



Friday, June 16, 2023

Waller Separates Monetary, Stability Policy

FRB Gov. Waller [today](#) defended recent rate hikes against criticism that they undermine financial stability, noting that monetary and stability policy are inter-related but must generally be addressed with different tools. The Fed's financial-stability toolkit includes bank regulation and supervision as well as emergency liquidity for banks and "other intermediaries," tools which he said have been proved effective. The FOMC is monitoring the impact of higher rates on credit availability but sees no significant issues and, regardless, must focus on reducing inflation to target levels to adhere to the Federal Reserve's mandate.

Brown-Scott Clawback Bill Adds Enforcement Teeth

In his first legislative mark-up since assuming the chairmanship in 2021, Banking Committee Chairman Brown (D-OH) will convene voting next [Wednesday](#) on compromise compensation-reform legislation on which he and Ranking Member Scott (R-SC) have agreed. This bill does not go as far as the Warren-Vance measure ([see FSM Report COMPENSATION36](#)), for example reinstating current law with regard to FDIC discretion to seek clawbacks. As we noted in our analysis, this flexibility may be necessary to ensure that troubled banks are able to attract the talent necessary for a turn-around. Indeed, the bill now expressly protects "white knights." Sen. Warren (D-MA) has signaled stiff opposition to the measure, which also slightly scales back how much prior compensation is at risk. The new bill retains her compromise exemption for banks with assets under \$10 billion. The Brown-Scott bill also includes standards mandating improvements to bank incentive alignment and governance, also giving the banking agencies additional powers to oust management deemed deficient on safety and soundness grounds, with regulators also given greater civil money penalty authority for "reckless" violations of safety-and-soundness standards or failure to adhere to fiduciary duty.

Hsu Warns of Tokenized-Settlement, AI Risk

Acting Comptroller Hsu's [speech](#) today highlights both the benefits and risks of tokenization and AI, urging parallel development of new technologies and essential controls. Emphasizing the importance of trust on which the OCC is now focused for banks ([see FSM Report CONSUMER50](#)), Mr. Hsu decries crypto but asserts that centrally-operated blockchains have considerable potential via tokenized real-asset settlement perhaps, Mr. Hsu hints, via CBDC. Nevertheless, many legal questions remain before tokenized settlement is viable from the OCC's supervisory perspective. Turning to AI, Mr. Hsu reiterates longstanding regulatory concerns about objective alignment and unintended consequences not only regarding discrimination, but also fraud and misinformation. Thus, both tokenization and AI adoption requires staged implementation that pairs control build-out and testing with product offerings. New third-party guidance ([see FSM Report VENDOR10](#)) must thus be carefully followed, he says, with national banks told to get prior supervisory approval for significant innovation rather than expecting forgiveness if things go wrong.

Democrats Try Again To Mandate TILA, CFPB Small-Business Authority

Banking Committee member Sen. Menendez (D-NJ) yesterday [introduced](#) legislation (S. 2021) along with Small Business Committee Ranking Member Velazquez (D-NY) (H.R. 4192) to extend TILA protections to small business lending, also giving the CFPB authority in this sector. The bills aim to protect small business borrowers against predatory lending, bar financing options with unfair terms and conditions, ensure existing TILA consumer lending safeguards, and enhance transparency in small commercial-loan originations. Sen.

Menendez's bill has three cosponsors, including Senate Banking Chairman Brown (D-OH), Finance Committee Chairman Wyden (D-OR), and Small Business Committee Chairman Cardin (D-MD) and stands a chance in the Senate. Rep. Velazquez's bill is cosponsored by HFSC Ranking Member Waters (D-CA) but is sure not to advance through HFSC in light of strong GOP antipathy to the CFPB ([see Client Report CONSUMER51](#)).

Fed Fears Little Systemic Risk

The financial-stability discussion in today's [report](#) from the Federal Reserve ahead of next week's hearings generally reiterates conclusions from the most recent Fed financial-stability report ([see Client Report SYSTEMIC96](#)): banks are generally sound and resilient and, despite MMF worries, most other vulnerabilities are of only moderate systemic concern. The discussion also reiterates key factors in recent bank failures and regional-bank stress, noting that the Fed continues to monitor them and is prepared to "use all its tools" should stress resume. Contradicting calls for new rules, the report also says that most banks are well capitalized and hold ample liquidity, reiterating the Fed's view that SVB and SBNY were idiosyncratic cases.

Fed's Long-Awaited Master-Account Database Goes Live

Conceding to a long-resisted and now statutory demand ([see FSM Report PAYMENT25](#)), the Federal Reserve today [published](#) the first database detailing who has or seeks access to Reserve Bank master accounts and services. The list of firms seeking access reflects those with requests pending on December 23, 2022, or which have since filed a request. Going forward, this database will be updated on a quarterly basis, with the application-status lists allowing better understanding of which Reserve Banks have granted access to which companies – an issue of significant importance in the wake of controversies surrounding decisions by the Kansas City Fed for several nonbanks in recent years.

LIBOR Transition Worries FSOC

The [readout](#) from FSOC's meeting this afternoon makes it clear that the LIBOR transition was the top concern, but the brief note provides no insight into FSOC's thinking beyond reiterating that it "expects" entities to be operationally ready. The readout also reiterates CRE concerns and ongoing monitoring, with the Council continuing to conclude that U.S. banks are generally well capitalized and have the ample liquidity also noted earlier today in the Fed's semiannual Congressional report. Finally, the comment period on the Council's proposed systemic methodology ([see FSM Report SYSTEMIC95](#)) and new SIFI-designation methodology ([see FSM Report SIFI35](#)) will be extended for thirty days, perhaps reflecting in part criticism [Wednesday](#) from HFSC Chairman McHenry (R-NC).

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-061523](#): The FHFA's [report to Congress](#) this year was eagerly awaited to see if it shed any insight into what FHFA might do after its listening [sessions](#) and Sandra Thompson's [promise](#) to do something sometime soon about the Home Loan Banks.

- **CONSUMER51**: With Rep. Andy Barr (R-KY) leading the attack with an accusation of CFPB “McCarthyism,” today’s HFSC hearing with Director Chopra tracked much in yesterday’s Senate Banking [session](#).
- **REFORM227**: Treasury Secretary Yellen was pressed at today’s HFSC hearing to comment on pending bank capital standards, the scope of FDIC coverage, and failed-bank resolutions.
- **CONSUMER50**: Reflecting Acting Comptroller Hsu’s focus on consumer protection, fairness, and inclusion, the OCC is seeking views on what could become an annual survey of what consumers and especially bank customers think of their bank.
- **VENDOR10**: After frequently citing third-party relationships and outsourcing as worrisome risk, the banking agencies have now finalized guidance first proposed in 2021 to govern them.
- **GSE-060823**: As we will detail in a forthcoming in-depth report, the banking agencies’ new “guidance” on third-party vendors essentially brings all nonbank counterparties with whom banking organizations deal under the agencies’ enforcement thumb.
- **COMPENSATION36**: Sen. Warren (D-MA) has introduced a revised version of legislation to ensure that both the FDIC and other federal banking agencies can demand that executives and others governing failed banks refund direct and indirect compensation to the federal government.
- **GSE-060223**: As we detailed earlier this [week](#), the OCC’s new enforcement [policy](#) is a paradigm shift in terms of the legal and reputational risk run by national banks and federal thrifts – that is, by the depository institutions that matter the most to mortgage finance.
- **CHINA17**: While largely focused on countering fentanyl, today’s Senate Banking hearing on China, saw Committee Democrats try to ascertain the details of a potential outbound investment [executive order](#) and Republicans addressing what they believe to be shortcomings in data privacy, AML regulation, and sanctions policy.
- **SUPERVISION2**: Following a speech earlier this year by the Acting Comptroller arguing that some banks are “too big to manage” and the furor caused by recent failures, the OCC has significantly revised its enforcement policy.
- **GSE-052323**: Today’s HFSC hearing with Sandra Thompson was the anti-LLPA event we [anticipated](#) when it came to Republicans that also saw the stout defense Democrats were sure to provide combined with FHFA’s resolute stand on doing nothing to change the LLPAs or guarantee-fees beyond what might come of the pending [RFI](#).
- **REFORM226**: Describing the CEOs’ statements at his last hearing as “the dog-ate-my-homework” excuses for grievous failings, Senate Banking Committee Chairman Brown (D-OH) also attacked Republicans for placing blame on monetary policy, not the culture of supervisory laxity he details with various quotes from Trump Administration officials.
- **CRYPTO44**: Although there were still considerable party-line differences of opinion on stablecoin legislation, today’s HFSC Digital-Assets Subcommittee hearing suggests that remaining divides are narrowing, increasing the odds of a new federal-regulatory framework.
- **GSE-051723**: With Republicans on the anti-LLPA warpath, FHFA is hoping to preserve as much of the current fee structure as possible without paying too high a political price, issuing a [request for information](#) (RFI) in hopes that letter-writing will keep everyone busy until Congress moves on to other matters.
- **REFORM225**: A joint hearing today of HFSC’s Financial Institutions and Oversight Subcommittees expanded on themes at yesterday’s full Committee session with bank regulators ([see Client Report REFORM224](#)) and Senate Banking’s session with SVB’s and SBNY’s [CEOs](#), with First Republic’s CEO now added to the Congressional firing line.