

## Minutes of the Financial Stability Oversight Council

December 4, 2019

### PRESENT:

Steven T. Mnuchin, Secretary of the Treasury and Chairperson of the Financial Stability Oversight Council (Council)  
Jerome H. Powell, Chairman, Board of Governors of the Federal Reserve System (Federal Reserve)  
Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation (FDIC) Jay Clayton, Chairman, Securities and Exchange Commission (SEC)  
Heath P. Tarbert, Chairman, Commodity Futures Trading Commission (CFTC) Kathleen Kraninger, Director, Consumer Financial Protection Bureau (CFPB)  
Mark Calabria, Director, Federal Housing Finance Agency (FHFA)  
Joseph Otting, Comptroller of the Currency, Office of the Comptroller of the Currency (OCC) (by telephone)  
Rodney Hood, Chairman, National Credit Union Administration (NCUA)  
Thomas E. Workman, Independent Member with Insurance Expertise  
Dino Falaschetti, Director, Office of Financial Research (OFR), Department of the Treasury (non-voting member)  
Steven Seitz, Director, Federal Insurance Office (FIO), Department of the Treasury (non-voting member)  
Charles G. Cooper, Commissioner, Texas Department of Banking (non-voting member) (by telephone)  
Eric Cioppa, Superintendent, Maine Bureau of Insurance (non-voting member)  
Melanie Lubin, Securities Commissioner, Maryland Office of the Attorney General, Securities Division (non-voting member)

### GUESTS:

#### Department of the Treasury (Treasury)

Justin Muzinich, Deputy Secretary of the Treasury  
Bimal Patel, Assistant Secretary for Financial Institutions  
Kipp Kranbuhl, Principal Deputy Assistant Secretary for Financial Markets  
Howard Adler, Deputy Assistant Secretary for the Council  
Eric Froman, Assistant General Counsel (Banking and Finance)  
Stephen Ledbetter, Director of Policy, Office of the Financial Stability Oversight Council, and Executive Director of the Council

#### Board of Governors of the Federal Reserve System

Randal Quarles, Vice Chairman for Supervision  
Andreas Lehnert, Director, Division of Financial Stability

Federal Deposit Insurance Corporation

Travis Hill, Deputy to the Chairman for Policy

Securities and Exchange Commission

Jeffrey Dinwoodie, Chief Counsel and Senior Policy Advisor for Market and Activities-Based Risk

Commodity Futures Trading Commission

Jaime Klima, Chief of Staff and Chief Operating Officer

Consumer Financial Protection Bureau

Ryan Kelly, Financial Analyst

Federal Housing Finance Agency

Sandra Thompson, Deputy Director, Division of Housing Mission and Goals

Comptroller of the Currency

Morris Morgan, Deputy Comptroller for Supervision Risk Management

National Credit Union Administration Andrew

Leventis, Chief Economist Office of the

Independent Member with Insurance

Expertise

Charles Klingman, Senior Policy Advisor

Federal Reserve Bank of New York

John Williams, President and Chief Executive Officer (by telephone)

Office of Financial Research

Alexander Pollock, Principal Deputy Director for Research and Analysis

Federal Insurance Office

Bruce Saul, Senior Insurance Regulatory Policy Analyst

Texas Department of Banking

Michael Townsley, Policy Counsel, Conference of State Bank Supervisors (CSBS) (by telephone)

Maine Bureau of Insurance

Mark Sagat, Assistant Director, Financial Policy and Legislation, National Association of Insurance Commissioners

## PRESENTERS:

### *Repurchase Agreement Market Developments*

- *James Clouse, Deputy Director, Monetary Affairs, Federal Reserve*
- *Nathaniel Wuerffel, Senior Vice President, Federal Reserve Bank of New York*
- *Michael Hsu, Associate Director, Division of Supervision and Regulation, Federal Reserve (available for questions)*

### *2019 Annual Report*

- *Stephen Ledbetter, Director of Policy, Office of the Council, and Executive Director of the Council, Treasury*

### *Final Interpretive Guidance on Nonbank Financial Company Determinations*

- *Howard Adler, Deputy Assistant Secretary for the Council, Treasury*

## **Executive Session**

The Chairperson called the executive session of the meeting of the Council to order at approximately 3:53 P.M.

The Chairperson began by outlining the meeting agenda, which had previously been distributed to the members together with other materials. The agenda for the executive session of the meeting included repurchase agreement market developments.

### 1. Repurchase Agreement Market Developments

The Chairperson then introduced the first agenda item, a presentation on repurchase agreement market developments. The Chairperson introduced James Clouse, Deputy Director of the Division of Monetary Affairs at the Federal Reserve, and Nathaniel Wuerffel, Senior Vice President at the Federal Reserve Bank of New York.

Mr. Clouse began by describing the decision in January 2019 by the Federal Open Market Committee (FOMC) to continue operating in an ample reserves regime. He explained that under this regime, administered rates were the primary means of control over the federal funds rate and other short-term interest rates. He stated that the ample reserves regime provided a sufficient supply of reserves so that short-term changes in demand for or supply of reserves do not result in large moves in the federal funds rate. He noted that the FOMC monitored a wide range of information to determine the appropriate level of reserves in an ample reserves regime. He then stated that there was significant volatility in repurchase agreement (repo) rates in mid-September 2019. He attributed the market volatility to a number of factors, including large corporate tax payments and the settlement of Treasury security auctions. He stated that the Federal Reserve continued to study the reasons for the volatility.

Mr. Wuerffel then described the Federal Reserve's response to the September 2019 repo market volatility. He noted that in September 2019, the Federal Reserve had conducted term and overnight repos to ease pressures in the repo market and to limit the risk of spillover to the federal funds market. He noted that the Federal Reserve's repo operations (1) supplied funding and reserves and (2) influenced short-term interest rates. He noted that the Federal Reserve's repo operations had resulted in a decrease in the federal funds rate. He stated that in October 2019, the FOMC had reaffirmed its policy implementation in the ample reserves regime, including ensuring ample reserves through purchases of Treasury bills at least through the second quarter of 2020. He stated that the Federal Reserve was also conducting term and overnight repos at least through January 2020. He stated that the Federal Reserve's open market operations had been effective, and that the federal funds rate was within the FOMC's target range and that pressures in money markets had receded. He also described changes over time in the total amount of reserves in the banking system. He concluded by highlighting that it was typical for there to be temporary pressures on money market rates around the end of the calendar year, and that the Federal Reserve was monitoring conditions and would adjust its repo operations as necessary. He concluded by noting that the Federal Reserve would continue to conduct research on the causes of the recent dislocations in money markets.

Council members then asked questions and had a discussion, including the reasons for the significant decrease in total reserves in mid-September and potential causes of the repo market volatility.

## 2. Other Business

The Chairperson then noted that Treasury had hosted a meeting with regional banks regarding the transition away from the London Interbank Offered Rate (LIBOR) to the Secured Overnight Financing Rate (SOFR). He stated that he would work with the other Council member agencies to understand issues related to the transition.

The Chairperson adjourned the executive session of the meeting at approximately 4:13 P.M.

## **Public Session**

The Chairperson called the open session of the meeting of the Council to order at approximately 4:18 P.M.

The Chairperson outlined the agenda for the open session, which included (1) a vote on the Council's 2019 annual report, (2) a vote on the Council's final interpretive guidance on nonbank financial company determinations, and (3) a vote on the minutes of the Council's meeting on November 7, 2019.

### 1. 2019 Annual Report

The Chairperson then turned to the first agenda item, the Council's 2019 annual report. The Chairperson noted that the Council's annual report was the product of extensive analysis and

collaboration across the Council's member agencies. He stated that the report provided the Council's assessment for the public of the Council's view of potential risks across the financial system, and included recommendations to enhance the integrity, efficiency, competitiveness and stability of U.S. financial markets. The Chairperson stated that the report highlighted recent accomplishments and areas where further work was needed.

The Chairperson then introduced Stephen Ledbetter, Director of Policy in the Office of the Council, and Executive Director of the Council, at Treasury, to provide an overview of the report's findings and recommendations.

Mr. Ledbetter began by stating that the Council reports annually to Congress on significant financial market and regulatory developments, potential emerging threats to U.S. financial stability, and the Council's activities. He noted that the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) requires the annual report to include Council recommendations to enhance U.S. financial markets, promote market discipline, and maintain investor confidence. He stated that this report noted the continued strength of the U.S. economy, as reflected in low unemployment rates, low corporate and consumer delinquency and default rates, and financial conditions that were broadly stable.

Mr. Ledbetter stated that, according to the report, overall risks to U.S. financial stability remained moderate. He noted that the report nonetheless emphasized the importance of remaining vigilant regarding potential emerging threats to financial stability, and discussed potential vulnerabilities and recommendations for addressing them. Mr. Ledbetter then provided a brief summary of key topics discussed in the report.

Mr. Ledbetter first focused on cybersecurity risks. He stated that the report discussed the increasing reliance of the financial system on information technology, and the increased risk that institutions may experience a severe cybersecurity event. He noted that the report included a number of recommendations, including that Council member agencies continue information technology and cybersecurity examinations of financial institutions and infrastructure. He stated that the report also encouraged continued cooperation across government agencies and the private sector through the use of existing partnerships, such as the Financial and Banking Information Infrastructure Committee.

Mr. Ledbetter noted that a second issue highlighted in the report was the anticipated cessation or degradation of LIBOR and the importance for markets of the transition to alternative reference rates. He stated that the report noted the risks to institutions that fail to adequately prepare for the transition away from LIBOR, and discussed the work of the Alternative Reference Rates Committee and others to facilitate the transition. He noted that the report also included recommendations regarding the importance of market participants formulating and executing transition plans, and of Council member agencies using their authorities to identify and mitigate risks from potential dislocations during the transition process.

Mr. Ledbetter stated that a third issue discussed in the report was the increase in borrowing and leverage by nonfinancial businesses. He noted that by several measures, leverage was elevated relative to historical averages. He stated that this increased borrowing reflected, in part, the strong performance of the U.S. economy and expectations for continued economic growth. He noted that strong interest coverage and liquidity positions had allowed businesses to service their debts with low delinquency rates. Mr. Ledbetter stated that the report noted the potential for conditions to change. He noted that any potential impact on financial stability depended on a number of factors, including the severity of market losses and the extent to which market participants are adequately capitalized and hold liquid assets. He stated that the report therefore made a number of recommendations, including that agencies continue to monitor levels of nonfinancial business leverage, trends in asset valuations, and potential implications for the entities they regulate, in order to assess and reinforce their ability to manage losses.

Mr. Ledbetter stated that a fourth issue discussed in the report was the risk associated with the increasing share of residential mortgages originated and serviced by nonbanks. He noted that the report discussed the potential fragility of the nonbank business model, and included a recommendation that federal and state regulators coordinate in collecting data, identifying risks, and strengthening oversight of nonbank mortgage companies.

Mr. Ledbetter noted that a fifth issue discussed in the report was the growth of technological innovations in the financial system, including the growth of digital assets and distributed ledger technologies. He stated that the report noted that, if digital assets were to become widely adopted as a means of payment or a store of value, disruptions could affect the wider economy. Mr. Ledbetter noted that the report therefore encouraged continued coordination among U.S. financial regulators, including through the Council's digital asset and distributed ledger technology working group, to promote consistent regulatory approaches and to identify and address potential risks.

As a sixth issue, Mr. Ledbetter noted that the report reaffirmed the Council's view regarding the urgency of housing finance reform. He noted that the report recommended that the FHFA continue to develop capital and other prudential requirements for Fannie Mae and Freddie Mac to help inform their application to future secondary market housing entities, upon completion of housing finance reforms. He stated that the report also recommended that regulators and market participants take steps to encourage a larger role for private capital in the housing finance system.

Finally, Mr. Ledbetter stated that the report discussed some of the actions that Council member agencies had taken to enhance the efficiency of financial regulation by tailoring regulation to the risks posed by firms and activities. He stated that the report recommended that federal and state regulators continue to work together to evaluate regulatory overlap and duplication, modernize outdated regulations and, where authority exists, continue to tailor regulations based on the size and complexity of financial institutions. Mr. Ledbetter concluded by stating that the report was a collaborative effort among Council members and member agencies.

After Mr. Ledbetter's remarks, the Chairperson presented to the Council the following resolution approving the annual report:

*WHEREAS, the Financial Stability Oversight Council (the "Council") under section 112 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") is required to annually report to and testify before Congress on (1) the activities of the Council; (2) significant financial market and regulatory developments, including insurance and accounting regulations and standards, along with an assessment of those developments on the stability of the financial system; (3) potential emerging threats to the financial stability of the United States; (4) all determinations made under section 113 or title VIII of the Dodd-Frank Act, and the basis for such determinations; (5) all recommendations made under section 119 of the Dodd-Frank Act and the result of such recommendations; and (6) recommendations (a) to enhance the integrity, efficiency, competitiveness, and stability of U.S. financial markets; (b) to promote market discipline; and (c) to maintain investor confidence; and*

*WHEREAS, the staffs of the Council members and their agencies prepared the attached 2019 annual report of the Council (the "2019 Annual Report") pursuant to section 112 of the Dodd-Frank Act, and members of the Council have reviewed and commented on the attached report.*

*NOW, THEREFORE, BE IT RESOLVED, that the Council hereby approves the 2019 Annual Report and authorizes the Chairperson, or his designee, to take such actions as they may deem necessary or appropriate to transmit the 2019 Annual Report to Congress and to release it to the public; and*

*BE IT FURTHER RESOLVED, that the Council hereby delegates authority to the Chairperson, or his designee, to make technical, nonsubstantive, or conforming changes to the text of the 2019 Annual Report and to take such other actions as they may deem necessary or appropriate to prepare the report for transmittal to Congress and release to the public.*

The Chairperson asked for a motion to approve the resolution, which was made and seconded. The Council approved the resolution by unanimous vote.

## 2. Final Interpretive Guidance on Nonbank Financial Company Determinations

The Chairperson then introduced the next agenda item, the Council's final interpretive guidance on nonbank financial company determinations. The Chairperson stated that the final interpretive guidance represented the culmination of nearly two years of work by Council members and their staff. He stated that the Council was making these changes after review of public comments regarding the proposed guidance, which he stated were largely positive. He stated that the final interpretive guidance enhanced how the Council identified, assessed, and responded to potential risks to U.S. financial stability. The Chairperson noted that the final interpretive guidance prioritized an activities-based approach that would rely on existing regulators to address potential

risks to financial stability. He also noted that the guidance enhanced the Council's process for evaluating nonbank financial companies for potential designation.

The Chairperson then introduced Howard Adler, Deputy Assistant Secretary for the Council at Treasury, to provide an overview of the final interpretive guidance.

Mr. Adler began by noting that the final interpretive guidance would replace the Council's existing interpretive guidance on nonbank financial company determinations, which was adopted in 2012. Mr. Adler stated that in March 2019, the Council issued proposed interpretive guidance for public comment. He noted that the Council had received 26 comments, most of which supported the Council's proposal.

Mr. Adler stated that the final guidance described the approach the Council intended to take in using an activities-based approach. He noted that the key focus of the guidance was on the Council working with relevant financial regulators to identify products, activities, or practices that could raise potential risks to financial stability and to address those risks, leveraging the expertise of primary financial regulatory agencies. Mr. Adler stated that the guidance also included reforms designed to enhance the analytical rigor and transparency of the process the Council intended to follow if it were to consider designating a nonbank financial company, including a cost-benefit analysis, the consideration of the likelihood of the company's material financial distress, and pre- and post-designation off-ramps. He noted that the guidance stated that the Council would be most likely to pursue entity-specific nonbank designations only in rare instances, such as if the products, activities, or practices of a company that pose a potential threat to U.S. financial stability are outside the jurisdiction or authority of financial regulatory agencies. Mr. Adler stated that the guidance emphasized the importance of market discipline as a mechanism for addressing potential risks to U.S. financial stability.

Mr. Adler stated that the guidance would establish a two-step process for the activities-based approach. He stated that the Council would first monitor markets to identify and assess potential risks to U.S. financial stability. Mr. Adler noted that if, in the first step, the Council identifies a risk to financial stability, then in the second step the Council would work with relevant regulators to seek the implementation of actions intended to address the potential risks. He noted that in response to comments, the guidance provided detail regarding how the Council would take into account the risk profiles and business models of market participants engaging in the products, activities, or practices under evaluation.

Mr. Adler stated that the final guidance also required a cost-benefit analysis if the Council seeks to issue any formal, nonbinding recommendations to a regulator under section 120 of the DoddFrank Act. He noted that this cost-benefit analysis would be performed either by the existing regulator or by the Council, depending on circumstances. Mr. Adler stated that if a potential threat cannot be addressed through an activities-based approach, the Council may evaluate a nonbank financial company for a potential determination.



Mr. Adler stated that the guidance would make several changes to enhance the analytical rigor and transparency of the nonbank designation process. He noted that the guidance condensed the previous three-stage designation process into two stages, by eliminating the previous stage 1. He further noted that the Council would perform a cost-benefit analysis under the guidance prior to designating any nonbank financial company. Mr. Adler stated that only if the expected benefits from the designation justify the expected costs would the Council make the designation. He noted that the Council would also assess the likelihood of a nonbank financial company's material financial distress when evaluating the firm for a potential designation. He stated that both the cost-benefit analysis and assessment of likelihood had been revised in the final guidance to provide greater clarity about how the Council would perform those analyses.

Mr. Adler stated that the guidance would also increase the Council's engagement with companies and their existing regulators before and during the designation process. He noted that the increased engagement would provide a company with a potential pre-designation "off-ramp." He noted that the guidance also included procedures intended to clarify the post-designation "off-ramp." In addition, Mr. Adler stated that in response to public comments, the guidance required a vote of the Council to advance from the activities-based approach to consideration of a nonbank financial company for potential designation.

The Chairperson then presented to the Council the following resolution approving the final interpretive guidance on nonbank financial company determinations:

*WHEREAS, the Council's duties under section 112 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") include monitoring the financial services marketplace in order to identify potential threats to U.S. financial stability; recommending to the Council member agencies general supervisory priorities and principles reflecting the outcome of discussions among the member agencies; identifying gaps in regulation that could pose risks to the financial stability of the United States; and making recommendations to primary financial regulatory agencies to apply new or heightened standards and safeguards for financial activities or practices that could create or increase risks of significant liquidity, credit, or other problems spreading among financial companies and markets; and*

*WHEREAS, section 113 of the Dodd-Frank Act authorizes the Council to determine that a nonbank financial company shall be supervised by the Board of Governors of the Federal Reserve System (the "Federal Reserve") and shall be subject to prudential standards if the Council determines that material financial distress at the company, or the nature, scope, size, scale, concentration, interconnectedness, or mix of the activities of the company, could pose a threat to the financial stability of the United States; and*

*WHEREAS, on April 3, 2012, the Council approved a final rule, with accompanying interpretive guidance (the "2012 Interpretive Guidance"), that describe the manner in which the Council intended to apply the statutory standards and considerations, and the processes and procedures that the Council intended to follow, in making determinations regarding nonbank financial companies under section 113 of the Dodd-Frank Act; and*

*WHEREAS, on February 4, 2015, the Council issued supplemental procedures relating to nonbank financial company determinations (the “Supplemental Procedures”), which supplemented its final rule and the 2012 Interpretive Guidance; and*

*WHEREAS, on June 8, 2015, the Council published staff guidance (the “Stage 1 Guidance”) pursuant to the Supplemental Procedures explaining how certain quantitative thresholds were calculated in Stage 1 of the Council’s process for identifying nonbank financial companies for potential determination under section 113 of the Dodd-Frank Act; and*

*WHEREAS, on March 13, 2019, the Council issued proposed interpretive guidance (the “Proposed Interpretive Guidance”) that would replace the 2012 Interpretive Guidance, the Supplemental Procedures, and the Stage 1 Guidance, and that described the approach the Council proposed to take in (1) prioritizing its work to identify and address potential risks to U.S. financial stability using an activities-based approach and (2) enhancing the analytical rigor and transparency in the processes the Council would follow if it were to consider making a determination under section 113 of the Dodd-Frank Act; and*

*WHEREAS, in response to the public comments received on the Proposed Interpretive Guidance, the staffs of Council members and their agencies have prepared final interpretive guidance (the “Final Interpretive Guidance”); and*

*WHEREAS, the staffs of the Council members and their agencies recommend that the Council approve and publish the Final Interpretive Guidance.*

*NOW, THEREFORE, BE IT RESOLVED, that the Council hereby approves the Final Interpretive Guidance, which supersedes and replaces the 2012 Interpretive Guidance, and authorizes the Chairperson, or his designee, to cause the Final Interpretive Guidance to be published in the Federal Register, in a form and manner acceptable to the Chairperson, or his designee, and to otherwise make it available to the public as the Chairperson, or his designee, deems appropriate.*

*BE IT FURTHER RESOLVED, that the Supplemental Procedures and the Stage 1 Guidance are hereby rescinded.*

*BE IT FURTHER RESOLVED, that the Council hereby delegates authority to the Chairperson, or his designee, to make technical, nonsubstantive, or conforming changes to the text of the Final Interpretive Guidance to ensure that it can be published in the Federal Register, and to take such other actions and issue such other documents incidental and related to the foregoing as the Chairperson, or his designee, deems necessary or appropriate to fulfill the Council’s objectives in connection with its publication.*

The Chairperson asked for a motion to approve the resolution, which was made and seconded. The Council approved the resolution by unanimous vote.

3. Resolution Approving the Minutes of the Meeting Held on November 7, 2019

*BE IT RESOLVED, by the Financial Stability Oversight Council (the "Council"), that the minutes attached hereto of the meeting held on November 7, 2019 of the Council are hereby approved.*

The Chairperson asked for a motion to approve the resolution, which was made and seconded. The Council approved the resolution by unanimous vote.

The Chairperson adjourned the meeting at approximately 4:32 P.M.