FedFin Daily Briefing

Wednesday, October 11, 2023

Bowman Targets U.S. Leverage Ratio, NBFIs

In remarks during the Morocco IMF/Bank meeting today, FRB Gov. Bowman contrasted U.S. bank resilience with the IMF's findings yesterday on potential vulnerabilities as rates rise and macroeconomic conditions soften. She instead pointed to U.S. bank resilience, noting that the majority of institutions are managing both interest-rate and credit risk, although some banks face challenges due to reliance on higher-cost, volatile funding and CRE concentrations. NBFI risk is also a top concern, focusing here on hedge funds, prime funds, insurance companies, some bond funds, and the Treasury market. Ms. Bowman reiterated the importance of enhanced bank supervision in concert with limited regulatory changes and like-kind rules for nonbanks executed in part by the FSB and via domestic standards addressing matters such as hedge-fund leverage. Notably, Ms. Bowman argued that a key approach to reducing Treasury-market risk is to conform the U.S. leverage ratio to international norms rather than continue current, higher requirements. Gov. Bowman supports current efforts to ensure banks are operationally ready to use the discount window or their Fed backstops, but says contingency-funding planning should only be encouraged, not mandated.

FSB Reiterates Stability Concerns

The FSB's latest work plan reiterates all it most recently said to the G20. Global regulators continue to prioritize cryptoassets, NBFIs, CCPs, climate, cross border payments and GSIB resolution as key vulnerabilities in the global financial system. They also continue to highlight the importance of implementing the Basel framework.

CFPB Barrels Down on "Basic" Banking Fees

In conjunction with a new White-House junk-fee initiative, the CFPB today issued "guidance" – i.e., essentially a final rule – banning large banks and credit unions from collecting "unreasonable" fees for what the Bureau considers reasonable and "basic" account information. We will shortly provide clients with an in-depth analysis of the new standards, which the White House announcement says is a flat-out ban. In practice, it seems to be a prohibition based on CFPB bank-by-bank determinations, but we will address this question in our in-depth assessment. Regardless, it is clear that the Bureau intends the standard to bite. Although monetary penalties are said to be possible only for violations of the guidance found after February 1, 2024, the Bureau is already undertaking enforcement actions in this area with civil monetary penalties. In conjunction with the new advisory, the Bureau issued supervisory "highlights" reiterating the guidance and noting fees have already been imposed when fees are not only improperly related to a basic service, but also found to be deceptive because the consumer did not in fact receive the service. The FTC today also released a proposal countering fees it deems "junk" from nonbanks. While the rule would principally target resort and ticketing fees, it also has implications for non-bank lenders so far outside the CFPB's guidance. Both the White House and Mr. Chopra also confirm statement last week that the agency will soon release its open-banking proposal (see FSM Report **DATA**), now linking this to junk fees and the broader question of consumer rights.

SEC Throws Wrench into TLAC Standards

As we noted yesterday, the FSB's assessment of the global resolution framework's effectiveness found significant glitches it urges national regulators quickly to address via standards such as those now pending in the U.S. to bring smaller banking organizations into the resolution-planning regime (see FSM Report **LIVINGWILL23**). As in Basel's analysis of the 2023 crash (see *Client Report* **REFORM228**), the FSB also raises significant concerns about the ability of resolution authorities to deploy bail-in debt such as the AT1 instruments that proved so problematic in the CS resolution. However, the details of FSB's report suggest a substantive and immediate challenge for all GSIBs operating in the U.S. when it comes to complying with home-country TLAC standards and thus with U.S. requirements (see FSM Report **TLAC6**). The report notes that SEC staff believe that triggering bail-in debt creates an equity obligation that must be considered a registered security under U.S. law. As a result, resolution planning by banks and national authorities needs to ensure operational readiness quickly to obtain SEC registration upon the trigger (which is said to constitute sale of a registered security). Registration in turn is dependent on acceptable pro forma financial statements; the SEC does not observe in the FSB report that these were not available from CS, meaning that AT1 instruments could not have been registered, and CS would have violated U.S. securities law but for the fact that it failed, making the violation substantively moot. Given all this, the FSB plans further work with the SEC to let national banking authorities do what is needed in terms of TLAC planning and execution, but we expect many GSIBs will reconsider the balance between bail-in and long-term debt in order to comply with current TLAC requirements. This is essentially the approach taken in the U.S. to GSIBs, although they are not required to issue the internal TLAC proposed for regional banking organizations (see FSM Report **TLAC9**).

OFR Study: Short-Selling Does Not Harm Financial Stability

OFR today released a model-based study that finds no evidence that short-selling adversely affects financial stability. Short-selling restrictions are said to result in increased returns, lower spot volatility, narrower spreads, and an increase in depth at best ask price, suggesting that at least some short sellers switch from removing liquidity from the bid side to providing liquidity on the ask side. The blog post accompanying the study suggests that these benefits boost financial stability because, despite the restrictions being short-lived, the price impacts are persistent.

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.

- **REFORM228:** As we noted yesterday, the Basel Committee's October meeting concluded not only with plans for new disclosure consultations, but also a report on lessons learned from the 2023 crisis.
- **GSE-100223:** As we noted earlier today, the FRB has issued a seemingly technical FAQ liberalizing the treatment of certain credit-linked notes.
- **GSE-092523:** In her Congressional testimony last week, FedFin managing partner Karen Petrou focused on the unintended consequences wrought by new banking proposal based on their cumulative impact.

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

- **GSE-092023**: Or maybe it is, but not everyone has heard.

- **LIVINGWILL23**: Although a pending FDIC/FRB proposal imposes a raft of new requirements for resolution plans from IDIs with over $100 billion in assets, the FDIC has also issued a freestanding proposal doing the same, also setting information-filing standards for IDIs below $100 billion but above $50 billion.

- **CAPITAL235**: With HFSC Chairman McHenry (R-NC) leading the way, GOP Members of the panel's Financial Institutions Subcommittee today blasted the banking agencies' end-game proposal (see *Client Report* **CAPITAL234**).

- **LIVINGWILL22**: In conjunction with proposing a new long-term debt (LTD) requirement for categories II, III, and IV banks, the Fed and FDIC are pursuing other ways to enhance resolvability.

- **TLAC9**: Building on an advance notice of proposed rulemaking, the banking agencies have issued several proposals to enhance the resolvability of large banking organizations not covered by stringent GSIB standards.

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