FedFin Daily Briefing

Monday, October 3, 2022

Gruenberg Commits to Climate-Risk Standards, Cautious on Premium Hike

Acting FDIC Chairman Gruenberg today strongly defended banking-agency action addressing climate risk, indicating that the FDIC will advance pending risk-management principles akin to those pending from the OCC (see FSM Report **GREEN12**) along with working with the Fed. Although the FDIC plays no role in climate policy, Mr. Gruenberg states that climate risk poses financial risks and thus falls squarely within the ambit of safety-and-soundness considerations. He also emphasized the importance of continuing international collaboration and better data, risk management, and dialogue across the banking industry, and tailored climate standards. Under questioning, Mr. Gruenberg also seemed sympathetic to suggestions that the FDIC's proposed premium increase (See FSM Report **DEPOSITINSURANCE114**) may not be needed in light of recent slowing and even reversal of deposit growth.

FRB-Chicago Study: Big U.S. Banks are Oligopolists

A new Federal Reserve Bank of Chicago working paper finds that U.S. banking has become increasingly concentrated judged by the top-five bank's market share and a standard market-power index, concluding that this "oligopolistic" sector is thus able to charge undue fees to weaker corporate customers. This in turn increases capital misallocation, reduces productivity, and increases macroeconomic shocks. The model-driven study also finds that failure of a large bank allows remaining firms to increase their market power, prolonging recessions. The paper thus suggests that policy should bail out troubled giant banks. To the extent this paper has any impact on policy, it is likely to be on mergers, making standards more stringent, rather than leading regulators to allow TBTF intervention.

Warren Zelle Report Finds "Rampant" Fraud, Slams Banks

Following the hearing with large-bank CEOs (see *Client Report* **REFORM213**), Sen. Warren (D-MA) released a scathing report concluding that Zelle is plagued by "rampant and increasing fraud." The report also uses data provided to her by four large banks to conclude that banks repay only a fraction of unauthorized transactions in likely contravention of law and rule. Unlike her prior statements, Sen. Warren's report differentiates fraud from scams, implicitly conceding to the banks' assertion that they are not required to reimburse consumers when the consumer inadvertently or mistakenly authorizes a transaction. Looking solely at fraud, the paper finds that the banks reimbursed only 47% of fraud for which they are legally liable, noting also that fraud is rapidly increasing. Sen. Warren renews her call for the CFPB to govern Zelle and mandate reimbursement for all transactions a consumer believes to be fraudulent or in error. Guidance from the Bureau on Zelle and other money-transfer services that would increase payment-service provider liability appears imminent.

Board Defies Critics, Demands Two Networks for Online Debit Transactions

Ahead of possible Congressional action on legislation to restrict credit-card interchange fees (see FSM Report **INTERCHANGE10**), the FRB today voted 6-1 to finalize its controversial proposal (see FSM Report **INTERCHANGE8**) requiring debit-card issuers to enable at least two unaffiliated payment-card networks, including with regard to "card not present" transactions. We will shortly provide clients with an in-depth analysis of this rule, which the Board says is substantially the same as its proposal, adding only provisions clarifying compliance. Gov. Bowman was the lone dissenter, noting in her statement that the rule poses undue cost to community banks. No changes were made to interchange fees, but the board reiterated its commitment to review them. The rule will be effective on July 1, 2023.

FSOC Presses New Law, Rule, Supervisory Standards to Tackle Crypto Systemic Risk

As anticipated, the FSOC today approved a sweeping report on cryptoasset financial stability, finding that interconnectedness between this sector and the financial system poses significant risk that warrants structural action. FSOC thus recommends legislation to clarify market regulation, a move that would give the CFTC authority over the spot market without – as SEC Chairman Gensler emphasized today – altering the need for firms also to register with the Commission if they are engaged in securities activities. The report also wants cryptoasset firms subject to over-arching oversight reaching to affiliates and service providers, questioning the extent to which FTX can ensure instant clearing per a proposal pending before the CFTC. These recommendations reflect the report's broader focus on regulatory arbitrage, with recommendations provided on interagency coordination and stablecoin legislation. The report also initiates a study investigating whether crypto firms' vertical integration poses new risks. CFPB Director Chopra urged FSOC to designate any bigtech company that issues stablecoins as a financial market utility and acting Comptroller Hsu emphasized the importance of enforcement as agencies and Congress address regulatory arbitrage. We will shortly provide clients with an in-depth analysis of the FSOC report. FSOC also announced a new climate-risk advisory committee, with staff describing work on Treasury's cloud service provider report. This assesses potential risks of cloud software and infrastructure and challenges faced by smaller banks. The report is due by the end of the year.

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-100322:** Our take on the first two days of FHFA's FHLB "listening session" last week is that battle lines are shaping up much as we expected with the exception of a couple of powerful groups with new ideas about how the System could be put to better use for themselves and/or the public interest.

- **MORTGAGE121:** The CFPB has asked for views on the extent to which it can facilitate certain refinancing (refi) products it believes enhance economic justice.

- **GSE-092622:** As will be evident in our forthcoming in-depth analysis, the CFPB's fusillade last week on mortgage-finance could have far-reaching implications for the entire market based on how far it takes

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its new campaign for equitable housing finance and whether the market is willing to come along on at least some of the agency's new ideas.

- **AML136:** Treasury is seeking comments on issues raised by the President's executive order (EO) on digital assets to guide further work curbing illicit-finance and national-security risks in this sector.

- **REFORM213:** Senate Banking's hearing with big-bank CEOs proved much more combative than HFSC's session yesterday (see *Client Report* **REFORM212**).

- **GSE-092222:** In this report, we follow our earlier analysis of Treasury's CBDC recommendations and housing finance with an analysis of another Treasury report in response the President's executive order focused on the overall construct of cryptoassets in the U.S.

- **REFORM212:** At today's big-bank oversight HFSC hearing, Committee Democrats focused on each bank's progress on social issues, such as internal diversity, unionization, and historic roles in financing slavery.

- **GSE-092122:** In this analysis, we drill down in Treasury's high-impact reports to the President on the future of digital assets to identify key considerations and strategic implications for housing finance.

- **CRYPTO32:** We follow our prior in-depth analysis of Treasury's CBDC and payments report (see *Client Report* **CBDC14**) with a detailed assessment of the Department's assessment of overall cryptoasset policy.

- **SANCTION19:** Today's Senate Banking hearing on Russian sanctions showcased bipartisan concern that anti-Russian sanctions have yet to have meaningful impact and doubts about the extent to which oil-price caps will reverse this.

- **CBDC14:** In this in-depth report, we follow through as promised on our initial analysis of key sections in last Friday's Treasury report on CBDC and changes to the payment system.

- **INVESTOR20:** The Senate Banking hearing with Chairman Gensler today went as expected: Democrats generally praised his work while Republicans strongly opposed it on both substantive and procedural grounds.

- **INSURANCE61:** Chairman Brown (D-OH) convened a hearing today focused on the insurance industry largely focusing on the extent to which private-equity takeovers endanger insurance solvency and threaten pensioners following risk transfers.

- **GSE-090722:** Reinforcing the sharp turn-around in housing markets evident since the Fed surprised markets with its first 75 bps hike, a new working paper from the San Francisco Fed provides the first hard evidence of how monetary-policy shocks in the U.S. hit listing prices hard and fast.

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