FedFin Daily Briefing

Friday, December 15, 2023

Crypto Measures Await Next Session

As anticipated, HFSC Chair McHenry (R-NC) was able to fend off concerted efforts by Sens. Brown (D-OH) and Warren (D-MA) to add the Warren-Marshall crypto bill to the National Defense Authorization Act. Indeed, this must-pass bill is stripped clean of financial-services provisions. The next target for negotiations over this bill and Rep. McHenry's broader crypto-jurisdiction and stablecoin bills is the appropriations measures that must be resolved in January to avoid yet another government shut-down. It seems unlikely that agreements on all of these bills will be reached by then, likely moving these issues forward until Rep. McHenry is able to reach some agreement with Democrats on how the SEC is treated in the jurisdiction bill and the extent to which the measure preserves investor protections. The role of the FRB in stablecoin regulation also remains a significant sticking point.

FSOC to Target Hedge Funds, Nonbank Mortgage Companies

The readout from Treasury on yesterday's FSOC meeting provides insight into the Council's executive session suggesting significant near-term systemic action regarding hedge funds. The readout not only says that the Council reviewed its longstanding working group's deliberations, but that the group is determining hedge-fund risk in intermediating the Treasury market's systemic risk, a clear warning in our view that the Council itself is considering actions to address it. Nonbank mortgage servicers also remain on the Council's watch list and the OCC presented work on how best to monitor climate financial risk, a framework the Council intends to incorporate in its systemic-risk reviews. Our forthcoming analysis of FSOC's annual report will focus on these issues given the likelihood of near-term action.

FSB Plans Broad Rewrite of Public Backstops, GSIFI Resolvability, Operational Readiness

The FSB's 2023 Resolution Report today advises banks and public sector authorities to be prepared to access public sector funding in resolution, with the Board planning to review whether existing public sector backstops are adequate to meet potential failure scenarios. As noted, this is a significant issue in the wake of the March failures, with the banking agencies laying out guidance demanding discount-window readiness and Sen. Warner (D-VA) planning legislation to enforce it (see *Client Report* **GSIB23**). The FSB Resolution Steering Group will also conduct further work on public-sector backstop funding, the choice of resolution strategies and optionality of resolution tools, the interaction between resolution and deposit insurance, and ways for resolution authorities to respond to the speed of bank runs. The report also highlights plans for further work to assess GSIFI systemic significance, resolution planning, and loss-absorbing capacity, assessing whether some elements of its TLAC Principles (see FSM Report **TLAC4**) and Guiding Principles on Internal TLAC of GSIBs (see FSM Report **TLAC8**) could be applied to nonbanks – a more aggressive approach to NBFIs than presaged in the FSB's initial approach to this sector (see *Client Report* **NBFI2**). The U.S. would be hard-pressed to mandate any of these standards for nonbanks other than any FSOC came to designate although many foreign authorities have broader nonbank power and might choose to do so. Although it notes that the FSB's 2016 Guidance on Arrangements to Support Operational Continuity in Resolution (see FSM Report **RESOLVE40**) remains appropriate, increased use of digital services could create issues for contractual provisions, mapping of services, and governance arrangements, with the Board promising to clarify implementation of its guidance. Finally, the FSB will publish a final report on financial resources and tools for CCP resolution in the first half of 2024.

Brown Renews Bipartisan Quest to Constrain Nonbank Banks

Advancing the big-tech concerns he most recently voiced before GSIB CEOs (see *Client Report* **GSIB23**), Senate Banking Chairman Brown (D-OH) has introduced S. 3538, bipartisan legislation to impose bank regulation on non-bank parent companies of insured depository institutions. The measure is a redraft of provisions introduced at the end of the last Congress by Sens. Brown and Kennedy (R-LA) in somewhat different form (see FSM Report **ILC13**). We will shortly assess the bill in an in-depth report, but its requirement that parent companies comply with BHC requirements could generally force divestiture because of restrictions on BHC commercial activities unless the bill's drafting limits the rules to which these nonbanks would be subjected. Current ILC parents would be grandfathered, but changes in control would be barred. This bill is likely to advance in the Senate if Sen. Brown pursues it but will face challenges in the House despite strong banking-industry support for the measure.

DOJ Targets Fraudulent Microtransactions

Cracking down on unauthorized bank account charges, the DOJ today announced multiple actions against "sham" companies alleged to have used misrepresentations or unauthorized charges to steal money from consumers' financial accounts. Addressing part of the broader problem with fraudulent transactions, DOJ targets microtransactions and microdebits – large numbers of low-value, straw transactions – used by defendants to lower chargeback rates and conceal unauthorized charges.

CRS Warns Credit Card Act Could Result In Risky Retailer Payment Networks

The CRS this week issued a report analyzing the Durbin-Marshall Credit Card Competition Act, S.1838 (see FSM Report **INTERCHANGE10**), projecting that fee caps will have a greater impact on transaction fees than competition, with the bill in fact reducing merchant transaction fees. However, the report also warns of unintended consequences such as major retailers creating their own payment networks to cut out major payment networks, and thus tightening the connection between banking and commerce. Prohibitions on routing restrictions are found also to have varying results, with no clear mechanism for regulators to ensure that banks make networks available to merchants. The report claims merchants and consumers would not be incentivized to switch payment networks and suggests that the bill may also reduce payment security.

Progressives Again Push Public Banks

"Squad" Democrats such as Reps. Tlaib (D-MI) and Ocasio-Cortez (D-NY) have introduced H.R. 6775, the latest version of their efforts to facilitate state and local public banks. Unlike prior measures, the bill would tie public-bank charters to compliance with environmental-justice, labor, and similar standards and expressly give them access to FRB payment services. A new liquidity facility would also be set up for public banks along with an "incubator" for these charters and federal grants. The bill is unlikely to advance but revises debate over longstanding efforts to charter these banks by creating federal incentives and a more viable business proposition. FedFin has previously assessed public banks in two blog posts that may be found at https://economicequality.blog/2018/12/06/public-banking-under-a-blue-wave/ and https://economicequality.blog/2018/08/27/public-or-perish-the-future-of-public-banking/.

Senate Bill Seeks Supervisory Oversight

The rush of end-session bills also includes one from Sens. Moran (R-KS), Hagerty (R-TN), Tillis (R-NC), and Manchin (D-WV), S. 3541, that would force supervisors more quickly to answer bank queries and create an FFIEC independent review officer from whom banks could seek review of supervisory judgments. This official would be empowered to refer matters to an administrative law judge for dispute resolution upon a bank's request. The industry supports the measure which is more likely to advance in the House than 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.

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- **GSE-121423:** In a blog post today, Fannie quietly renews its quest for alternatives to traditional title insurance.

- **GSIB23:** The agencies' capital proposal (see FSM Report **CAPITAL230**) unsurprisingly dominated discussion at today's Senate Banking hearing with big bank CEOs.

- **FINTECH33:** At today's HFSC Digital Assets Subcommittee hearing on banking agency financial innovation, Republicans raised concerns about the Fed's novel activities guidance (see FSM Report **FINTECH32**), interagency guidance on third-party risk management (see FSM Report **VENDOR10**), and the SEC's predictive data analytics proposal.

- **CONSUMER54:** Today's Senate Banking hearing with Director Chopra was even more cordial than yesterday's HFSC session (see *Client Report* **CONSUMER53**) even though Republicans continued to criticize the Bureau's recent rulemakings.

- **GSE-113023:** A new FRB-NY study confirms that 83% of loans from 2000-2022 went to first-time homebuyers, compared to 56% for the GSEs and 57% for private lenders.

- **CONSUMER53:** In sharp contrast to most recent HFSC hearings with CFPB Director Chopra, today's session was relatively calm.

- **GSE-112723:** The most significant thing in FHFA's final capital rule is not what is to be done, but what FHFA left out: ending the GSEs' advanced-approach requirement.

- **DEPOSITINSURANCE122:** As the law requires and the FDIC Chairman promised after SVB and Signature Bank were declared systemic, the FDIC has finalized its proposed approach to imposing a systemic assessment to reimburse the Deposit Insurance Fund (DIF) for the resolution costs related to uninsured deposits following a systemic designation.

- **GSE-111623:** As our reports on the Senate and House hearings with bank regulators made clear, our prediction that the agencies would compromise on mortgage risk-based capital requirements will prove itself in the final standards.

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