FedFin Client Report

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Partisan Differences on Full Display as Senate Banking Considers Financial Regulation

Client Report: **RESCUE77**

Executive Summary

At its first hearing following last week's election, Senate Banking today heard testimony from the federal prudential regulators which largely covered ongoing efforts to combat the COVID pandemic's impacts on the financial system. However, acting Comptroller Brooks strongly defended his work to expand digital and cryptocurrency finance through the banking system, making it clear he will press many of his controversial initiatives unless or until he is replaced. Led by Chairman Crapo (R-ID), Republicans applauded the agencies' temporary regulatory relief, pushing for more. Sen. Crapo also reiterated his strong opposition to financial institutions deciding not to lend to certain sectors, a point Mr. Brooks also raised in testimony stating that he will work hard to prevent banks from "discriminating" against fossil-fuel companies.

Led by Ranking Member Brown (D-OH), Democrats argued that Trump Administration regulators have continued through the pandemic to advance the interests of "Wall Street," also urging that the biggest banks be broken up. With Sen. Warren (D-MA), he also urged a full ban on bank capital distributions and Democrats called for incorporating climate risk into bank risk-management frameworks. Sen. Tester (D-MT) had an unusually sharp exchange with Fed Vice Chairman Quarles that led the senator, usually supportive of the central bank, to claim that Mr. Quarles' views on the economy and the need for Fed facilities undermine Fed independence. Under questioning, Mr. Quarles also said that he does not think the GSIB surcharge should be recalibrated now, preferring to consider this after the U.S. acts on Basel IV in 2021.

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Analysis

Opening Statements

Chairman Crapo praised regulators for temporary regulatory relief measures designed to mitigate the impact of the pandemic, arguing for them to continue to use their discretion to alleviate burdens associated with a variety of asset-based regulatory thresholds. He also commended the OCC for its final CRA rule (see Client Report **CRA28**). Sen. Crapo argued that lending decisions must be based only on creditworthiness and not target specific industries, noting both the firearms and oil and gas industries in particular but saying that all legal industries should have credit access.

Ranking Member Brown said regulators appointed by the Trump Administration have put their thumbs on the scale for wealthy corporations while rejecting efforts to support families. He argued that voters have rejected this approach and instead want the parties to work together on issues such as wages and housing. Sen. Brown called for taking on "Big Oil" and other corporate polluters and breaking up the biggest banks.

Testimony

Mr. Quarles highlighted the temporary relief actions the Fed has taken to support the recovery, referring senators to the FRB's recent financial stability report (see Client Report **SYSTEMIC89**). Although the recovery is now underway, households and businesses still face significant burdens and the Fed thus remains committed to using its full range of tools.

Acting Comptroller Brooks stressed that, while banks remain sound, there is the potential for troubled assets ahead in commercial and residential real estate, small business and consumer lending, and travel and hospitality. Banks with concentrations in these areas should take a "sober" view of these risks. He also highlighted OCC efforts to increase representation and inclusion in the banking system, pointing to work on expanding affordable housing, reinvigorating minority banks, and reaching the millions of Americans without a credit score. In his written statement, Mr. Brooks also defended OCC actions such as the controversial Kraken charter (see FSM Report **CRYPTO15**) the need for both fintech and payment charters, and final action on the agency's NPR to expand national bank activities (see FSM Report **CHARTER26**).

FDIC Chair McWilliams said the FDIC stands ready to issue additional guidance as appropriate to support the recovery. The FDIC will soon finalize rulemakings on both brokered deposits (see FSM Report **DEPOSITINSURANCE109**) and ILCs (see

FSM Report **ILC14**). She also said regulators need to foster the development of technology as people increasingly move to digital banking.

NCUA Chairman Hood noted that, like the banking agencies, the NCUA has provided considerable temporary regulatory relief. He said the insurance fund is strong, its equity ratio is within the statutory range, and there is no need to assess a premium at this time. Mr. Hood said temporary relief should be extended for the duration of the pandemic.

Q&A

- Reg Relief: Sen. Crapo asked about additional areas in which regulators could use their discretion to provide relief. Mr. Brooks noted interagency work to provide relief on certain asset thresholds, saying these would likely apply to thresholds below $10 billion and that banks above this threshold are not experiencing difficulty. FDIC Chair McWilliams agreed that relief should target smaller banks. NCUA Chairman Hood asked that his agency be able to provide relief from prompt corrective action rules on a temporary basis. Sen. Toomey (R-PA) pushed for threshold relief on interchange fees, and Sen. Rounds (R-SD) argued for excluding lower-risk assets from the GSIB surcharge. Vice Chair Quarles pushed back on the need for surcharge relief, noting that GSIBs have not said it is a concern. Mr. Quarles said its calibration would likely be reevaluated after final implementation of the Basel III framework, which he intends to accomplish over the next year. However, any recalibration would seek to ensure the level of capital in the banking system remains essentially the same.
- CRA: Sen Menendez (D-NJ) castigated the OCC's CRA final rule. Acting Comptroller Brooks defended it and said that the Fed's ANPR is very similar to the OCC's final rule, showing interagency agreement.
- Stimulus: Sen. Reed (D-RI) asked if a second CARES Act package is needed, arguing that without it there could be a wave of evictions and foreclosures as early as January that would then impact the banking system. Mr. Quarles said that is up to Congress, giving his view that additional stimulus could accelerate the recovery but may not ultimately be necessary. Sen. Warren noted that assumptions of stimulus were built into the most recent stress tests and argued that banks are thus likely in a less sound position than these indicate.
- Climate Risk: Sen. Schatz (D-HI) asked Vice Chair Quarles if he agrees that climate risk should be integrated into banks' risk-management framework; he does. Sen. Schatz then asked if the Fed plans to formally join the Network for Greening the Financial System (NGFS). Mr. Quarles said this is up to the NGFS, but noted that the Fed has requested membership and may join in the Spring around the time of the NGFS annual meeting.

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- Fed Facilities: Arguing that these have been a success, Sen. Toomey said the emergency facilities should be closed. Sen. Schatz thanked the Fed for lowering the minimum loan threshold for the Main Street Program.
- State/Local Support: Sen. Reed argued for additional support for state and local governments. Vice Chair Quarles stressed that the Fed can work only through its emergency facilities, not with direct fiscal support. He was later pushed on this point by Sen. Tester, who in a heated exchange argued that although the Fed cannot implement fiscal policy, Mr. Quarles could voice support for it when asked by Congress but is choosing not to do so for political reasons.
- PPP: Sen. Menendez asked if either Chair McWilliams or Acting Comptroller Brooks knew about Treasury guidance directing banks to prioritize their existing customers. Both said they didn't, contending that BSA/AML issues led to existing customers receiving loans more speedily.
- True Lender Rule: Sen. Cortez Masto (D-NV) argued that lenders will use the rule (see FSM Report **PREEMPT35**) to circumvent state usury laws and engage in predatory lending. Mr. Brooks said that Congress and the courts decided years ago that national banks should be able to export their home state's interest rates and that the rule is restoring this bipartisan understanding.

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