FedFin Daily Briefing

Wednesday, June 30, 2021

FSB MMF Consultation: Options, Contingent Questions Make Structural Change Uncertain

As promised late last year (see *Client Report* **NBFI**), the FSB today issued a consultation on specific remedies enhancing MMF resilience. This is a top-priority issue also in the U.S., although the last FSOC meeting continued to defer near-term action to an SEC that, under Gary Gensler, seems very likely to undertake considerable change once the global construct is finalized. It is, though, unclear the extent to which FSB's final October recommendations will lay out a few specific reforms or if a slate of options will be detailed from which IOSCO and national jurisdictions may select those best suited to their sector and circumstance. The FSB's consultation also says that MMF reform should be accompanied by mandatory changes to fund risk management and underlying reform of short-term funding markets. The latter is a particularly thorny U.S. issue given the global impact of the Treasury market and the extent to which unprecedented basis and other risks led to the "dash for cash" despite the usual flight-to-quality factors expected to prevail in crises such as March 2020.

We will shortly provide clients with an in-depth analysis of this consultation. It lays out the costs and benefits of reform options including swing pricing, a minimum balance-at risk and capital buffer (the solution preferred by FRB Gov. Brainard), an end or rewrite of redemption gates and/or fees, and floating NAVs. Comment is due by August 16, with the prospects for meaningful final action depending on the extent to which FSB's final recommendations are conditional on pending actions and specific enough to envision national and IOSCO accountability.

FHFA Expands Borrower Relief

Acting quickly under its new director to increase borrower relief, FHFA today revised its loan-mod terms for COVID-impacted borrowers, significantly expanding borrower eligibility for interest-rate reductions. Now, borrowers with a permanent COVID-related hardship are eligible regardless of their LTV; the policy previously only afforded this relief to borrowers with mark-to-market LTVs greater than or equal to 80 percent. Recent sharp rises in house prices meant that market prices often brought loans below the LTV-eligibility threshold, forcing possible distressed sales if a borrower cannot resume full payment after forbearance ends. As with CFPB and FHFA action yesterday, this action also facilitates near-term loan rewrites that minimize the number of borrowers with whom servicers will need to deal next fall.

IOSCO Tries to Dry Up Greenwashing

Responding to greenwashing allegations, IOSCO today solicited comment on recommendations for regulatory and supervisory expectations surrounding ESG investments. We expect the SEC to follow suit under the President's climate-risk order; these disclosures are controversial but still pose fewer implementation challenges than those the SEC is also developing for securities registrants. Moving beyond its recent announcement on conforming climate-risk disclosures to new accounting standards, IOSCO now proposes to tell supervisors to ensure that asset managers take sustainability-related risks into account in investment decision-making and risk management. They are also to address greenwashing risk through improved transparency, in part via a new, common lexicon for sustainable finance terms that would ensure global consistency. Comment is due August 15.

HFSC Dems Highlight Crypto Risks

In today's HFSC Subcommittee on Oversight and Investigations hearing, Democrats worried about crypto's volatility and its potential for fraud and systemic risk, with Full Committee Chairwoman Waters (D-CA) highlighting what she believes may be the systemic risk presented by hedge fund investment in crypto. While Rep. Sherman (D-CA) called for a ban on cryptocurrencies to keep up with China, Rep. Garcia (D-TX) noted crypto's financial-inclusion and reserve-currency benefits. Led by Ranking Member Emmer (R-MN), Republicans pushed back against Democratic calls for greater regulation, instead urging greater clarity, certainty, and streamlining in the application and enforcement of existing regulations. Rep. Loudermilk (R-GA) also noted that blockchain could be used to enhance cybersecurity and Rep. Kustoff (R-TN) worried that the U.S. may be moving too slowly on CBDC while China accelerates its digital yuan.

FDIC Adopts Expanded Inclusion Definition, Objectives

FDIC Chair McWilliams today espoused a new definition of financial inclusion: "whether the financial system is working" for an individual, not just whether one has a checking or credit account. She also detailed several initiatives the FDIC has underway to achieve inclusion under this definition. These include tech sprints, collaboration with MDIs and CDFIs, and regulatory reform such as the new brokered deposits rule (see FSM Report **DEPOSITINSURANCE111**). Interagency work such as 2019 guidance on alternative data (see FSM Report **FCRA29**) and a 2021 RFI on AI/ML (see FSM Report **AI**) is also noted. No new initiatives were announced.

Regulators, FinCEN Launch Prioritized AML/CFT Revamp

Responding both to industry requests and a new mandate (see FSM Report **AML133**), federal and state bank regulators, FinCEN, and the NCUA today issued their AML/CFT priority list. No rules have changed, but FinCEN – as also required by law – will determine if new rules are needed and issue them within 180 days. Banks are thus advised to begin to prepare for new rules based on these new priorities, with examiners told not to judge banks by these new priorities until any new rules are finalized. New examination and other guidance will then also be issued.

As laid out by FinCEN, priorities reflect the President's new focus on corruption, virtual currency (with a focus on convertible VC), international and domestic terrorism (with this statement emphasizing FATF's new focus on anti-racial or ethnic extremism), fraud, transnational criminal organizations, human trafficking and smuggling, and proliferation (another FATF priority). Little beyond descriptions of all of these priorities is included in FinCEN's statement, although questions and comments are welcomed.

Dems Stress Climate-Related Financial Stability Risks

HFSC's Subcommittee on Consumer Protection today held a short hearing in which Democrats, led by Full Committee Chairwoman Waters (D-CA) and Subcommittee Chairman Perlmutter (D-CO) supported stress testing and climate disclosures to address the "urgent" financial stability risk posed by climate change. Witnesses generally urged greater action by both federal regulators and Congress to address climate risk, highlighting systemic risk concerns. The author of the stress-testing legislation before the subcommittees, Rep. Casten (D-IL) asked how best to balance stress testing and scenario analysis; Steven Rothstein, Managing Director at Ceres, suggested stress testing individual banks and using scenario analysis for the entire financial system.

Republicans worried about government-driven disinvestment from fossil fuels, warning against the creation of a climate-risk framework before the risk is fully understood by both regulators and financial institutions.

Rep. Luetkemeyer (R-MO) also doubted the accuracy of climate modeling; Clifford Rossi, Professor at the University of Maryland, agreed. Rep. Lucas (R-OK) asked how Mr. Rossi's idea of a "climate credit default swap" could be used to mitigate risk; Mr. Rossi suggested developing a climate-related derivative removing risk from the balance sheet. Although the committee memo noted a draft bill that would impose climate-related capital charges, it was not discussed. It remains to be seen if Chairwoman Waters believes a full Committee hearing is necessary before proceeding to mark-up on these climate-risk bills, many of which will face not just the stiff GOP opposition voiced today, but withering fire in the Senate.

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 info@fedfin.com giving the requested item name, firm, and e-mail address. To learn more about *GSE Activity Reports*, click here.

- **GSE-063021**: With numerous modifications designed to make its proposal less onerous, the CFPB on Monday issued a final rule providing temporary foreclosure protection without the *de facto* moratorium that, had the Bureau heeded some on the Hill, would have prolonged nonpayment, possibly precipitating a flood of borrower requests which servicers could not reasonably be expected to handle with justice for all.

- **FCRA30**: Today's HFSC hearing on credit reporting laid the foundation for legislative action on measures that will prove highly controversial.

- **GSE-062821**: After last week's colossal Supreme Court decision, we provided our first assessment of its impact on near-term charter, mission, and regulatory decisions. Now, we turn in detail to what might come to pass for the conservatorship.

- **CBDC6**: As previously noted, the BIS has released its most full-throated endorsement yet for CBDC. This not only puts further pressure on central banks – the Fed very much included – to accelerate work, but also on the shape of emerging CBDCs.

- **GSE-062321**: There is much rejoicing in mortgage-industry land that the Supreme Court decision today means rapid repeal of Mark Calabria's regulatory legacy and still more rejoicing among affordable-housing advocates about GSEs yoked to a new public-welfare and racial-equity mission without any hope of an end to the conservatorship.

- **CHINA16**: The Senate has passed by a wide margin legislation taking an array of actions to counter the threat now seen to be posed by the People's Republic of China.

- **GSE-061721**: We have reviewed FHFA's massive report to Congress on its 2020 activities, finding only lots of handy facts and no significant policy insights.

- **GSE-061621**: As detailed in our new in-depth report, the Basel Committee is proposing a new regulatory framework for bank exposures to cryptoassets that will influence not only what banks do in this critical arena, but also what the GSEs can do and thus what happens to the digital mortgage.

- **CRYPTO19**: Advancing some of the most controversial ideas in a 2019 discussion paper, the Basel Committee has now formally proposed capital, liquidity, risk-management, and supervisory standards it believes nations should apply to bank cryptoasset exposures.

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

- **CBDC5**: Kicking off Congressional action on CBDC, the hearing today in Senate Banking's Economic Policy Subcommittee made it clear that, as we forecast, progressive Democrats such as Chairwoman Warren (D-MA) are strong supporters of a U.S. CBDC that not only facilitates payments, but also supplants retail banks and other private-sector consumer-finance entities.

- **GSE-060821**: This Friday, FSOC will meet in closed session to craft its agenda for 2021 and beyond. Housing and the GSEs will figure prominently in this work plan, but not as you might think.

- **PAYMENT23**: Continuing work on a priority set by the Group of Twenty heads of state, the FSB in consultation with other global bodies is seeking views on how best to measure progress towards the G20's goal of a faster, safer, cheaper, transparent, and inclusive cross-border payment system.

  CBDC4: Members of Congress have launched an initiative to secure continued dominance of the dollar as the globe's reserve currency, focusing on the extent to which China could over time threaten this via its own CBDC along with strategic financial activities such as its Belt and Roads initiative.

- **GSIB19**: Although the GSIB CEOs got another earful at HFSC's marathon hearing yesterday, it – like the Senate Banking session that preceded it (see Client Report GSIB18) – generated more anger than clear action plans.

- **CRYPTO18**: Following an array of actions by the OCC, the FDIC has begun its consideration of the rules governing insured depository institutions (IDIs) engaged in digital-asset activities.

- **GSIB18**: As anticipated, Senate Banking progressives today excoriated big-bank CEOs for what Chairman Brown (D-OH) describes as their preference for profit over public welfare.

- **ACCESS:** The Federal Reserve's latest wellbeing survey provides important, new insights into how Americans view their financial-services firms at a time of heightened focus on access and equity.

- **REFORM206**: In the one-two punch we anticipated, Senate Banking Chairman Brown (D-OH) convened today's hearing with FRB Vice Chairman Quarles not only to lambast supervision and regulation under Mr. Quarles' watch, but also to reiterate the malign role he believes big banks play in the U.S. economy ahead of tomorrow's hearing with GSIB CEOs.

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