# Bloomberg *vs.* the Fed

*Was the news organization excessive in its demands for central bank transparency?*

BY JOHN BERRY

In early 2008, Bloomberg News editors spied a journalistic target of opportunity: the Federal Reserve's nearly century-old policy of not disclosing the names of financial institutions borrowing money from it, the amount of each loan, or what collateral had been posted to secure it. "Why, that's public money and the public has a right to promptly know all those details, so let's seek the information," the editors decided. If the Fed provided it, Bloomberg would have a great story that would turn financial markets, already deeply in crisis, on their head. Or if the Fed refused, as it surely would, Bloomberg would demand the data on the grounds they were public documents covered by the Freedom of Information Act. Along the way Bloomberg reporters could write many news stories about the secretive Fed and how it was pandering to banks at the cost of the public's right to know.

As a news organization, Bloomberg had every legal right to demand the information. As a central bank fighting to counter a crisis that threatened to plunge the U.S. economy into a second Great Depression, the Fed had every reason to refuse the request. After all, the crisis wasn't just the result of large losses by financial institutions on structured financial products secured by subprime mortgages that were defaulting in waves. It was the uncertainty about whether key institutions were still solvent that had caused short-term funding markets, which many large banks used to finance big chunks of their assets, to freeze up. If a big bank was known to be borrowing large amounts from the Fed, its funding might disappear overnight. As the Fed said that autumn, "loss in confidence in and between financial institutions can occur with lightning speed and devastating effects." That possibility, however, made no difference to Bloomberg editors embarked on their right-to-know crusade.

In the early stages of the crisis in the fall of 2007 as short-term funding was drying up, Fed officials encouraged banks to

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THE MAGAZINE OF INTERNATIONAL ECONOMIC POLICY
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borrow from the discount windows at each regional Fed bank. Most institutions were reluctant to do so because there had long been a stigma attached to such borrowings. Even healthy banks were reluctant to go to the window because if it became known, then potential counterparties likely would cut off funding. That was simply a fact of life, and it is currently a serious problem for many European banks scrambling for short-term money that the European Central Bank has had to provide.

There was a more limited episode in the early 1990s when a number of major banks, among them Citibank, were in trouble because of large losses on real estate loans and were short of funding. Peter Fisher, now a senior managing director at BlackRock, who earlier managed the New York Fed's Open Market Desk, recalls that in those days the Fed published total discount window borrowing from each of the twelve district Federal Reserve banks.

"It was reasonably easy to discern who the borrower was if it was a big bank outside New York," Fisher said. "As soon as the borrowing was reported, big corporate depositors would call up and ask if a bank was the borrower, and if they were, they would pull their deposit. There was a true stigma attached."

Over time, short-term funding using repurchase agreements and other sources, such as money market funds, became both more important and more sensitive to banks' reputations than deposits, large portions of which were insured by the federal government. So in December 2007, the Fed sought to encourage borrowing by creating the Term Auction Facility at the New York Fed rather than the discount window. Using it, banks were able to approach the Fed collectively, rather than one by one, and avoid the stigma, and they could borrow for twenty-eight days rather than overnight and at an interest rate determined by the bidders rather than the Fed. This worked well, and the Fed reported how much was lent and at what interest rate. Nothing was secret except the names of the borrowers and how much each bidder got. Later, other facilities were set up to address specific problems in different segments of the crisis-ridden financial markets. Again, all the details were reported except the names and amounts each institution borrowed.

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After the New York Fed extended a $29 billion nonrecourse loan to JPMorgan Chase to help finance its purchase of Bear Stearns, a failing brokerage house, Bloomberg also asked for details about the collateral, how much it had been discounted, and so forth.

On November 7, 2008, Bloomberg filed a Freedom of Information Act suit in U.S. District Court in New York. In it, Bloomberg claimed the documents it sought "are central to understanding and assessing the government's response to the most cataclysmic financial crisis in America since the Great Depression. The effect of that crisis on the American public has been and will continue to be devastating. Hundreds of corporations are announcing layoffs in response to the crisis, and the economy was the top issue of many Americans in the recent elections."

"To discharge its obligation as the eyes and ears of the public, Bloomberg sought access to this information under FOIA," the filing said.

After the filing, Bloomberg News carried stories with headlines such as, "Fed Defies Transparency Aim in Refusal to Identify Bank Loans." The story said, "Americans have no idea where their money is going or what securities the banks are pledging in return."

Another story noted that the Bloomberg suit asserted, "The Federal Reserve should identify U.S. banks funded by its emergency lending because taxpayers are 'involuntary investors' who need to know the risks."

Of course, that is the real issue involved concerning detailed disclosure of the loans. Bloomberg essentially argued that the risk that the Fed and thus taxpayers would lose money on some of the loans was more important than the risk that disclosure could disrupt the Fed's herculean effort to prevent a collapse of the financial system. Indeed, by raising questions about the loans and whether they were somehow unfairly benefitting banks when the country was suffering intensely from the crisis, the Bloomberg stories added to the Bush Administration's difficulties in persuading Congress to approve its Troubled Asset Relief Program, or TARP.

After a great deal of legal maneuvering over the Freedom of Information Act by both sides, Bloomberg won its suit in August 2009. Judge Loretta A. Preska ruled against the Fed on several grounds, including that it had not shown that disclosure of the loan details would do

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"imminent" harm to the borrowers. The FOIA requirements for an exemption were too tough for the Fed to meet. The good news was that the litigation itself and implementation of the order delayed disclosure for many months. The sort of harm that might have been done had the data all come out in late 2008 at the height of the crisis following the failure of Lehman Brothers Holdings was avoided.

Judge Preska's decision was hardly the end of the matter. When the Fed got done turning over the data, it included 29,000 pages documents and central bank records of more than 21,000 transactions. As a Bloomberg story summarized late last year, "The Fed didn't tell anyone which banks were in trouble so deep they required a combined $1.2 trillion on December 5, 2008, their single neediest day. Bankers didn't mention that they took tens of billions of dollars in emergency loans at the same time they were assuring investors their firms were healthy. And no one calculated until now that banks reaped an estimated $13 billion of income by taking advantage of the Fed's below-market rates."

And then there's this remarkable assertion: "While Fed officials say that almost all of the loans were repaid and there have been no losses, details suggest taxpayers paid a price beyond dollars as the secret funding helped preserve a broken status quo and enabled the biggest banks to grow even bigger."

It's certainly true that the some of the biggest banks have gotten bigger as some pretty big ones, such as Wachovia, failed and were absorbed by other bigger institutions. Again, however, Bloomberg never compares that supposed "price beyond dollars" to the price taxpayers—the whole country—would have paid had the financial system collapsed.

Shortly after this story was published, one of the authors, Bloomberg reporter Robert Ivry, was interviewed by Kathleen Hays on a Bloomberg radio program about the story. Said Ivry, "We don't engage the argument over whether or not what the Fed did during the crisis was correct or not. I am not even sure I have a definitive opinion on that.

"But what we are looking at is how that information was kept from certain people, and we say in our story last week that the Treasury policymakers who were putting together TARP didn't know which of the banks was getting the money, and how much, and the lawmakers who were putting together Dodd-Frank [financial reform legislation] in 2010 had no idea that Morgan Stanley's borrowing from the Fed peaked at $107 billion or that Bank of America and Citigroup both had more than $90 billion in loans from the Fed at any particular time.

"What we are keying on is what were the costs of the lack of transparency by the Fed."

Unfortunately, Ivry never identified what the costs may have been. Treasury officials and interested members of Congress could easily have looked at the Fed's weekly reports on all the lending facilities and found out how much had been lent to financial institutions. Ivry never explains why having specific information about the amount of borrowing by particular banks would have made any difference.

For instance, his story said that the six biggest banks—JPMorgan Chase, Bank of America, Citigroup, Wells Fargo, Goldman Sachs, and Morgan Stanley—"accounted for 63 percent of average daily debt to the Fed by all publicly traded U.S. banks, money managers, and investment-services firms, the data show. By comparison, they had about half of the industry's assets before the bailout…" So? Did legislators need to know that?

The claim in the story's headline, "Secret Fed Loans Gave Banks $13 Billion Undisclosed to Congress," is even more problematical. In fact, there was no such number to disclose. It was a Bloomberg calculation based on assuming that a group of 190 banks were able to earn their reported average net interest margin on the money borrowed over time from the Fed. Even the story admits "the method isn't perfect.

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There was another guest on Kathleen Hays' program that day, Ricardo Reis, professor of economics at Columbia University, and she asked what he thought about Ivry's story.

Reis first praised the Fed for becoming much more open and transparent over the past twenty years, but added, "Now when it comes to the discount window, though, it important to have secrecy. And it is important when it comes to emergency lending to keep some secrecy, because

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at the time of a crisis it is important that it's not revealed who is the bank that is in more trouble…. If you do so, you're basically isolating who the prey is for the predators. So you really don't want to do that."

As for the banks making that $13 billion, Reis said, "What the Bloomberg piece did was look on average at what interest rates these banks were lending and given on average how much they were borrowing at, what was their margin… However, the Fed did not charge average interest rates. The Fed charged a penalty rate."

"As for them making money, you have to realize that to some extent the Fed saved the American financial system… American households got extremely large gains in terms of not having a spike in interest rates on their credit cards, on their homes, on their autos… [The majority of the gains] went to U.S. households either directly or then by whatever [payments] the Fed made to the Treasury. The share of how much money the banks made was small, quite small relative to that and I am not even sure it's positive."

In the end, the disclosure issue was settled not by the court but by Dodd-Frank—and in a sense, in the Fed's favor. A provision requires that details of all discount window lending be published eight quarters after the quarter in which they are made. If the Fed were to create a new lending facility in the future, details of loans would have to be released a year after the Fed formally closed the facility. ◆