FedFin Daily Briefing

Wednesday, July 29, 2020

Warren, Schatz Challenge Fed Capital Policy

Late yesterday, Sens. Warren (D-MA) and Schatz (D-HI) sent a letter to the Fed objecting to prior authorization for large-bank dividend payments. The letter largely reiterates many objections raised at the time, perhaps now more as a warning shot to Chairman Crapo (D-ID) than as an appeal for changed Fed policy. Press reports on Tuesday signalled that Sen. Crapo is seeking to add language to the COVID package sought by Vice Chairman Quarles to provide leverage ratio flexibility for Tier 1 capital akin to that granted under recent SLR changes (see FSM Report **LEVERAGE23**). The battle over the McConnell COVID bill will be fought on party lines regardless of any bank-capital language, but debate on this provision suggests it will gain public attention and thus be used at the least to ensure Democratic opposition to capital relief when the COVID bill passes the Senate and heads to conference with the House.

However, while political, the Warren-Schatz letter is also substantive. It takes specific issue with the Fed's sensitivity analysis, arguing that a W-shaped recession is now the most likely forecast and that the Fed's own data suggest large banks would be vulnerable under it. Had the Fed accounted for bank capital previously paid in dividends in its forward-looking projects, the letter estimates a fifty basis point reduction in aggregate capital suggesting several banks would then be under-capitalized. The letter also challenges use of the February stress-test results despite significant macroeconomic change due to the pandemic. The letter requests that the FRB make public by August 11 an array of data on large-bank capital resilience, the Fed's forward-looking plans for stress testing and dividending, why banks that breached capital minimums in the sensitivity analysis need not now raise capital, and why post-stress leverage ratios were not included in these Fed analyses.

Brooks Stands by Payment-Charter Plan

At his Brookings Institution event today, Acting Comptroller Brooks stopped short of unveiling a new payments charter but continued to champion the concept, laying out a strong legal argument supporting OCC action. When questioned about a letter sent to the OCC today in which seven trade organizations critiqued the OCC's initiative, Mr. Brooks said that any decisions regarding charters granted to payments companies would be as transparent as any other chartering decisions, rejecting assertions that the agency will issue a "light-touch" charter. Mr. Brooks also refuted the letter's contention that chartered payments companies should be required to have a parent BHC, stating that BHCs may only control entities that include an insured depository among their holdings.

Powell Open to Tier 1 LR Fix, Takes Expansive 13(3) View

Following today's cautious and pessimistic FOMC statement, Chairman Powell made it very, very clear that the course of the economy and thus of Fed policy depends on the pandemic. Mr. Powell was equivocal about GOP plans to seek a provision in the Senate COVID plan providing relief from the Tier 1 leverage ratio, saying that this was up to the Senate, should be temporary if enacted, and that other nations have eased their leverage ratios even as he also said the Fed had not established a position on the legislation. Asked about the scope of the Fed's 13(3) powers, the chairman spoke generally of the law's purpose without expressly stating whether the law permits direct equity purchases. He did say that corporate-bond purchases – now of course well under way – are authorized by 13(3)'s credit purpose. Interestingly, Chair Yellen in 2016 stated that the Fed would need a change of law to purchase corporate debt. Mr. Powell was also pressed on whether Congress should redirect funds backing FRB facilities given their low utilization; he said that this is up to Congress, acknowledging lower-than-expected facility use, but stressing that facilities must be "fully" funded and remain in place. Mr. Powell did not say whether he thought the Fed needed a racial-equity mandate as called for yesterday by Joe Biden, reiterating what he described as the Fed's longstanding focus on black unemployment and the more important role of fiscal policy in advancing racial equality.

Separately, the FRB extended the temporary U.S. dollar liquidity swap lines and the temporary repurchase agreement facility for foreign and international monetary authorities (FIMA repo facility) through March 31. When asked about this, Mr. Powell made it clear that this deadline is a movable target because these facilities will remain in place for as long as necessary.

Recent Files Available for Downloading

The following reports and analyses have been sent to retainer clients recently. Copies are also available to retainer clients on the Archives section of Federal Financial Analytics' website: www.fedfin.com or clients may obtain the reports/analyses by e-mailing requests@fedfin.com giving the requested item name, firm, and e-mail address. To learn more about GSE Activity Reports, click: http://www.fedfin.com/index.php?option=com_content&view=article&id=18&Itemid=18

- **CONSUMER34:** As expected, Democrats led by Ranking Member Brown (D-OH) sharply criticized CFPB Director Kraninger at the contentious Senate Banking hearing, citing a lack of enforcement actions and pandemic measures on credit reporting and mortgage forbearance.

- **GSE-072720:** In recent in-depth analyses, we assessed the OCC's new valid-when made doctrine and its latest proposal to define who is deemed a "true lender."

- **PREEMPT34:** As promised by Acting Comptroller Brooks, the OCC has quickly followed up its controversial valid-when-made rule with a proposal defining "true lender" to facilitate the partnerships between banking organizations and other financial companies sometimes called "rent-a-bank" charters.

- **GREEN3:** Building on its 2017 climate-change disclosure work, the FSB issued what it describes as a "stocktake" – i.e., a survey combined with next steps – in this increasingly critical area.

Federal Financial Analytics, Inc.
2101 LStreet, N.W. – Suite 300, Washington, D.C. 20037
Phone (202) 589-0880
E-mail: info@fedfin.com www.fedfin.com

- **GSE-071720:** A new Federal Reserve Bank of New York staff paper sheds timely light on the impact of foreclosure-mitigation efforts on long-term housing markets and household wealth.

- **SBA39:** In this report, we assess the financial policy implications of the wide-ranging House Small Business Committee hearing with Treasury Secretary Mnuchin and SBA Administrator Carranza.

- **MORTGAGE117:** In this report, we assess the HFSC Oversight and Investigations Subcommittee hearing on mortgage servicing.

- **GSE-071520:** FSOC has officially begun the activity-and-practice designation of the secondary-mortgage market foreshadowed in FSOC's annual report.

- **TBTF23:** Moving cautiously to assess the extent to which large banks are no longer too big to fail (TBTF), the FSB has gone beyond a request for comment to a somewhat more specific solution that may lead to policy actions not yet spelled out for public comment in this report.

- **COVEREDFUNDS2:** The banking agencies, SEC, and CFTC have finalized a long-awaited, complex, and comprehensive proposal rolling back many of the restrictions on covered funds imposed in the 2013 rules implementing the Volcker Rule provisions of the Dodd-Frank Act.

- **GSE-070720:** In the final version of "Volcker 2.0," the FRB, FDIC, OCC, SEC, and CFTC finalized a massive, controversial rewrite of the rules governing the funds which U.S. banks and foreign banks doing business here may hold, own, sponsor, or otherwise serve and even market across an array of asset classes.

- **DERIVATIVES36:** Reflecting strong industry pressure and growing concerns about market structure, the banking agencies have joined others with which they share jurisdiction to finalize proposed revisions reducing the capital cost of the 2015 margin rule for non-cleared derivatives.

Federal Financial Analytics, Inc.
2101 LStreet, N.W. – Suite 300, Washington, D.C. 20037
Phone (202) 589-0880
E-mail: info@fedfin.com www.fedfin.com