debt limit is different than other risks to financial stability, as the ability to eliminate the risk is entirely within the control of the U.S. government. If Congress had not raised the debt limit, it was the view that this would have inflicted significant harm on the U.S. and its citizens.

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
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United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

RUSSELL SULLIVAN, STAFF DIRECTOR
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October 18, 2011

The Honorable Eric M. Thorson
Chair, Council of Inspectors General on Financial Oversight
Inspector General, Department of the Treasury
1500 Pennsylvania Avenue, NW
Room 4436
Washington, DC 20220

Dear Chairman Thorson:

I write to ask that the Council of Inspectors General on Financial Oversight review responses provided to inquiries that I made to voting members of the Financial Stability Oversight Council (FSOC) in late July and early August of this year.

During the recent debt limit impasse, I requested information from FSOC members about Treasury's cash and short-term asset positions, projections of Treasury's near-term cash positions and incoming due obligations, and contingency plans of FSOC members in the event that Treasury ran dry of operating cash and lacked additional borrowing authority or in the event of a downgrade of the sovereign debt rating of the United States, among other things. To date, responses I have received have been incomplete and some of my inquiries have been ignored.

As background, in late July and up through August 1st, Congress and the American people were warned during debate over raising the debt limit of an impending cash drought at Treasury that risked a federal default and potential "catastrophe." We also faced the risk of a ratings downgrade on U.S. sovereign debt—a risk that, unfortunately, was realized on the downside.

In the debt limit debate, Congress was in the unfortunate situation of deciding on multi-trillion dollar deficit reduction proposals with only limited information. Indeed, members of Congress were using estimates and projections of Treasury cash flows and obligations produced by a local "think tank" or by major Wall Street financial firms.¹ In addition, there were various press accounts of assurances from Treasury and Federal Reserve (Fed) officials that plans were either in place or being developed for how to address possible destabilizing effects of a lack of increase in the debt limit, default, or a ratings downgrade. To my knowledge, no one has seen those plans outside of Treasury, the regulatory agencies, and, perhaps, Wall Street.

As Ranking Member on the Senate Finance Committee, with responsibility for oversight of Treasury's debt and cash management, I found the lack of information available to Congress unacceptable. Therefore, I wrote a letter to voting members of the FSOC on July 27th.

¹ During the debt limit debate, many members of Congress relied on estimates of Treasury cash flows from the Bipartisan Policy Center, whose analysis can be found at <http://www.bipartisanpolicy.org/library/staff-paper/debt-limit-analysis>. Press reports also identified cash projections by large financial firms suggesting that Treasury would have had ample cash available to pay incoming due obligations well into the month of August, and perhaps beyond.

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My letter (see Attachment A) asks for, among other things, details concerning Treasury's cash and liquid asset positions, projections of those positions for every day through the end of August, and contingency plans of FSOC members for an event in which Treasury runs dry of cash and the debt limit is not raised or an event of a ratings downgrade on U.S. debt and other obligations. I requested a response by 5:00 p.m. on July 28th.

Having received only limited responses from two members of the FSOC by that time, I wrote again on July 29th (see Attachment B). Subsequently, in email and telephone correspondences to my office, the Fed and others deferred to Treasury, and a Treasury official indicated, on July 30th, that a response would be forthcoming but would take time given lags associated with coordinating approval from all members of the FSOC.

In the face of a chorus of dire warnings of catastrophe if the debt limit was not raised, it took five days for Treasury to formulate a response and obtain approval from FSOC members (see the response in Attachment C).² That belated response came within one hour of the House having approved legislation to raise the debt limit.

The response I received was incomplete. Treasury did reconfirm August 2nd as the date it "will exhaust its borrowing authority." Despite my specific question about Treasury's *cash* positions and projections of its cash positions, I received no word on whether Treasury was projecting internally that it would run out of cash at that time—cash flows and positions are not the same as borrowing authority, as Treasury and FSOC officials know. I received no word on Treasury's short-term cash flow projections, aside from identifying such information as "highly market sensitive" and therefore not published.

With warnings that the Treasury could run out of sufficient cash to meet incoming due obligations, and with threats of a U.S. government default, when I first wrote to FSOC members on July 27th, it was reasonable to be concerned that Treasury could run dry of sufficient cash even before August 2nd. Indeed, point-estimate projections of stochastic operating cash balances and incoming due obligations have confidence bands, which means that there may have been a high likelihood of running dry of cash on *any* date beyond July 27th, not merely August 2nd. Prudence dictates adequate planning by Congress and the Treasury for such a contingency. Given my oversight responsibility over Treasury cash management operations, it was necessary for me to know details about Treasury's projected evolution of cash flows and incoming due obligations before August 2nd. I did not obtain the relevant information from any FSOC member.

Note that on a daily basis, Treasury cash managers form estimates of cash balances. Also, each morning before 9:00 a.m., Treasury cash managers and staffers at the Federal Reserve Bank of New York make independent estimates of certain cash balances and compare their estimates

² Dire warnings of catastrophe in the event that the debt limit was not raised or Treasury was to run out of cash include warnings from the President, the Treasury Secretary, the Chairman of the Board of Governors of the Federal Reserve System, and many others. On the floor of the Senate on July 29th (Congressional Record http://frwebgate.access.gpo.gov/cgi-bin/getpage.cgi?position=all&page=S5028&dbname=2011_record) the Senate Majority Leader of the stated that "The country defaults at 12 o'clock on Tuesday [August 2nd] on its debt." Of course, the only thing that could have forced default would have been failure to increase the statutory limit to allow more Treasury borrowing authority *and* insufficient cash at Treasury necessary to pay all due obligations. The open question of whether Treasury would have run dry of sufficient cash on or before August 2nd remains unanswered.

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during a 9:00 a.m. conference call to arrive at a consensus for that day's discretionary cash management action. While daily estimates of cash positions are clearly available, neither those estimates nor any projections of Treasury cash positions that I requested have, to date, been provided to me by anyone on the FSOC.

Note, also, that Treasury debt- and cash-management officials meet on a quarterly basis with the Treasury Borrowing Advisory Committee (TBAC) composed of primary dealers, investment managers, hedge funds, and the like. According to a recent Government Accountability report: "...TBAC meetings are closed due to the sensitivity of the matters under discussion..."³ TBAC is currently chaired by a Managing Director of JPMorgan Chase; the Vice Chair is a Managing Director at Goldman Sachs & Co., and the members include representatives of some of the largest financial institutions in the country.

Based on TBAC Discussion Charts from past meetings (e.g., November 2, 2004 available at <http://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Pages/TBAC-Discussion-Charts.aspx>), data on Treasury's near-term cash projections have in the past been revealed to TBAC members prior to those data being revealed to the general public. My understanding is that Treasury officials and representatives of the largest financial companies in the country discuss "market sensitive" information not contemporaneously available to the Congress or the American people. It appears that Wall Street interests can obtain preferential information advantages over the public and even members of Congress who have oversight responsibility over Treasury operations. Moreover, those large financial firms have preferential access to "market sensitive information" which, according to the Treasury Secretary's responses to my questions, cannot be revealed to Congress, even ex post.

Neither Treasury nor all but one voting FSOC member (the National Credit Union Administration [NCUA]—see the July 28th letter from the NCUA in Attachment D) identified anything about contingency plans they had for the events I inquired about, including any planning for potential disruptions in money markets, the tri-party repo market, systemically important financial utilities, or the payments system.⁴ If Treasury had prioritized payment plans in the event of a government default, I was not informed of any such plans.

Contingency plans for adverse outcomes associated with a Treasury cash drought, a default, or a ratings downgrade, including possible disruptions to markets or the payment system from failure to have raised the debt ceiling, were not revealed to me, despite my requests. Yet press reports

³ See the May 2010 GAO report titled "Debt Management: Treasury Was Able to Fund Economic Stabilization and Recovery Expenditures in a Short Period of Time, but Debt Management Challenges Remain," available at <http://www.gao.gov/new.items/d10498.pdf>.

⁴ My concern about risks to money markets, the payments system, the tri-party repo market and, perhaps, overall financial stability was mirrored in press reports at the time of the debt limit debate in late July and early August. For example, a July 31st New York Times article identified the following (<http://www.nytimes.com/2011/08/01/business/money-market-fund-investors-wary-but-hopeful.html>):

"I don't believe the Treasury markets are going to freeze up," said one federal regulator, who spoke on the condition of anonymity because he feared the knowledge that regulators were watching might cause undue concern about a market segment. "The funds we have talked to are well positioned to substantially handle the kinds of outflows that they have seen recently."

"The greater danger is to money funds with extensive holdings of short-term corporate i.o.u.'s, or commercial paper. Any issuer that enjoys a high credit rating because of implicit or explicit support from the government could be subject to downgrades if the government's rating fell."

"Those include Fannie Mae, one of the big government mortgage companies, whose debts are guaranteed by Washington but which would likely be downgraded as well, and some of the largest banks, which might enjoy an implicit belief that the government would bail them out in a financial crisis, as it did in 2008."

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identify assurances from the Treasury Secretary to the chief executive of JPMorgan Chase, in a July 26th telephone conversation, that Treasury and the Fed had taken steps to keep the payment system functioning smoothly.⁵ At least one regional Federal Reserve Bank official has stated publicly that the Fed and Treasury were working on developing contingency plans for the event of a government default.⁶ Press reports identify the possible existence of a payment prioritization plan at Treasury for the event of a government default.⁷ The minutes of the Federal Reserve's Federal Open Market Committee's meeting of August 9, 2011 identify "plans that the Federal Reserve and the Treasury had developed regarding the processing of federal payments, potential implications for bank supervision and regulatory policies, and possible actions that the Federal Reserve could take if disruptions to market functioning posed a threat to the Federal Reserve's economic objectives." To date, the only response to my request for details of any contingency plans of FSOC members has been the limited response from the NCUA.

Having not received adequate responses to questions I posed to FSOC members, I followed up once again with a letter on August 11, 2011 to the FSOC Chairman (see Attachment E).

The most recent response that I received, from the Treasury Secretary on September 23rd (see Attachment F), provides an elusive response regarding projected cash flows, pointing out what I already acknowledged in my initial request and what is obvious—that projections and forecasts are "uncertain and subject to error." The response identifies no information about contingency plans, aside from an assurance that alternatives were examined. With respect to cash flows at Treasury, the response directs me to Daily Treasury Statements, which identify realizations and not the projections that I seek.⁸

I persist in seeking information about Treasury's cash projections and government contingency plans because:

⁵ See the July 31st New York Times article (<http://www.nytimes.com/2011/07/31/business/wall-street-mobilizes-to-raise-debt-ceiling.html?pagewanted=all>), identifying that: "On Friday, Jamie Dimon, JPMorgan Chase's chief executive, raised concerns with Treasury Secretary Timothy F. Geithner about the standoff over the debt ceiling and its potential to disrupt the system through which JP Morgan and other big banks disburse federal payments. Mr. Geithner assured him that the Treasury and Federal Reserve had taken steps to keep the payment system functioning smoothly, according to individuals briefed on the call." According to an August 4th article in the Wall Street Journal (<http://online.wsj.com/article/SB10091424053111903885604576486613348006704.html>): "Separately, Treasury Secretary Timothy Geithner and J.P. Morgan CEO James Dimon talked twice in the last week about the debt-ceiling deliberations, said people familiar with the conversations. Mr. Dimon called Mr. Geithner last week and the two discussed how the markets were reacting and whether a government default would upend U.S. payment systems. On Monday Mr. Geithner called Mr. Dimon to brief him on the final deal, one of these people said."

⁶ According to a Reuters article on July 21st (<http://www.reuters.com/article/2011/07/22/usa-geithner-bernanke-idUSN1E76K2GA20110722>), "U.S. Treasury Secretary Timothy Geithner will meet with Federal Reserve Chairman Ben Bernanke and New York Federal Reserve Bank President William Dudley on Friday morning, the Treasury said on Thursday... Philadelphia Fed Bank President Charles Plosser told Reuters on Wednesday that the Fed and Treasury were actively engaged in contingency planning for the possibility that the debt ceiling is not raised in time."

⁷ According to a Bloomberg article on July 28th (<http://www.bloomberg.com/news/2011-07-28/u-s-contingency-plan-gives-bondholders-priority.html>): "The U.S. Treasury will give priority to making interest payments to holders of government bonds when due if lawmakers fail to reach an agreement to raise the debt ceiling, according to an administration official... The official requested anonymity because no announcement has been made."

⁸ According to the Daily Treasury Statement for August 1st, the closing balance of Treasury's total operating cash balance was \$68,939 million; according to the Statement for August 2nd, the closing balance was \$54,031 million. These realizations do not, of course, imply that as of August 1st, a cash projection for August 2nd would have indicated that Treasury felt as of the 1st that it would have sufficient cash on the 2nd or beyond necessary to pay incoming due obligations. That is the essence of my request; whether the Treasury was projecting internally a cash drought in the event that the statutory debt limit was not raised. Such projections were almost surely made internally in Treasury using all available information and Treasury's projection models. The confidence bands may have been wide, but the projections were likely made nonetheless. The projections may have had wide associated confidence bands, but they were not impossible to make.

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- I have a responsibility as Ranking Member on the Finance Committee for oversight of Treasury debt and cash operations, and I take that responsibility seriously;
- In the event of a future debt limit impasse, I do not want to again have members of Congress and the public relying on guesses about Treasury's cash position and liquidity from local think tanks or Wall Street firms;
- Lacking information about government contingency plans in, say, the event of a ratings downgrade is unacceptable. Congress and the American people need to know of any government crisis contingency plans that were put in place, and possibly shared with private individuals; and because
- The finances of our Nation's seniors and fighting forces were threatened in the recent debt limit crisis, and I do not want that to happen again. Government officials said there could be no assurances that Treasury would have enough cash available to pay Social Security benefits on August 3rd. Government officials also, by not revealing information that I requested, fostered conditions under which military leaders told our troops that their paychecks could not be guaranteed.⁹

The threats to seniors in Utah and across the country and to our troops around the world were one of the reasons why I wrote my initial letter to the FSOC—to find out just how much cash Treasury had and expected to have in the short run, and how much in liquid assets was available to act to make sure that there was more than enough to pay Social Security benefits and our troops. If, as was being threatened, there was a possibility of cash running dry at Treasury in early August or even late July, I wanted to see the best way forward to gather all available liquidity, get the cash on hand, and make payments.

Treasury at the time held roughly \$80 billion of mortgage-backed securities (MBS) purchased during the financial crisis.¹⁰ Those securities could have been sold at a faster pace than Treasury had been previously making sales, to ensure cash availability. They could perhaps have been used as collateral to obtain cash in the repo market. They could perhaps have been sold to the Federal Reserve at an appropriate haircut.

The FSOC, according to a Treasury document (see Attachment F) “has a clear statutory mandate that creates for the first time collective accountability for identifying risks and responding to emerging threats to financial stability” and would establish processes “for monitoring and reporting on systemic risk, and for monitoring the financial system for emerging risks.” Further, the document identifies that “the FSOC provides new accountability to Congress and the American people to address emerging threats to financial stability...”

Given warnings by the Treasury Secretary of “catastrophic economic consequences that would last for decades” in the event that the debt limit was not raised and the government defaulted on

⁹ The President, in an interview with CBS news on July 12th (<http://www.cbsnews.com/video/watch/?id=7373061n>) stated that he could not guarantee Treasury would have enough cash to pay Social Security benefits on August 3rd. Admiral Mullen warned troops, in the midst of war, that he did not know whether they would be paid for defending our country (see the Congressional Record account at <http://www.gpo.gov/fdsys/pkg/CREC-2011-07-31/pdf/CREC-2011-07-31-pt1-PgS5147-7.pdf#page=1>).

¹⁰ At the end of July (<http://www.treasury.gov/resource-center/data-chart-center/Pages/mbs-purchase-program.aspx>) Treasury held \$82.9, at face value, of agency- (Fannie and Freddie)-guaranteed MBS purchased between October 2008 and December 2009, during the financial crisis. Treasury has been selling its MBS holdings at a pace of roughly \$10 billion or so per month; the largest three purchasers in the period March through August of this year were JPMorgan, Bank of America, and Barclays Capital according to the dealer scorecard available at <http://www.treasury.gov/resource-center/data-chart-center/Documents/August%202011%20Dealer%20Scorecard.pdf>.

Letters to the Chair of the Council of Inspectors General on Financial Oversight and Inspector General of the Department of the Treasury

obligations, it seems clear that FSOC officials perceived a threat to stability. Moreover, there are ample press accounts of concern of FSOC members over potential systemic threats to stability during the impasse and following the subsequent rating downgrade, stemming from possible stresses in money markets, government-debt markets, and the tri-party repo market, among other things. In the face of possible catastrophe, it is not clear why the FSOC as a body was not issuing clear warnings of stability threats outside of its annual report.

I ask that you please provide analyses, responses, and recommendations related to the following requests:

- Generally, I ask that you analyze FSOC responses to my inquiries to FSOC members in my July 27th letter, assess the completeness of those responses, arrive at answers to unanswered questions, and analyze internal procedures of the FSOC leading to a lack of response to clear inquiries from a member of Congress.
 - Included in the answers that I seek is determination of whether, using data that were available and used by Treasury up to and including August 1st and using Treasury's cash projection models, Treasury was internally projecting that it would not have sufficient cash on July 28th or any day thereafter to meet all projected incoming due obligations.
- Investigate what contingency plans were in place at Treasury, the Fed, and other regulatory agencies for disruptions that could have occurred if the debt limit had not been raised and the federal government defaulted or if there was a credit rating downgrade on the U.S., and who was made aware of those plans. Please note that there were ample press accounts of the existence of contingency plans quoting Treasury, Fed, and other regulatory officials. Note, also, the release of one element of what likely was part of regulators' contingency plans on August 5th identifying a regulatory response by the Fed, Federal Deposit Insurance Corporation, NCUA, and Office of the Comptroller of the Currency to the ratings downgrade on government obligations.¹¹
- Assess whether Treasury or any FSOC officials withheld information from Congress—information that my questions specifically requested.
- Determine what were the projections by Treasury staff of daily cash balances and receipts and due obligations of the U.S. Treasury from July 28th through August 30th. Given available data and estimation and projections methods, did those making projections of Treasury's operating cash balances and incoming due obligations project a shortfall of operating cash relative to due obligations for any day from July 28th onward (point estimates)? On August 1st, was Treasury projecting (point estimate) that its operating cash balance for August 2nd would be below its projection of due obligations in the absence of an increase in the statutory debt limit?
- Investigate whether any official at the Treasury, Fed, or any regulatory agency represented on the FSOC revealed to any private party any contingency plan of the government that was not made publicly available related to disruptions that could have occurred from the debt limit impasse, from Treasury running dry of cash, from a U.S. government debt default, or from a downgrade of a rating on U.S. sovereign debt obligations. In your investigation,

¹¹ See, for example, the Federal Reserve press release at <http://www.federalreserve.gov/newsevents/press/bcreg/20110805a.htm>.

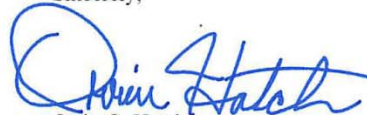
**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

please include consideration of any information made available to TBAC members by Treasury officials or any other public officials.

- Investigate whether Treasury could have sold some or all of its stock of MBS to obtain cash to pay seniors and our troops, if necessitated by a cash drought, or could have posted them as collateral to obtain cash in the repo market, or could have agreed upon a price with the Fed and sold them to the Fed. I am *not* asking for Treasury's assessment of potential impacts on volatility in the MBS or other markets of accelerated MBS sales relative to Treasury's historic pace of sales.
 - Include in your investigation an assessment of whether Treasury could have sold or otherwise used MBS to obtain cash, used the proceeds to pay Social Security benefit payments that were due on August 3rd, and correspondingly extinguished a like amount of debt held by the Social Security Trust Fund. That action would have opened up a like amount of headroom under the statutory debt limit, which would have allowed for a subsequent ability to borrow a like amount using fresh debt. The result would have been payment of Social Security benefits due on August 3rd with no net effect on where the Treasury stood relative to the statutory debt limit and no breach of the statutory debt limit. That is, Social Security payments due on August 3rd could have been assured.
- Assess whether the FSOC met its statutory mandate for collective accountability for identifying risks and responding to emerging threats to financial stability, whether the FSOC appropriately reported on systemic risk, and whether the FSOC proved appropriately accountable to Congress and the American people during the debt limit impasse (during which Treasury officials and others warned of "catastrophic" outcomes) and the subsequent rating downgrade on U.S. sovereign debt.
- Based on your reviews, investigations, and assessments, please make recommendations on how to improve FSOC accountability to Congress and the American people regarding threats to stability of the financial system, including threats emanating from U.S. government fiscal policy, the federal debt position, or monetary policy.

Thank you for your consideration. I respectfully ask that my request be handled in an expedient manner. Please have representatives of your office contact Jeff Wrase (202-224-4515) to coordinate a mutually agreeable timeline.

Sincerely,



Orrin G. Hatch
Ranking Member

cc: Marla A. Freedman

Letters to the Chair of the Council of Inspectors General on Financial Oversight and Inspector General of the Department of the Treasury

MAX BAUCUS, MONTANA, CHAIRMAN
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RUSSELL SULLIVAN, STAFF DIRECTOR
CHRIS CAMPBELL, REPUBLICAN STAFF DIRECTOR

United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

July 27, 2011

The Honorable Timothy Geithner
Secretary
Department of the Treasury
1500 Pennsylvania Ave. NW
Washington, DC 20220

The Honorable Ben Bernanke
Chairman, Board of Governors
The Federal Reserve System
20th Street and Constitution Ave. NW
Washington, DC 20551

The Honorable Gary Gensler
Chairman
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street NW
Washington, DC 20581

The Honorable Mary Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Martin J. Gruenberg
Acting Chairperson
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Edward DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street NW, 4th Floor
Washington, DC 20552

The Honorable Debbie Matz
Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

John Walsh
Acting Comptroller
Office of the Comptroller of the Currency
250 E Street SW, Room 9048
Washington, DC 20219

Dear Secretary Geithner, Chairmen Bernanke, Gensler, Matz, Shapiro, Acting Chairperson Gruenberg, Acting Director DeMarco, and Acting Comptroller Walsh:

The President, on July 25, spoke to the American public about risks associated with failure to raise the statutory debt limit, saying that: "We would risk sparking a deep economic crisis..." The President warns of a deep crisis and risks to financial stability.

You, the voting members of the Financial Stability Oversight Council (FSOC), are charged by the Dodd-Frank Wall Street Reform and Consumer Protection Act with the responsibility to identify risks and potential emerging threats to the financial stability of the United States.

- Does the Council agree with the President's assessment that possible failure to raise the statutory debt limit by sometime in early August represents an emerging threat to the financial stability of the United States?

Letters to the Chair of the Council of Inspectors General on Financial Oversight and Inspector General of the Department of the Treasury

- Does any voting Council member dissent from whatever is the majority view of the Council? If so, please explain precisely why.

Neither the Minutes of the FSOC July 13, 2011 meeting nor the Annual Report of the FSOC, which was approved on July 22, 2011, identify possible failure to raise the statutory debt limit by August 2 as an imminent risk to the financial stability of the United States worthy of a warning to the American people, and do not come close to recent statements by Treasury officials warning of “catastrophe.”

In addition to inquiring about the Council’s views on possible risks to financial stability, I write to ask the Council and its voting members about their current knowledge of recent Treasury cash inflows and outflows and projections of those cash flows, daily, through the month of August.

Treasury officials have warned that based on actual and projected revenues and expenditures, along with potential exhaustion of available “extraordinary measures” to avoid breach of the statutory debt limit, the United States will exhaust its borrowing authority under the limit and possibly run out of available cash to pay obligations of the federal government that are due.

Unfortunately, Congress and the American people do not have sufficient information about Treasury’s actual and projected revenues, expenditures, and cash flows to make informed judgments. Many Americans and members of Congress are, unfortunately, relying on estimates and projections from either large Wall Street financial institutions or non-governmental organizations often labeled “think tanks.” The lack of information is unsatisfactory.

In a May 2, 2011 letter to Congress, Treasury Secretary Geithner stated the as a result of stronger than anticipated tax receipts, Treasury then estimated that extraordinary measures to provide headroom under the statutory debt limit would be exhausted on August 2, 2011. Since that time, more data have become available. Some reports since that time have indicated that receipts may have been turning out higher than previously expected. Further, the Federal Reserve’s July 2011 Monetary Policy Report to the Congress identifies that “Federal receipts have risen rapidly lately—they are up about 10 percent in the first eight months of fiscal 2011 compared with the same period in fiscal 2010.”

I recognize that receipts and Treasury’s cash inflows and outflows can be lumpy and are stochastic. However, the date at which extraordinary measures available to Treasury become exhausted, and cash inflows may prove insufficient to meet incoming obligations that are due, has almost surely changed from the August 2 date estimated by Treasury on May 2. Given incoming data since May 2, does August 2 remain the date with the highest statistical likelihood of being the point in time at which Treasury will run out of extraordinary measures to provide additional headroom under the debt limit and will face insufficient cash inflows relative to obligations that are coming due?

Please provide, by 5:00 p.m., Eastern Standard Time on Thursday, July 28, detailed information known by the Council and by any voting member on:

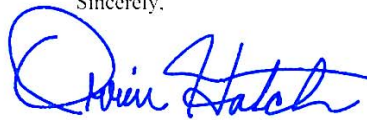
- Actual revenues and expenditures through July 27;
- Projected or actual daily Treasury cash inflows and outflows for each day between July 28 and August 31, along with methods used to make projections;

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

- Whether, given current projections of cash inflows and obligations coming due, Treasury would run out of cash and not have sufficient cash available to meet all obligations that become due on any date between August 2 and August 31 (projections here mean point estimates, with the acknowledgement that projections are inherently uncertain);
- Any cash or liquid accounts available (presently or any time during August) to Treasury, such as Treasury's \$5 billion liquid balance sitting idle in its Supplementary Financing Program Account at the Federal Reserve, established to allegedly assist the Federal Reserve with management of its balance sheet during the financial crisis (the Daily Statement of cash and debt operations of the United States Treasury for Monday, July 25, 2011 indicates that the \$5 billion was available to Treasury on that date) ;
- Current values of securities and other marketable assets available (presently or any time during August) to Treasury, including mortgage-backed-securities and other financial claims amassed by Treasury during the recent financial crisis, which could be liquidated and converted to cash (my request is for total values, not an assessment of the advisability of asset sales);
- Contingency plans for generation of cash within Treasury in the event that the statutory debt limit is not raised by August 2, 2011;
- Contingency plans of regulators of financial institutions, including any plans for regulatory forbearance, in the event of a ratings downgrade of United States Treasury debt securities;
- Contingency plans of the Federal Reserve System and the Federal Reserve Bank of New York in the event of a ratings downgrade of United States Treasury debt securities, including plans related to "breaking of the buck" by a money market mutual fund, disruptions in the tri-party repo market, disruptions in payment systems or systemically important financial utilities, or creation of programs or facilities with broad-based eligibility under authorities provided by Section 1101 of the Dodd-Frank Wall Street Reform and Consumer Protection Act;
- Any private assurances by any government officials to any financial institution or significant financial market participant that the United States Treasury will not fail to pay principal and interest on Treasury securities even if the statutory debt limit is not raised.

As Ranking Member of the Senate Finance Committee, with a responsibility for oversight of our sovereign debt and Treasury's cash management practices, I am deeply concerned about the lack of information about upcoming cash flows and reliance of Congress and the American people on non-governmental projections of those flows in decision making. Time is of the essence, and I require, as I stated, the information that I have requested by 5:00 p.m. Eastern Standard Time on Thursday, July 28. Please contact Jeff Wrase at 202-224-4515.

Sincerely,



Orrin G. Hatch
Ranking Member

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

MAX BAUCUS, MONTANA, CHAIRMAN
JOHN D. ROCKEFELLER IV, WEST VIRGINIA
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RUSSELL SULLIVAN, STAFF DIRECTOR
CHRIS CAMPBELL, REPUBLICAN STAFF DIRECTOR

United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

July 29, 2011

The Honorable Timothy Geithner
Secretary
Department of the Treasury
1500 Pennsylvania Ave. NW
Washington, DC 20220

The Honorable Ben Bernanke
Chairman, Board of Governors
The Federal Reserve System
20th Street and Constitution Ave. NW
Washington, DC 20551

The Honorable Gary Gensler
Chairman
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street NW
Washington, DC 20581

Martin J. Gruenberg
Acting Chairperson
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Edward DeMarco
Acting Director
Federal Housing Finance Agency
1700 G Street NW, 4th Floor
Washington, DC 20552

The Honorable Mary Schapiro
Chairman
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

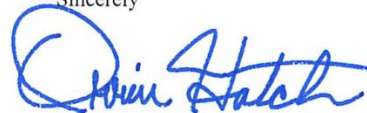
Dear Secretary Geithner, Chairmen Bernanke, Gensler, Shapiro, Acting Chairperson Gruenberg, and Acting Director DeMarco:

I requested information from you in a letter dated July 27, but have not received a response from you. The request I made of you sought information about, among other things, the short-term cash and liquidity positions of the U.S. Treasury, current projections of those positions, information about contingency plans in the event of cash shortages at Treasury or a ratings downgrade.

The information I requested includes data that are necessary for Congress to proceed to have an informed debate, with the most accurate and timely data available, over the debt limit. I ask that you respond to my request without delay—contact information was provided in my prior letter.

As my Wednesday letter stated quite clearly: Time is of the essence. Your lack of response to my request is unacceptable.

Sincerely



Orrin G. Hatch
Ranking Member

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

SECRETARY OF THE TREASURY

August 1, 2011

The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
United States Senate
Washington, DC 20510

Dear Senator Hatch:

Thank you for your letter to me and the other members of the Financial Stability Oversight Council (the Council) regarding the threat that a possible failure to raise the statutory debt limit poses to the financial stability of the United States.

Your letter asks whether the Council has considered the risks associated with not raising the debt limit and its implications for our Nation's financial stability. The Council is taking the possible failure to raise the debt limit extremely seriously. As you note, the Council unanimously approved its first annual report on July 22, 2011. The report discusses this substantial risk to the financial stability of the United States in the final paragraph of the Executive Summary:

The recent financial crisis provides a stark illustration of how quickly confidence can erode and financial contagion can spread, as well as how challenging and expensive it is to repair the damage. This lesson is important to bear in mind in the current debate over the increase in the federal government's debt limit. It is vital to the stability of the U.S. financial system and the global financial system for the debt limit to be raised in a timely manner to avoid creating any risk of default on U.S. obligations.

In short, a possible failure to raise the debt limit poses the most immediate threat that we face to the financial stability of the United States.

Your letter also inquires about Treasury's cash balances. The most accurate and up-to-date source of information about Treasury's cash position is the Daily Treasury Statement, which is made public every day and is available at: <http://www.fms.treas.gov/dts/index.html>. In addition to providing opening and closing cash balances, the Daily Treasury Statement provides detailed information about inflows and outflows, including tax deposits and refunds. For example, you inquired about Treasury's \$5 billion balance in the Supplementary Financing Account at the Federal Reserve. The Daily Treasury Statement for July 28, 2011 shows that the remaining \$5 billion in that account has been drawn down.

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**


As you recognize, predicting actual cash inflows and outflows on a daily basis is imprecise and subject to considerable fluctuation. Such information is also highly market sensitive. For these reasons, we do not publish estimates of daily cash flows. We do, however, publish quarterly borrowing estimates which provide an aggregated estimate of borrowing needs for the current and subsequent fiscal quarters. Our most recent borrowing estimate was issued today. Quarterly borrowing estimates are available on our website at: <http://www.treasury.gov/resource-center/data-chart-center/quarterly-refunding/Pages/Latest.aspx>.

With respect to your inquiry about marketable securities held by Treasury, as of the end of July, we held approximately \$82.9 billion in agency mortgage-backed securities (MBS). When we began disposing of the MBS portfolio in March 2011, we made clear to the market that we would sell up to \$10 billion of these securities per month. We believe that the clarity that we have provided the market about the plans for the orderly disposition of the MBS portfolio has maximized returns for taxpayers. A fire sale of this mortgage portfolio or any of the government's other assets (including gold, student loans, and any of the other assets acquired as part of the market stabilization policies in 2008 and 2009) would be highly disruptive to the market and would not be in taxpayers' best interest. We provide monthly updates about the remaining value of the portfolio at: <http://www.treasury.gov/resource-center/data-chart-center/Pages/mbs-purchase-program.aspx>.

Your letter also asks whether August 2 remains the date that Treasury will exhaust its borrowing authority. Regarding this date and Treasury's policy on notifying Congress and the public about when the federal government will exhaust its borrowing authority under the debt limit, Treasury has attempted to provide as much transparency as possible throughout this process. Since my May 2, 2011 letter to Congress, we have reconfirmed the August 2 date on June 1, July 1, and most recently on July 27. August 2 remains the date when we expect to exhaust the extraordinary measures we have employed to extend our borrowing authority in the absence of congressional action to increase the debt limit.

Finally, you ask about the President's assessment that failure to raise the debt limit "would risk sparking a deep economic crisis." I strongly agree with that view. Only an act of Congress can ensure that we meet our obligations on time, and the leadership of both parties in both houses of Congress has committed to the country and to the President that they will not allow the country to default for the first time in our history. The time to deliver on that commitment is now.

Sincerely,



Timothy F. Geithner

cc: The Honorable Ben Bernanke
The Honorable Gary Gensler
The Honorable Mary Schapiro
The Honorable Debbie Matz
Mr. Martin J. Gruenberg
Mr. Edward DeMarco
Mr. John Walsh

Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury



Office of the Chairman

National Credit Union Administration

July 28, 2011

The Honorable Orrin G. Hatch
Ranking Member
U.S. Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510-6200

Dear Senator Hatch:

Thank you for contacting the National Credit Union Administration (NCUA) and the other members of the Financial Stability Oversight Council (FSOC) about the risks that a failure to address the federal government's debt ceiling poses to the stability of our financial system. We have discussed these matters within the FSOC, and I remain very much focused on this critically important issue.

Earlier this week, the FSOC released its first annual review about emerging risks in the financial system. Regarding the need to raise the debt ceiling, the report's Executive Summary notes:

"The recent financial crisis provides a stark illustration of how quickly confidence can erode and financial contagion can spread, as well as how challenging and expensive it is to repair the damage. This lesson is important to bear in mind in the current debate over the increase in the federal government's debt limit. It is vital to the stability of the U.S. financial system and the global financial system for the debt limit to be raised in a timely manner to avoid creating any risk of default on U.S. obligations."

Economic security and financial stability depend, in large part, on public and investor confidence. Confidence in U.S. Treasury obligations and by extension the full faith and credit of the U.S. Government is therefore absolutely vital to domestic and global financial stability. We cannot take this trust for granted.

Any failure to raise the statutory debt limit would undermine investor confidence, result in sharp increases in government and private borrowing costs, and—in my estimation—create a severe economic downturn producing higher unemployment rates. As noted last month by Treasury Secretary Timothy Geithner in a letter to Senator Jeff Sessions, the failure to increase the debt limit would also make it more expensive for Americans to start and grow businesses, send their children to college, pay their credit card bills and purchase homes. In short, I agree with the President, Secretary Geithner, and other members of the FSOC that a failure to raise the statutory debt limit and the economic consequences would be severely destabilizing for the U.S. economy.

Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury

page 2
Senator Orrin G. Hatch

According to NCUA's Office of the Chief Economist, a failure to raise the statutory debt limit will dampen the ongoing recovery of the credit union system from the 2008 financial crisis. In addition, failing to raise the statutory debt limit will result in an increase in interest rates, higher unemployment, and weaker consumer demand. This in turn will bring about weak loan demand, higher delinquencies, increased bankruptcies, and balance sheet stress.

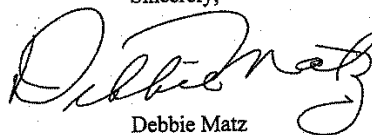
In your letter you further ask about the contingency plans of financial regulators in the event of a downgrade of U.S. Treasury obligations by credit rating agencies. NCUA has initiated efforts to address a failure to increase the debt ceiling, any default on U.S. Treasuries, and any downgrade issued by credit rating agencies. Specifically, NCUA is working to ensure that the U.S. credit union system remains strong, continues to be well capitalized, and maintains sufficient liquidity to deal with debt ceiling related contingencies.

As a group, credit unions reported an aggregate capital buffer of nearly 10 percent at the end of March 2011—substantially higher than the 7 percent statutory minimum to be considered well capitalized. Additionally, the credit union system currently has nearly \$89 billion in cash on hand, as well as the capacity to offer loans to their members needing short-term help and to cover anticipated withdrawal requests.

NCUA is also working to ensure that consumers understand that their accounts at credit unions remain safe, insured and protected up to \$250,000. The security provided by federal deposit insurance matters greatly to consumers, especially during times of turmoil. To avoid any consumer confusion about the link between deposit insurance and the full faith and credit of the U.S. Government, it is imperative that Congress raise the debt ceiling on or before August 2.

In sum, a failure to address the debt ceiling would have very serious consequences for the broader economy and financial stability. I urge Congress to act as expeditiously as possible to increase the debt ceiling and reaffirm the trust investors all over the world have placed in the full faith and credit of the United States.

Sincerely,



Debbie Matz
Chairman

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

MAX BAUCUS, MONTANA, CHAIRMAN
JOHN D. ROCKEFELLER IV, WEST VIRGINIA
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JOHN F. KERRY, MASSACHUSETTS
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TOM COBURN, OKLAHOMA
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RICHARD BURR, NORTH CAROLINA

United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

RUSSELL SULLIVAN, STAFF DIRECTOR
CHRIS CAMPBELL, REPUBLICAN STAFF DIRECTOR

August 11, 2011

The Honorable Timothy Geithner
Secretary, Department of the Treasury
Chairperson, Financial Stability Oversight Council
1500 Pennsylvania Ave. NW
Washington, DC 20220

Dear Secretary Geithner:

You wrote, on August 1st, a belated and incomplete response to my July 27th inquiry to Financial Stability Oversight Council (FSOC) members concerning Treasury's short-term cash and liquid asset positions, near-term projections of those positions, and contingency plans for events such as a ratings downgrade. Some of my inquiries seem to have simply been ignored. I write again for a more complete response.

Your letter reconfirmed August 2nd as the date Treasury "will exhaust its borrowing authority." No word on whether that means running out of cash at that time, despite my having specifically requested confirmation of August 2nd as Treasury's estimate of the most likely date of cash exhaustion. No word on Treasury's short-term cash flow projections, aside from identifying them as "highly market sensitive" and therefore not published. No word on contingency plans for the events I inquired about, including a ratings downgrade on U.S. debt.

Disturbingly, a July 30th article in the New York Times indicates that assurances were made by you to the Chief Executive of JPMorgan Chase that Treasury and the Fed had taken steps to keep the payment system functioning smoothly. Perhaps Wall Street has learned more than I have.

According to Treasury's website: "The FSOC provides new accountability to Congress and the American people to address emerging threats to financial stability and to coordinate regulatory actions to address them." I do not believe that the FSOC has followed through in any meaningful way on this promise. I do believe that claims by the FSOC to provide "for the first time, comprehensive monitoring to ensure the stability of our nation's financial system" are overly heroic and illusory.

The American people and Congress faced a considerable threat to stability from the possibility that the U.S. Treasury would have been forced to default on obligations on August 2nd, as you had been warning for some time. Was it the case that Treasury, on the August 1st date of your response to my inquiry, still projected August 2nd as its point estimate of the statistically most likely date at which Treasury would run out of cash and not have enough available to meet all incoming due obligations? Treasury's opening operating cash balance was \$68.939 billion and its closing balance was \$54.031 billion on August 2nd.

Letters to the Chair of the Council of Inspectors General on Financial Oversight and Inspector General of the Department of the Treasury

Your response concerning cash flows was elusive, identifying August 2nd as still being the date that Treasury expected “to exhaust the extraordinary measures we have employed to extend our borrowing authority in the absence of congressional action to increase the debt limit.” I asked about projections of cash exhaustion and not solely about exhaustion of measures to extend borrowing authority. Treasury could have exhausted those measures, yet still have expected sufficient cash inflows to cover expected payments of obligations that became due.

Your letter states that Treasury does not publish estimates of daily cash flows, because the information is “highly market sensitive.” I presume this means, also, that estimates of near-term cash flows are not revealed during meetings, such as the one on August 3rd, of the Treasury Borrowing Advisory Committee, composed of members that include several large Wall Street interests. I presume that the expected near-term cash position of the U.S. Treasury in the days and weeks prior to August 2nd was not discussed by Treasury or any federal financial regulator with anyone in the private sector. And, I presume that August 2nd is independently confirmable as the statistically most likely date at which Treasury expected, as of August 1st, to have run out of cash sufficient to meet all due obligations.

In the event of a future debt limit impasse, with default hanging in the balance, it appears that Congress and the public will have to again rely on estimates of Treasury’s short-term finances from think tanks and Wall Street. If the information is too “market sensitive” to share, how can Social Security recipients, our troops, or anyone worried about being paid by government know what to expect? If FSOC members have information about Treasury’s short-term finances or about their own crisis contingency plans, what are the obstacles to revealing that information? Perhaps Council members feel compelled not to reveal information out of concern over unwarranted speculation. Perhaps they are concerned that revealing information could spark panic and contribute to the very instability they are charged to guard against. It will be instructive to find out.

My request for information about contingency plans for an event of a downgrade of the U.S. sovereign credit rating was issued, in part, to avoid a repeat of the destabilizing government reactions to events observed during the recent financial crisis. Congress and the public were often informed of government plans and actions in cryptic, last-minute press releases from financial regulators. Market participants and the public did not understand what the plans of government and regulators were to address systemic instability. The added uncertainty about those plans on how to address evolving instability seems to unnecessarily add to instability.

I asked on July 27th for contingency plans regarding a ratings downgrade. It was not until August 5th, *after* the Standard & Poor’s (S&P) downgrade of the sovereign credit rating of the U.S., that I learned from yet another set of cryptic, last-minute press releases about regulatory guidance from the Federal Reserve Board, Federal Deposit Insurance Corporation, NCUA, and OCC. It was not until August 8th that I learned from a joint statement of “G7” finance ministers and central bank governors, including you and Federal Reserve Chairman Bernanke, of a commitment to taking “coordinated action where needed, to ensuring liquidity, and to supporting financial market functioning, financial stability and economic growth.” I still do not know exactly what that commitment would entail.

Letters to the Chair of the Council of Inspectors General on Financial Oversight and Inspector General of the Department of the Treasury

Following the S&P downgrade, it is important to bear in mind that other major ratings agencies have also issued downgrade warnings. S&P itself warns of further downgrades. Thus, the threat to systemic stability and to the depth and liquidity of markets for U.S. Treasury securities from additional possible ratings downgrades remains. Yet I still have not been fully informed by FSOC members about any plans that they have to address such a contingency and help preserve the integrity of markets for Treasury securities.

The consequences of further ratings downgrades would likely be significant, and could include runs on money market funds, disruptions in the tri-party repo market, and precipitous increases in borrowing costs for all Americans. Those developments could lead to more bailouts, special lending facilities, and other “backstops” observed during the recent financial crisis. I reiterate my request for information about contingency plans of members of the FSOC to address possible threats to stability from downgrades of the U.S. sovereign rating.

I continue to seek information about Treasury’s cash positions and government contingency plans for a number of reasons. First, transparency is essential wherever possible.

Second, I have oversight responsibility as Ranking Member on the Finance Committee of Treasury debt and cash operations, and I take that responsibility seriously to ensure preservation of the depth and liquidity in markets for Treasury securities.

Third, we may again have a debt limit impasse in the event of unexpectedly sluggish economic activity and receipts, or if Congress fails to follow through on deficit reduction called for in the recent debt limit legislation. I wish to avoid having Congress and the public relying on guesses about Treasury’s cash position and liquidity from think tanks and Wall Street firms.

Fourth, lacking information about government contingency plans in the event of further ratings downgrades puts us back in the crisis setting where government officials react sporadically and unexpectedly at the last minute to imminent threats to stability. We need to know about any plans in place or, if those plans are cloaked behind regulators’ concerns about market sensitivity, we need to know why.

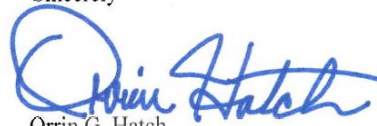
Fifth, it is unacceptable that our seniors and fighting forces were used as political poker chips in the recent debt limit crisis, and I do not want a repeat. The President unnecessarily struck fear into the financial outlook of seniors in Utah and across the country by saying that he could not guarantee that Treasury would have enough cash available to pay Social Security benefits on August 3rd. He also needlessly allowed conditions under which our military leaders told troops that their paychecks could not be guaranteed.

The threats to seniors relying on timely Social Security benefit payments and to our troops around the world were unconscionable. They were important reasons why I wrote my letter to the FSOC—to find out just how much cash Treasury had and expected to have over the short run, and how much in liquid assets was available to act to ensure ample resources for payments to troops, Social Security recipients, and others.

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

I urge you to carefully review questions that I raise above and questions I initially posed in my July 27th letter to FSOC members. I do not believe that you responded to several questions that I posed, and request that you do so. For contact information, please refer to my July 27th letter.

Sincerely



Orrin G. Hatch
Ranking Member

Cc: The Honorable Ben Bernanke
The Honorable Gary Gensler
The Honorable Mary Schapiro
The Honorable Debbie Matz
Mr. Martin J. Gruenberg
Mr. Edward DeMarco
Mr. John Walsh

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

**DEPARTMENT OF THE TREASURY
WASHINGTON D.C.**

SECRETARY OF THE TREASURY

September 23, 2011

The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
United States Senate
Washington, DC 20510

Dear Senator Hatch:

I am writing in response to your letter of August 11, 2011 regarding the recent debate on the statutory debt limit.

In your letter you asked for a specific date when Treasury would have exhausted its cash, absent passage of the debt limit increase in the BCA. It is not possible for us to estimate this with any precision because the rate at which cash would have been drawn down would have depended on factors that were inherently unpredictable, such as the willingness of investors to re-invest in, or "roll over," Treasury securities. If investors had become less willing to loan the United States money in light of the uncertainty surrounding the exhaustion of borrowing authority, the United States could have exhausted its entire cash balance on a single day. This uncertainty and risk to the full faith and credit of the United States underscores why it was critical that Congress raise the debt limit.

You also raised the issue of Treasury's ability to provide cash flow projections. Any such projection is merely a forecast of the future and is therefore, by definition, uncertain and subject to error. Treasury's cash flow projections can also rely on information that is sensitive or that has not been released to the public, such as planned transactions whose premature disclosure would be market sensitive, or policy changes that have not yet been publicly announced, such as the recent sale of some oil reserves. In addition, various government entities that both remit their cash to the Treasury and rely on the Treasury for their funding needs could alter their behavior should they anticipate a risk that insufficient cash might be available during a debt limit impasse to meet their requirements. Such behavior, such as withholding payments or accelerating cash draws, could accelerate the date on which the debt ceiling would be reached.

Rather than providing forecasts of the future, Treasury publishes its actual cash position each day in the Daily Treasury Statement. This daily statement reflects our commitment to make the most timely and accurate information publicly available regarding Treasury's cash balance, deposits and withdrawals, and debt transactions.

Finally, you also asked about contingency plans for generation of cash within Treasury in the event that the statutory debt limit was not raised by August 2, 2011. As Treasury has stated repeatedly, we examined all known alternatives for funding government operations and meeting

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

our obligations beyond August 2, including the sale of gold and various other ideas. Like all previous Treasury Secretaries of both parties who have faced debt limit impasses, I concluded that there were no other options that were prudent or feasible. For this reason, as Treasury consistently maintained during the course of the debate last spring and summer, there was no alternative except enactment of an increase in the debt limit.

I appreciate the opportunity to respond to your questions and would of course be pleased to discuss these issues or any other matters of concern with you at your convenience.

Sincerely,



Timothy F. Geithner

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

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United States Senate

COMMITTEE ON FINANCE
WASHINGTON, DC 20510-6200

RUSSELL SULLIVAN, STAFF DIRECTOR
CHRIS CAMPBELL, REPUBLICAN STAFF DIRECTOR

January 18, 2012

The Honorable Eric M. Thorson
Chair, Council of Inspectors General on Financial Oversight
Inspector General, Department of the Treasury
1500 Pennsylvania Avenue, NW
Room 4436
Washington, DC 20220

Dear Chairman Thorson:

I write to follow up on my October 18, 2011 letter asking that the Council of Inspectors General on Financial Oversight (CIGFO) review responses provided to inquiries that I made to voting members of the Financial Stability Oversight Council (FSOC) in late July and early August of last year during the debt limit impasse.

Your staff and mine seem to have converged on a refined set of specific questions that I request the CIGFO to address. Please do, however, use the detailed exposition of developments surrounding the debt limit impasse contained in my prior letter for background information.

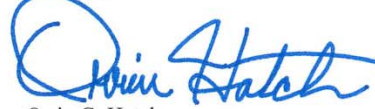
Please address the following questions:

1. Determine whether Treasury was internally projecting, using its cash projection models, that it would not have sufficient cash to meet all projected incoming due obligations on July 28, 2011, or any day thereafter, absent an increase to the debt limit.
2. Determine what Treasury's daily cash balance projections and daily projections of incoming due obligations were from July 28th through August 30th, 2011.
3. On August 1st, was Treasury projecting (point estimate) that its operating cash balance for August 2nd, 2011, would be below its projection of due obligations in the absence of an increase in the statutory debt limit?
4. Determine whether there were contingency plans developed by FSOC voting member agencies for disruptions that could have occurred if the debt limit had not been raised and the federal government defaulted or if there was a credit rating downgrade on the U.S.
5. Provide any contingency plans identified in number 4 above.
6. Determine whether the FSOC met its statutory mandate for collective accountability for identifying risks and responding to emerging threats to financial stability and whether the FSOC reported on systemic risks surrounding the debt limit impasse.

**Letters to the Chair of the Council of Inspectors General on Financial Oversight
and Inspector General of the Department of the Treasury**

Thank you for your consideration. I respectfully ask that my request be handled in an expedient manner. Please have representatives of your office contact Jeff Wrase (202-224-4515) if you have any questions.

Sincerely,



Orrin G. Hatch
Ranking Member

cc: Marla A. Freedman
Robert A. Taylor



OFFICE OF
INSPECTOR GENERAL

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 24, 2012

The Honorable Max Baucus
Chairman
Committee on Finance
United States Senate
SD-219 Dirksen Senate Office Building
Washington, DC 20510-6200

Dear Chairman Baucus:

In my letter of January 19, 2012, I informed you that the Honorable Orrin G. Hatch, Ranking Member, had asked me as Chair of the Council of Inspectors General on Financial Oversight (CIGFO) and Inspector General of the Department of the Treasury to review responses provided to inquiries that he made to the voting members of the Financial Stability Oversight Council in late July and early August of last year, regarding the debt limit.

Enclosed please find a copy of my response to Ranking Member Hatch.

If you have any questions, you may call me at (202) 622-1090, or a member of your staff may call Marla A. Freedman, Assistant Inspector General for Audit, at (202) 927-5400.

Sincerely,

Eric M. Thorson
Chair, Council of Inspectors General on
Financial Oversight
Inspector General, Department of the Treasury

Enclosure