FedFin Daily Briefing

Thursday, August 12, 2021

FDIC Seeks Views on Exam Revamp

The FDIC today requested input on its examinations during the pandemic, seeking views on matters such as whether its approach to off-site exams might be used going forward, looking for example at using technology to replace some on-site activities. Commenters are also asked to detail any negative experiences with off-site examinations. If the FDIC changes its approach to more remote supervision, pressure will grow on the OCC and FRB to do so the same although we doubt they would agree to any significant shift in exam protocols for the largest banks. Comment to the FDIC is due October 12.

FTC Presses for Tough Fed Interchange Rule, Possible Expansion

Reflecting a concerted Administration position, FTC staff today followed the Department of Justice's lead and filed a comment strongly urging final Fed action on a revised, tougher version of its debit-routing proposal (see *FSM Report* **INTERCHANGE8**). The letter was filed by staff following a 3-2 Commission vote. Notably, the FTC's release opens with a statement emphasizing the importance of credit cards to household payments, indirectly supporting merchant groups working to expand the Durbin Amendment's provisions regarding debit cards (see *FSM Report* **INTERCHANGE7**) to credit cards. The comment focuses specifically on the pending proposal, tracking the DOJ by urging the Fed to finalize it with additional anti-evasion provisions (e.g., prohibitions on exclusivity arrangements). Noting the FTC's authority over debit-card networks, the letter also describes its efforts to force issuers to ensure merchant routing choice and what it views as incomplete compliance that led to anti-competitive effects for all but the largest merchants. Other anti-competitive issues related to card issuers are also cited, perhaps suggesting renewed FTC interest in enforcement actions in this sector. However, FTC staff do not echo the Justice Department's broader competition concerns or cite the President's recent order (see *Client Report* **MERGER6**). The agency thus defers to Justice on the broader Sherman Act and competitiveness questions noted yesterday; FedFin will shortly provide clients with an in-depth analysis of what these mean for future industry activities.

Global Regulators Absolve ETFs

In conjunction with global efforts to reduce NBFI risk, IOSCO today released a report generally absolving ETFs of the need for any of the structural reforms now contemplated for MMFs and bond funds (see *Client Report* **NBFI**). With this "clear-sailing" conclusion, asset managers already beginning to convert bond funds and other instruments into ETFs may well conclude that regulatory risk related to ETFs is considerably less, accelerating fund conversions already underway at some large banks. IOSCO concludes that ETFs generally fared very well through the worst of the pandemic crisis, although an ETF subset temporarily experienced unusual trading behavior. However, IOSCO is less certain that fixed-income ETF prices should be the basis of broader bond-market pricing, and certain derivatives-based ETFs may need standards ensuring better structures and contingency planning. IOSCO plans next to consult on ETF standards later this year.

HUD/FHFA Anti-Discrimination Agreement Raises GSE, Counterparty Legal, Rep Risk

Reinforcing our forecast (see *Client Report* **CONSUMER36**) of tougher fair-lending enforcement, HUD and FHFA today released a memorandum of understanding (MOU) aligning policies in ways sure to accelerate FHFA's new, far more stringent approach. FHFA remains an independent agency despite a recent Supreme Court decision, but the MOU essentially aligns FHFA's approach with HUD's newly-vigorous one under the President's racial-equity executive order.

Now, FHFA and HUD will coordinate and share information on possible fair-housing and fair-lending actions, as well as on compliance monitoring not only directly over the GSEs, but also over third parties working with them in various capacities. HUD now also has express authority to assess the GSEs in areas such as underwriting and appraisal guidelines, with FHFA committed to sharing its own enforcement plans with HUD to ensure coordination on related actions. The agencies will continue to adhere to various confidentiality and related requirements, but extensive provisions in the MOU discuss privilege and information-sharing protocols that could expose the GSEs and their counterparties to considerably greater risk of actions by HUD under the Fair Housing Act and to both agencies under the Fair Lending Act.

BIS Finds EU Banks Skew GSIB Scores, Recommends Designation Discretion

Going beyond a 2020 Fed Staff study finding limited window dressing at U.S. GSIBs, the BIS today released a staff paper finding extensive year-end data management by EU banks eager to avoid costly GSIB designation or “bucket” upgrade. Although Fed Staff found U.S. GSIBs window dressed only with regard to one of the twelve GSIB indicators (notional amounts of OTC derivatives), EU GSIBs are found to window dress to some extent across all categories. Several GSIB scores are estimated to have dropped by more than 70bps and thirteen banks avoided a higher bucket due to window dressing. Estimated relief due to lower bucket placement totals more than €31 billion of CET1 capital.

As in the Fed paper, the BIS recommends greater use of averaging rather than relying exclusively on year-end values. It goes on also to suggest that supervisors should allocate banks into higher GSIB buckets based on their own judgement, not just numerical indicators. While the Fed specifically reserves this authority in its own rule (see FSM Report **GSIB7**), supervisory judgement is generally limited in the Basel framework (see FSM Report **GSIB13**) only to GSIB designation, not bucket increases. However, a Basel carve-out for “exceptional” and “egregious” cases does exist, with bucket hikes implemented under this provision subject to international peer review.

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-081121**: As we briefly noted yesterday, the CFPB released a report assessing how the largest servicers handled borrowers over recent, chaotic months.
- **LIBOR6**: The House Financial Services Committee has reported H.R. 4616, a bill designed to prevent the chaos feared when the use of the LIBOR benchmark ceases for legacy contracts that lack language authorizing reliance on an alternative, "fallback" rate.
- **GSE-080421**: A new Fed study finds a significant mark-up in the cost of mortgages during the 2020 boom even though government guarantees secured continued mortgage supply for all but the lowest and highest ends of the housing market.

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- **REFORM207**: Today's Senate Banking hearing on bank supervision did not include FRB Vice Chairman Quarles, who came before the panel for withering criticism earlier this year (see Client Report REFORM206).

- **GSE-080221:** Whatever befalls the Senate infrastructure bill, we believe its $21 billion GSE pay-for is but one bit of a bigger de facto transformation of the GSEs.

- **GSE-073021**: As promised, we here follow up our assessment of Ginnie's proposed prudential standards for nonbank mortgage companies with an analysis of model rules aimed at the same goal from the Conference of State Bank Supervisors (CSBS).

- **PREEMPT37**: Senate Banking today held a hearing on new legislation (S. 2508) from Sen. Reed (D-RI) extending the Military Lending Act (MLA) interest-rate cap to certain consumer financial products to all consumers.

- **GSE-072821**: Ginnie's proposed new capital and, to a lesser extent, its liquidity standards could well redefine the mortgage playing field.

- **CBDC7**: Today's HFSC National Security Subcommittee hearing on CBDC featured bipartisan concern over China's threat to U.S. Dollar supremacy and the effectiveness of U.S. sanctions without a U.S. CBDC.

- **ACCESS2**: At a very well-attended HFSC Consumer Protection Subcommittee hearing, Democrats strongly supported government-led solutions to increase financial inclusion.

- **VENDOR9**: The banking agencies have proposed sweeping standards that would hold all of the banking organizations they govern responsible for the safety and soundness, consumer compliance, and perhaps even diversity of a wide range of third-party business arrangements …

- **GSE-071621**: Later today, we'll provide clients with a summary of key provisions in the housing-infrastructure package released earlier today by HFSC Chairwoman Waters.

- **FEDERALRESERVE63**: Signaling a tough challenge for a second Powell term, Senate Banking Chairman Brown (D-OH) today said, "It's time to try something different," also joining Sen. Warren (D-MA) lambasting Mr. Powell's role in what they characterize as risky big-bank regulatory relief.

- **FEDERALRESERVE62:** Although much of today's HFSC hearing with Chairman Powell was preoccupied by hot debate over the extent to which inflation is "transitory," key financial-policy questions also surfaced for substantive discussion.

- **GSE-071221**: On Friday, former FHFA Director Calabria suggested that the Administration's new competition policy powers up his proposal for authorizing multiple GSE charters just as a bank charter is granted to all qualified comers.

- **MERGER6**: In an executive order (EO) that truly deserves to be called "sweeping," President Biden today announced a "whole-of-government" initiative aimed at reducing market concentration, enhancing consumer choice, reducing prices, and enhancing economic equality.

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