

# United States Senate

WASHINGTON, DC 20510

COMMITTEES:  
APPROPRIATIONS  
BUDGET  
ENVIRONMENT AND  
PUBLIC WORKS  
FOREIGN RELATIONS

May 31, 2019

The Honorable Jerome H. Powell  
Chairman  
Federal Reserve Board  
20<sup>th</sup> Street and Constitution Avenue, N.W.  
Washington, D.C. 20551

The Honorable Jay Clayton  
Chairman  
Securities and Exchange Commission  
100 F Street, N.E.  
Washington, DC 20549-1090

The Honorable Jelena McWilliams  
Chair  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, N.W.  
Washington, D.C. 20429

The Honorable J. Christopher Giancarlo  
Chairman  
Commodity Futures Trading Commission  
1155 21<sup>st</sup> Street, N.W.  
Washington, D.C. 20581

The Honorable Joseph M. Otting  
Comptroller  
Office of the Comptroller of the Currency  
400 7th Street, S.W.  
Washington, D.C. 20219

Dear Chairman Powell, Chair McWilliams, Comptroller Otting, Chairman Clayton, and Chairman Giancarlo:

I am deeply troubled by recent news reports suggesting that your agencies, which are charged with enforcing Section 619 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, also known as the Volcker Rule, may be on the verge of adopting changes to the rule that are even more damaging to its core than your ill-founded 2018 proposal.<sup>1</sup> If true, your actions would constitute another attempt to undermine a critical provision of the law that seeks to prevent banks from gambling with depositor funds and putting taxpayers at risk.

Over the past few months, while your agencies have worked towards weakening the Volcker Rule to allow banks a free hand to profit from speculative trading, it seems that you have ignored a growing body of evidence suggestive of certain banks' substantial non-compliance with the rule. Although not conclusive, this evidence should have prompted your agencies to dig deeper and, where appropriate, enforce the Volcker Rule's relevant provisions and not try to water them down.

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<sup>1</sup>Hamilton, Jesse and Benjamin Bain, "Wall Street Nears a Big Win in the Latest Revamp of Volcker Rule." April 25, 2019. Available at: <https://www.bloomberg.com/news/articles/2019-04-25/wall-street-nears-a-big-win-in-the-latest-revamp-of-volcker-rule>

Specifically, data presented in a recent Federal Reserve Board study raise serious questions.<sup>2</sup> Using confidential high-frequency regulatory data, the study's authors found that, on average, some banks have amassed weekly trading profits of as much as \$117 million, weekly losses up to \$84 million and weekly exposures as high as \$505 million.<sup>3</sup> These findings not only seem to echo recent news reports of some traders raking in windfall profits and suffering outsized losses but also are instructive of the frequency with which they may be doing so.

Perhaps more alarming is the ratio of some banks' profits and losses to their values at risk ("VaR"). The VaR is a bank's own estimate of how much it stands to lose in a single trading day. Losses should not exceed a bank's VaR more than 1 percent of the time. Yet in the last few quarters alone, some banks have reported loss ratios that exceed VaR by 200 percent, and, in one instance, by as much as 1,200 percent.<sup>4</sup>

Bank filings with the Securities and Exchange Commission raise similar questions. The most recent Form 8-K filings of five of the eight largest global systemically important banks reflect wild swings in sales and trading revenue relative to prior quarters. The variability has been most dramatic in the banks' fixed income, currency and commodity lines of business, with Morgan Stanley, Goldman Sachs and Citigroup each experiencing variations in revenue of between 18 and 30 percent quarter over quarter.<sup>5</sup>

These trends raise red flags. They deserve your attention. Before you gut the most important structural reform to have emerged from the financial crisis—a reform that the Federal Reserve's own economists conclude has had "economically large financial stability benefits"<sup>6</sup>—you should investigate these trends. In order to give taxpayers some indication that you are on the job and effectively policing the markets, I request an extensive report on enforcement of the Volcker Rule with a detailed explanation on how the press reports and regulatory filings referenced above did not violate the rule.

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<sup>2</sup> Falato, Antonio, Diana Iercosan, and Filip Zikes (2019). "Banks as Regulated Traders," Finance and Economics Discussion Series 2019-005. Washington: Board of Governors of the Federal Reserve System. Available at: <https://doi.org/10.17016/FEDS.2019.005>

<sup>3</sup> Ibid, p. 12.

<sup>4</sup> Nasiripour, Shahien, Sonali Basak, and Steven Arons. "Wild Trading Day at Deutsche Bank Raises Questions on Risk," June 20, 2018. Available at: <https://www.bloomberg.com/news/articles/2018-06-20/wild-trading-day-at-deutsche-bank-raises-questions-on-u-s-risk>

and Bair, Sheila and Gaurav Vasisht. "Re: Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds (Docket ID OCC-2018-0010; Board Docket No. R-1608; RIN 7100-AF 06; FDIC RIN 3064-AE67; SEC File Number S7-14-18; CFTC RIN 3038-AE72," October 17, 2018. p. 8, 24.

<sup>5</sup> Morgan Stanley, Form 8-K, January 17, 2019. Available at

<https://www.sec.gov/Archives/edgar/data/895421/000115752319000085/a51926474.htm>

and Goldman Sachs Group, Inc., Form 8-K, January 17, 2019. Available at: <https://www.goldmansachs.com/investor-relations/financials/current/8k/8k-01-16-19.pdf>.

and Citigroup Inc., Form 8-K, January 17, 2019. Available at:

[https://www.sec.gov/Archives/edgar/data/831001/000110465919001687/a19-2779\\_18k.htm](https://www.sec.gov/Archives/edgar/data/831001/000110465919001687/a19-2779_18k.htm).

<sup>6</sup> Falato, Antonio, Diana Iercosan, and Filip Zikes (2019). "Banks as Regulated Traders," Finance and Economics Discussion Series 2019-005. Washington: Board of Governors of the Federal Reserve System, page 1. Available at: <https://doi.org/10.17016/FEDS.2019.005>

Once again, I am also requesting that regulators release the confidential data that I have now repeatedly asked for over several years. In a recent Congressional hearing, Federal Reserve Vice Chair for Supervision Randal Quarles referred to lawmakers' request for public release of Volcker Rule data as a "very reasonable request."<sup>7</sup> This data will help ensure that any future changes to the Volcker Rule are grounded in the type of rigorous analysis befitting a rule of its import.

Sincerely,



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Jeffrey A. Merkley  
United States Senator

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<sup>7</sup> U.S. House Committee on Financial Services, "Oversight of Prudential Regulators: Ensuring the Safety, Soundness and Accountability of Megabanks and Other Depository Institutions," May 16, 2019. Available at: <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=403653#Wbcast03222017>