June 12, 2017

Dear Senators and Representatives,

On Tuesday May 23, 2017, President Trump released his fiscal year 2018 budget request to Congress. The budget calls for draconian cuts that would threaten the economic security and the health and safety of American families. The budget hearings in both the House and Senate provide a necessary opportunity for Members of Congress to ask cabinet secretaries about the Administration’s budget request and justifications for their respective departments. With regards to the proposed budget for the Department of the Treasury, cuts to the Internal Revenue Service (IRS), Community Development Financial Institutions Fund (CDFI Fund), and the Office of Financial Research (OFR) are particularly troubling. These cuts will only limit our ability to police tax avoidance and evasion, will hurt investment in local communities, and will hinder efforts to monitor and respond to financial stability risks, respectively.

Our concerns with these cuts, along with targeted questions reflecting those concerns, are outlined below. This hearing with Secretary Mnuchin also provides a useful chance to gain clarity on the Administration’s stance on timely policy questions like the debt limit and to ask for updates on the various presidentially-mandated reviews of financial regulation currently being conducted by the Treasury Department.

**Executive Orders and Presidential Memoranda**

President Trump, through an executive order and two presidential memoranda, ordered Treasury Secretary Mnuchin to conduct a review of the U.S. financial regulatory regime. While the executive order required a study of how the entire landscape of financial regulations fits the President’s stated “core principles,” the executive memoranda specifically identify two regulations: Orderly Liquidation Authority (OLA) and the Financial Stability Oversight Council’s authority to subject systemically

---

important nonbank firms, like AIG, to enhanced regulation and oversight.\(^2\) It is important that Secretary Mnuchin update Congress on the status of these reviews.

Accordingly, we suggest Members ask Secretary Mnuchin the following questions during his hearing:

- What is the status of the presidentially-mandated reviews on financial regulation? Will you submit to Congress, and make public, the list of meetings that occurred during these reviews, including the names of the financial institutions you consulted with?
- The Executive Order considers a core principle of financial regulation to be that the government “empower Americans to make independent financial decisions and informed choices in the marketplace.” How does your agency plan to empower Americans while proposing to take away many of the tools and consumer protections that they rely on in the financial marketplace?

The Orderly Liquidation Authority is a new tool created by Dodd-Frank that gives regulators the authority to wind down complex financial institutions in an orderly manner. During the financial crisis, regulators had two terrible options for dealing with the failure of a complex financial institution: disastrous bankruptcy or taxpayer funded bailouts.

- Are bailouts unacceptable to the President? Did the bankruptcy of Lehman Brothers aggravate the financial crisis? Should financial regulators be limited to the same tools they had during the last financial crisis when it comes to dealing with the failure of a large, complex financial firm?

The Financial Stability Oversight Council was created to monitor and respond to emerging threats to financial stability, across the financial system. FSOC was given the authority to designate nonbank financial companies as “systemically important,” subjecting them to enhanced regulation and oversight. So far FSOC has exercised this authority in four instances, including for AIG, the insurance company that received a $182 billion bailout during the financial crisis.\(^3\)

- Is it possible for a nonbank financial firm to pose a systemic risk to the U.S. economy? Should systemically important nonbank financial firms, like AIG, be subject to enhanced regulation and oversight?

**Debt limit**

Maintaining the full faith and credit of the United States should be of paramount importance to any presidential administration. The United States can and must be trusted to pay its debts on time. A failure to maintain this confidence and breach this trust by defaulting on our debt could have a catastrophic

\(^2\) Executive Order no. 13,772, Code of Federal Regulations (2017); Orderly Liquidation Authority, Presidential Memorandum for the Secretary of the Treasury, April 21, 2017; Financial Stability Oversight Council, Presidential Memorandum for the Secretary of the Treasury, April 21, 2017.

impact on the global economy and make U.S. borrowing in the future costlier. Based on slower than usual tax receipts, the U.S. may run up against the debt limit as soon as this summer.\textsuperscript{4} It is concerning that as this deadline nears, different members of the Administration are sending different signals about raising the debt limit. Secretary Mnuchin urged Congress to pass a “clean” debt limit with no policy or spending strings attached.\textsuperscript{5} But Director of the Office of Management and Budget Mick Mulvaney has called for attaching spending conditions to the debt limit and National Economic Council Director Gary Cohn is open to “concessions” on the debt limit.\textsuperscript{6}

Given this clear confusion on a timely policy decision of great importance, we suggest Members ask Secretary Mnuchin the following questions:

- With regards to raising the debt limit with or without spending or policy conditions attached, what is the official and unequivocal position of the Trump administration? What do you think would be the economic consequences of failing to raise the debt limit?

\textbf{Internal Revenue Service}

Congress reduced the Internal Revenue Service budget by $1.2 billion from 2010-2015. During your confirmation, you told the Senate Finance Committee that you believed the IRS is “under-resourced to perform its duties” and that further cuts “will indeed hamper our ability to collect revenue.”\textsuperscript{7} Yet the Trump administration’s budget calls for a further reduction of $239 million.\textsuperscript{8} At the same time, the Administration is proposing tax policies that would expand avenues for tax avoidance. For example, the Administration is proposing a territorial tax system for corporations, presumably meaning that offshore profits will not be taxed at all—which would provide even stronger incentives for companies to shift profits offshore. They are also proposing what has been called the “mother of all tax loopholes” – special, low rate for passthrough businesses – while asserting that this new loophole won’t lead to more gaming and avoidance.

Based on these major budget cuts, we suggest Members ask Secretary Mnuchin the following question during his hearing:

- How will the IRS effectively police tax avoidance and tax evasion, given that it already faces an annual tax gap of roughly half a trillion dollars⁹?

Community Development Financial Institutions Fund and Capital Magnet Fund

President Trump’s proposed budget would eliminate the grant programs of the Community Development Financial Institutions Fund, cutting $210 million in appropriations that would benefit Community Development Financial Institutions, or CDFIs. The Administration claims that federal funding is no longer necessary, but defunding these programs that support lending in distressed communities is a stark reversal to a sector that has received federal support for over two decades. The budget would also eliminate the Capital Magnet Fund, or CMF, an affordable housing and economic development program overseen by the Treasury Department and financed through Fannie Mae and Freddie Mac revenues, on the grounds that it is duplicative with other housing programs.

The programs’ track records speak for themselves. Last year’s CMF awardees are expected to generate 17,000 affordable housing units, including 2,000 units for homeowners of modest means.¹⁰ CDFI Fund awardees made $3.6 billion in loans or investments in FY 2016, dollars that supported 11,000 businesses and 33,000 affordable housing units.¹¹ In both cases, federal funds are a catalyst for private financing, not a substitute for it. And for the Capital Magnet Fund, private capital is an explicit requirement: recipients must provide $10 in private funding for every dollar of federal funds.¹² Given the Trump administration’s proclaimed support for community banking, access to credit, and communities left behind, it would be incredibly short-sighted to defund tools that support financing to some of the most struggling urban and rural communities in the entire country. These cuts suggest that the Trump administration lacks an explicit economic development strategy. Massive budget cuts for CDFI and CMF—combined with other cuts to economic development, housing, and small business programs as well as major deregulatory proposals—will only leave these communities farther behind.¹³

Based on these major budget cuts, we suggest Members ask Secretary Mnuchin the following questions during his hearing:

---


¹¹ Ibid.

¹² Ibid.

• Other than documenting the growth in the number of certified CDFIs, how did the Trump administration come to the conclusion that the CDFI industry has become mature and no longer requires federal support?
• What substitutes to CDFIs does the Trump administration envision plugging the financing gaps of low-income communities? Would alternative financing be available at all for small businesses and other borrowers in these communities? Would other forms of financing be more expensive or predatory for borrowers?

Office of Financial Research

The budget submitted to Congress by President Trump calls for a drastic 25% funding cut to the Treasury Department’s Office of Financial Research, which translates to a reduction of 84 staff members. While most of President Trump’s severe budget cuts included in his request will not become law, OFR is a different story. The President and Treasury Secretary have the authority to unilaterally cut OFR’s budget and staffing because it is funded through assessments on systemically important banks and nonbank financial companies. This decision by the Trump administration would make the U.S. financial system more vulnerable to systemic risks and would not save taxpayers a single dime of direct spending.

The Office of Financial Research was created by the Dodd-Frank Wall Street Reform and Consumer Protection Act to provide data-driven research and analytical support to the Financial Stability Oversight Council (FSOC)—the systemic risk regulator also created by Dodd-Frank. One of the main lessons learned from the 2007-2008 financial crisis was that no one regulatory body was responsible for monitoring and responding to financial stability risks that emerge across the financial system. Each regulatory agency was focused only on their discrete piece of the financial sector. FSOC now brings regulators together to regularly communicate about risks across the system and has the authority to respond to financial stability threats as they emerge. The Office of Financial Research has played a critical role in providing FSOC with the research capacity and data-collection necessary to fulfill this important mandate.

The OFR has been a key source for data and analysis on potential threats to financial stability. From publishing reports on capital and liquidity requirements, to providing issue briefs on the importance of central counterparty clearing, the OFR has brought together talented researchers and academics to fulfill its mission. The OFR has also developed new financial stability monitoring tools for financial markets and institutions that map out the quarterly risk levels of various financial stability metrics. This work on financial stability and financial data standardization has not only been useful for FSOC, but also for academics, policymakers, and the public.

---

15 Dodd-Frank Wall Street Reform and Consumer Protection Act, Public law 111-203, 111th Cong., 2d sess. (July 21, 2010).
Based on this highly concerning budget for the Office of Financial Research, we suggest Members ask Secretary Mnuchin the following questions during his hearing:

- Do you support the Office of Financial Research’s efforts to monitor financial stability risks and to provide research and analytical support to the Financial Stability Oversight Council?
- Does cutting the budget of the Office of Financial Research by 25%—a move that does not save taxpayers a dime—make the U.S. financial system safer from emerging financial stability threats?
- How did you arrive at the decision to drastically cut the budget of the Office of Financial Research? Did any Member of the House of Representatives or the Senate advise you to cut this funding?

Conclusion

The budget request for the Department of the Treasury submitted to Congress by the Trump administration is deeply concerning. The hearing with Secretary Mnuchin is a good opportunity to get answers regarding some of the proposed drastic cuts and to press the Secretary on the questionable justifications for the request.

If you have any questions or would like to discuss these issues further, please contact Ryan Collins at (202) 741-6246.

Sincerely,

Joe Valenti
Director, Consumer Finance
Center for American Progress

Gregg Gelzinis
Special Assistant, Economic Policy
Center for American Progress