Minutes of the Financial Stability Oversight Council

December 17, 2021

PRESENT:

Janet L. Yellen, Secretary of the Treasury and Chairperson of the Financial Stability Oversight Council (Council)
Jerome H. Powell, Chair, Board of Governors of the Federal Reserve System (Federal Reserve)
Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation (FDIC)
Gary Gensler, Chair, Securities and Exchange Commission (SEC)
Rostin Behnam, Acting Chairman, Commodity Futures Trading Commission (CFTC)
Rohit Chopra, Director, Consumer Financial Protection Bureau (CFPB)
Sandra L. Thompson, Acting Director, Federal Housing Finance Agency (FHFA)
Michael J. Hsu, Acting Comptroller of the Currency, Office of the Comptroller of the Currency (OCC)
Todd M. Harper, 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)
Melanie Lubin, Securities Commissioner, Maryland Office of the Attorney General, Securities Division (non-voting member)

GUESTS:

Department of the Treasury (Treasury)
Nellie Liang, Under Secretary for Domestic Finance
Laurie Schaffer, Principal Deputy General Counsel
Sandra Lee, Deputy Assistant Secretary for the Council
Eric Froman, Assistant General Counsel (Banking and Finance)
Sean Hoskins, Acting Director of Policy, Office of the Financial Stability Oversight Council

Board of Governors of the Federal Reserve System
Andreas Lehnert, Director, Division of Financial Stability

Federal Deposit Insurance Corporation
Travis Hill, Deputy to the Chairman for Policy

Securities and Exchange Commission
Amanda Fischer, Senior Counselor

Commodity Futures Trading Commission
David Gillers, Chief of Staff

Consumer Financial Protection Bureau
Ashwin Vasan, Senior Advisor to the Director

Federal Housing Finance Agency
Naa Awaa Tagoe, Acting Deputy Director, Division of Housing Mission and Goals

Comptroller of the Currency
Blake Paulson, Senior Deputy Comptroller for Supervision Risk and Analysis

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
Richard Crump, Vice President, Capital Markets Function

Office of Financial Research
Michael Passante, Chief Counsel

Federal Insurance Office
Philip Goodman, Senior Insurance Regulatory Policy Analyst

Texas Department of Banking
Michael Townsley, Policy Counsel, Conference of State Bank Supervisors

Maine Bureau of Insurance
Ethan Sonnichsen, Managing Director of Government Relations, National Association of Insurance Commissioners

Maryland Office of the Attorney General, Securities Division
Vincent Martinez, General Counsel, North American Securities Administrators Association

PRESENTERS:

SEC Policy Agenda and Proposed Rulemakings

- *Gary Gensler, Chair, SEC*

Crypto-asset Policy Sprint Initiative

- *Molly Mahar, Senior Associate Director, Division of Supervision and Regulation, Federal Reserve*
- *Grovetta Gardineer, Senior Deputy Comptroller for Bank Supervision Policy, OCC*
- *Travis Hill, Senior Advisor to the Chairman, FDIC*

Climate-related Financial Risks

- *Sandra Lee, Deputy Assistant Secretary for the Council, Treasury*

2021 Annual Report

- *Sandra Lee, Deputy Assistant Secretary for the Council, Treasury*
- *Jonathan Rose, Senior Economist, Federal Reserve Bank of Chicago (available for questions)*
- *Alexandra Somers, Senior Policy Advisor, Office of the Financial Stability Oversight Council, Treasury (available for questions)*

Climate-related Financial Risk Committee

- *Sandra Lee, Deputy Assistant Secretary for the Council, Treasury*

LIBOR Transition

- *Michael Gibson, Director, Division of Supervision and Regulation, Federal Reserve*

Executive Session

The Chairperson called the executive session of the meeting of the Council to order at approximately 10:00 A.M. The Council convened by videoconference. The Chairperson outlined the meeting agenda, which had previously been distributed to the members together with other materials. The agenda for the executive session included (1) the SEC's policy agenda and proposed rulemakings, (2) the crypto-asset policy sprint initiative undertaken by the Federal Reserve, FDIC, and OCC, and (3) climate-related financial risks.

1. SEC Policy Agenda and Proposed Rulemakings

The Chairperson turned to the first agenda item, an update on the SEC's policy agenda and proposed rulemakings. She turned to Gary Gensler, Chair of the SEC, for the presentation.

Chair Gensler first described the SEC's three-part mission: to protect investors; maintain fair, orderly and efficient markets; and facilitate capital formation. He provided an overview of upcoming SEC initiatives, including projects focused on market structure, issuers, funds and advisers, and remaining initiatives under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). He then described each area in greater detail.

Chair Gensler first described the SEC's key initiatives with respect to equity markets, including the clearing and settlement cycle, market structure, and digital engagement practices. With respect to Treasury markets, he highlighted the SEC's efforts regarding dealer registration for principal trading firms and member clearing requirements. He also described efforts related to transparency in non-Treasury fixed income markets, and potential rulemakings or projects related to security-based swaps and crypto trading and lending platforms. Chair Gensler then described the SEC's key initiatives related to issuers, including disclosures regarding climate and cybersecurity risks; special purpose acquisition companies; amendments the SEC had recently proposed to the trading safe harbor for executives and issuers under the SEC's Rule 10b5-1; certain China-related issues, including related to auditor inspections; and crypto tokens. Chair

Gensler then described key initiatives related to funds and advisers, including a recently approved proposal for money market fund reforms; proposals related to open-end bond funds and amendments to the SEC's Form PF; the SEC's environmental, social and governance fund name rule; cybersecurity risk; private fund fee disclosures; and certain crypto-related matters. Finally, he said that the SEC would be undertaking several initiatives to adopt rules under the Dodd-Frank Act, including with respect to securities lending, short sale disclosures, and executive compensation. Chair Gensler concluded by noting that the SEC is also working on various other initiatives and expressed interest in collaborating with other Council member agencies.

Council members then had a discussion about upcoming SEC initiatives, expressing support for certain initiatives and for collaboration among Council members and member agencies.

2. Crypto-asset Policy Sprint Initiative

The Chairperson then introduced the next agenda item, a presentation on the crypto-asset policy sprint initiative undertaken by the Federal Reserve, FDIC, and OCC. She introduced Molly Mahar, Senior Associate Director in the Division of Supervision and Regulation at the Federal Reserve, Grovetta Gardineer, Senior Deputy Comptroller for Bank Supervision Policy at the OCC, and Travis Hill, Senior Advisor to the Chairman at the FDIC.

Ms. Gardineer began by stating that the Federal Reserve, FDIC, and OCC had embarked on a series of "policy sprints" during the summer of 2021. She said that the undertaking was based on the technology sprint model, which involves a small group of individuals with diverse expertise working together on an issue for a short period of time. She stated that the purpose of this sprint was to enhance the collective knowledge of the federal banking agencies regarding crypto-asset activities. She said that the agencies undertook three sprints, which were designed to develop a common crypto-asset vocabulary; analyze a range of potential crypto-asset activities conducted by banking organizations and associated risks, and review public comments received in response to the FDIC's May 17, 2021 request for information on digital assets; and identify potential policy gaps and opportunities to provide clarity. She noted that, in connection with their analysis, the agencies also engaged in outreach to stakeholders from each sector.

Ms. Gardineer stated that the agencies focused on the custody of crypto-assets, which underpins other crypto-services banks might offer. She stated that the custody of crypto-assets is different than other asset classes, due to the reliance on a cryptographic key, an alphanumeric password that provides access to associated digital assets. She said that banking organizations providing custody services may also offer related features, such as tax reporting, valuation services, and record-keeping, along with ancillary custodial services.

Mr. Hill then discussed lending practices involving crypto-assets, noting that a small number of banking organizations have begun offering loans secured by crypto-assets. He said that these loans may include requirements to maintain collateral levels above bank-established thresholds. He also noted that lenders may take crypto-assets into custody or use a third-party custodian to secure the collateral.

Mr. Hill also explained that banks are experimenting with blockchain to facilitate payment, clearing, and settlement activities, including for cross-border payments and intraday repurchase agreement transactions. He also noted banks' interest in participating in stablecoin arrangements.

Ms. Mahar then addressed how banking organizations are facilitating the trading of crypto-assets. She noted that some banking organizations are seeking to offer customers the ability to buy, hold, and sell crypto-assets, typically through a third party, in response to demand from retail and institutional customers. She noted that some banking organizations are also offering their customers indirect exposure through derivatives and investment funds. She noted that staff are assessing these activities, and banking organizations' related controls, to identify any gaps.

Ms. Mahar then described next steps for the agencies on this topic. She noted that the agencies issued an interagency statement on November 23, 2021 that described initiatives in their 2022 workplan, including providing greater clarity on permissibility, and developing interagency supervisory expectations on crypto-asset custody activities, loans collateralized by crypto-assets, and the facilitation of crypto-asset trading. She also noted that the agencies would develop a regulatory and supervisory framework for banking organizations' participation in stablecoin arrangements.

Council members then asked questions and had a discussion about the crypto-asset policy sprint initiative, including the letter issued by the NCUA on December 16, 2021 addressing the authority of federally insured credit unions with respect to certain digital asset services, the use of private keys in connection with crypto-asset technology, and the treatment of crypto-asset holdings in the loan underwriting process.

3. Climate-related Financial Risks

The Chairperson next introduced the next agenda item, the update on climate-related financial risks. She introduced Sandra Lee, Deputy Assistant Secretary for the Council at Treasury.

Ms. Lee noted that the Council issued a report on climate-related financial risk on October 21, 2021. Ms. Lee said that the climate report stated that the Council would establish a Climate-related Financial Risk Committee (CFRC) within 60 days. She noted that the Council would vote at this meeting on creating the new staff-level committee. She said that the proposed committee charter would establish the CFRC and formalize its purposes, duties, and operating structure. She stated that, as outlined in the climate report, the CFRC would play a central role in interagency collaboration, to identify, assess and mitigate climate-related risks to the financial system.

Ms. Lee stated that in the preceding weeks, Council member agency staff had held discussions regarding the actions that Council member agencies plan to undertake related to the report's recommendations, and how the Council can most effectively facilitate interagency coordination. She noted that some member agencies were engaging in outreach, others were developing internal workstreams, and others were assessing their data and analytical needs. She noted that member agencies would work together to focus on key themes that emerged from the bilateral meetings, which included data access and availability, data infrastructure, and information sharing and coordination.

Ms. Lee stated that if the CFRC charter was adopted at this meeting, staff would develop a proposed CFRC workplan. She also noted that, as stated in the report, the CFRC would provide at least semi-annual updates to the Council on the status of efforts by the Council and its member agencies to identify and address climate-related financial risks.

Council members then had a discussion about the CFRC and the efforts of Council member agencies regarding climate-related risks.

The Chairperson adjourned the executive session of the meeting at approximately 10:55 A.M.

Open Session

The Chairperson called the open session of the meeting of the Council to order at approximately 11:01 A.M.

The Chairperson outlined the agenda for the open session, which included (1) a presentation and vote on the Council's 2021 annual report, (2) a vote on the charter of the Council's Climate-related Financial Risk Committee, (3) an update on the LIBOR transition, and (4) a vote on the minutes of the Council's meeting on November 15, 2021.

1. 2021 Annual Report

The Chairperson turned to the first agenda item, a vote on the Council's 2021 annual report. She stated that the report analyzed recent episodes of financial turmoil to understand weak points in the financial system and identified potential threats. She noted that it reviewed actions taken by the Council to strengthen the financial system and recommended additional steps that could be taken by the public and private sectors. She stated that the report marked nearly two years since the first appearance of COVID-19 and the resulting financial turmoil in March 2020. She noted that as the economy began to shut down that month, many investors sought safety in the form of cash and short-term government securities. She also noted that corporate and municipal bond markets became illiquid. She stated that increased capital and liquidity helped banks weather the crisis. She said that the episode showed that the financial system was more shock-resistant than it was in 2008. She said that the annual report demonstrated that the lessons of 2008 and 2020 strongly inform the Council's work. She stated that she would review three key priorities for the Council that she outlined in March 2021 in her first meeting as Chairperson of the Council.

The Chairperson said the first priority was nonbank financial intermediation, including money market funds, open-end mutual funds, and hedge funds. She noted that the events of March 2020 demonstrated that open-end mutual funds and prime money market funds could amplify liquidation pressures because of liquidity risks in their business models and the incentives they give to investors. She said the same held true for hedge funds, because of their use of leverage. She noted that the annual report reviewed the Council's progress on work related to these three sectors. She said that in June 2021, the Council issued a statement regarding the structural vulnerabilities of money market funds. She noted that the statement called for reforms to improve the resilience and functioning of short-term funding markets. She stated that the Council expressed support for the SEC's engagement on this issue. She noted her support for the SEC's vote on December 15, 2021 to propose amendments to certain rules that govern money market funds, and said the Council would continue to monitor this effort. She stated that, in addition, the Council's working groups on open-end funds and on hedge funds were assessing the risks posed by these types of funds and would evaluate whether actions were necessary to address their vulnerabilities.

The Chairperson said the second priority was the resilience of the U.S. Treasury market. She noted that the Treasury market is the deepest and most liquid market in the world. She said that it was important to understand the disruptions that had occurred in that market because of its critical importance to the financial system. She noted that the annual report reviewed the progress of the Inter-Agency Working Group on Treasury Market Surveillance, which had worked with the Council to study the events of March 2020 and potential links between these events and other recent episodes. She said that the interagency working group was analyzing ways to improve the resilience of the Treasury market. She said that the working group was analyzing potential policies to improve data quality and availability, bolster the resilience of market intermediation, evaluate expanded central clearing, and enhance trading venue transparency and oversight.

The Chairperson stated that the annual report also discussed the Council's work regarding climate-related financial risks, which was the third priority she spoke of in March. She said that the Council must look forward, based on its responsibility under the Dodd-Frank Act, which gave the Council the duty to respond to emerging threats to the stability of the U.S. financial system. She stated that with this purpose in mind, the Council issued a report on climate-related financial risk in October, which made recommendations to promote the resilience of the financial system. She said that these steps included expanding capacity, improving data and measurement tools, enhancing disclosure of climate-related risk, assessing the scale of potential vulnerabilities, and adjusting regulatory and supervisory tools. She said that to help coordinate the Council's efforts on these issues, the climate report called for the Council to establish a new staff-level committee, the Climate-related Financial Risk Committee. She noted that the Council would vote on establishing the committee later in the meeting.

The Chairperson stated that climate was not the only emerging risk. She said that, as the annual report detailed, risks to U.S. financial stability were elevated compared to before the pandemic, even as the financial vulnerabilities of banks and central counterparties were low. She noted that, for instance, the report discussed potential shocks related to the elevated level of uncertainty characterizing the global growth outlook. She said the report also discussed vulnerabilities related to elevated asset prices.

The Chairperson stated that the report highlighted the critical importance of regulatory attention and coordination regarding stablecoins and other crypto assets, as the market for these assets continues to rapidly grow and evolve. She said that cybersecurity also remained a high priority, as did the LIBOR transition. She concluded her remarks by stating that she anticipated engaging with the Council in 2022 on these issues and others discussed in the annual report.

The Chairperson then introduced Sandra Lee, Deputy Assistant Secretary for the Council, to provide an overview of the report's findings and recommendations. She noted that Jonathan Rose, Senior Economist at the Federal Reserve Bank of Chicago, and Alexandra Somers, Senior Policy Advisor in the Office of the Financial Stability Oversight Council at Treasury, were available for questions.

Ms. Lee stated that this year's annual report was once again the product of extensive collaboration among all of the Council members and member agencies. She said the report brought together a number of interagency workstreams, including on climate-related financial risk, Treasury market resilience, nonbank financial institutions, and stablecoins. She noted that each of these workstreams involved extensive collaboration.

Ms. Lee said that in the annual report, the Council reports to Congress each year on certain subjects, including the activities of the Council, significant financial market and regulatory developments, and potential emerging threats to U.S. financial stability. She noted that the Council also makes recommendations in the report to enhance U.S. financial markets, promote market discipline, and maintain investor confidence.

Ms. Lee noted that this year's report was completed a year and a half after the onset of the COVID-19 pandemic. She said that the report noted that the U.S. economy had continued to rebound from disruptions related to the pandemic. She said the recovery had been supported by monetary and fiscal policy, substantial progress in vaccinations, and broadly accommodative financing conditions. She said the report also analyzed certain key economic developments that accompanied this recovery, including the growth of asset valuation pressures in residential housing and in other markets, as well as supply chain challenges and tightness in labor markets. She then highlighted some of the potential emerging threats and related recommendations in the report.

The first topic Ms. Lee highlighted was climate change. She said that this was the Council's first annual report that identified climate change as an emerging threat to U.S. financial stability. She said the report detailed the Council's work leading up to the publication of the Council's report on climate-related financial risk in October 2021. She stated that the annual report noted the importance of taking prompt action to improve the availability of data and measurement tools, enhance assessments of climate-related financial risks and vulnerabilities, and incorporate climate-related risks into risk-management practices and supervisory expectations for regulated entities. She said that the report also recommended that financial regulators should promote consistent, comparable and decision-useful disclosures that allow investors and financial institutions to take climate-related financial risks into account in their investment and lending decisions.

The second topic Ms. Lee addressed was the transition from LIBOR. She said that after years of planning and preparation, the transition away from LIBOR was entering a critical stage. She noted that the report discussed certain risks related to this transition: the selection of new reference rates, the possibility of continued issuance of instruments that create or extend LIBOR exposure, and legacy contracts without robust fallback provisions in the event of LIBOR cessation. She stated that the report emphasized that market participants should act with urgency to address their existing LIBOR exposures and transition to robust and sustainable alternative rates.

The third topic Ms. Lee highlighted was digital assets. She said the report detailed several risks related to digital assets, including high price volatility due to speculative activity; the possibility of operational failures, fraud, and market manipulation; risks stemming from direct or indirect connections with banking services, financial markets, and financial intermediaries; illicit financing; national security; cybersecurity; privacy; and international monetary and payment systems integrity. She noted that the report analyzed stablecoins in detail, and summarized the report on stablecoins published in November 2021 by the President's Working Group on Financial Markets (PWG), the FDIC and the OCC. She said the annual report recommended that federal and state regulators continue to examine risks to the financial system posed by new and emerging uses of digital assets and coordinate to address potential risks that arise from those digital assets. She stated that the annual report noted that the Council would further assess and monitor the potential risks of stablecoins and recommended that its members consider appropriate action to address those risks, while continuing to coordinate and collaborate on issues of common concern. She said the report noted that the Council would also be prepared to consider steps available to it to address risks outlined in the PWG report in the event comprehensive legislation is not enacted.

The fourth issue Ms. Lee highlighted was cybersecurity risk. She stated that the report noted that the financial sector, like other critical sectors, is vulnerable to a cybersecurity incident. She said that the report also noted that the implementation of teleworking strategies could increase cybersecurity vulnerabilities. She said the report contained a number of recommendations, including that federal and state agencies continue to monitor cybersecurity risks and conduct cybersecurity examinations of financial institutions and financial infrastructure to ensure, among other things, robust and comprehensive cybersecurity monitoring, especially in light of new risks posed by the pandemic, ransomware incidents, and supply-chain attacks.

The fifth and final issue Ms. Lee highlighted was the global growth outlook. She stated that the report noted that this outlook was characterized by elevated uncertainty, with the potential for continued volatility and unevenness of growth across countries and sectors. She said that risks included the possibility of higher-than-expected inflation; the possibility that financial vulnerabilities in China could lead to a hard landing; and the possibility that the pandemic could continue to cause volatility in economic activity. She stated that the report recommended that member agencies seek to ensure that the financial institutions they oversee are attentive to the risks posed by uneven or volatile global growth. She said that, in conclusion, the annual report provided an overview of the Council's identification of potential risks or vulnerabilities on these five subjects and other areas. She noted that the report highlighted key actions taken and made recommendations for addressing these risks.

Following Ms. Lee's remarks, the Chairperson called on other Council members to comment on the annual report.

Jerome Powell, Chair of the Federal Reserve, noted that each year the Council collaborated to identify emerging threats to U.S. financial stability and make recommendations to address them. He expressed his support for this year's annual report, and said that it built on a detailed review of risks by describing progress in the three priority areas identified by the Chairperson. He said that in each area, the annual report documented progress made in assessing the issue and in identifying steps that the Council and its member agencies could take to reduce systemic risks. Chair Powell concluded by stating that 2021 had been another year of unique challenges, but also of notable productivity and focus, and said that the annual report reflected the cooperation and coordination of the Council member agencies.

Jelena McWilliams, Chairman of the FDIC, stated that following significant economic turmoil in 2020, the banking system remained resilient. She said that in contrast to the financial crisis of 2008, only three banks had failed since the start of the pandemic in March 2020, and none had failed due to the pandemic or the ensuing economic stress. She noted that, at the same time, banks across the country had accommodated significant growth in deposits. Chairman McWilliams said that in 2021, the banking sector remained a source of strength for the economy, reinforced by banks' strong capital positions. She noted that banks remained strongly capitalized in the third quarter of 2021, holding a higher amount and quality of capital than just prior to the financial crisis. She stated that while these were signs to be cautiously optimistic, the FDIC would nonetheless continue to monitor economic trends, deposit trends, and other factors that affect the health of the banking sector. She said that in particular, the FDIC remained vigilant about the potential effects of inflation on banks and their customers, the potential economic impact of the Omicron variant, and the evolution of certain markets post-pandemic, including commercial real estate.

Gary Gensler, Chair of the SEC, expressed his support for the report and stated that he had asked SEC staff to address a number of the points raised in the report and make recommendations to the SEC for proposals on several projects. He noted that the SEC's vote on December 15, 2021 proposing amendments to rules that govern money market funds was one example. He said that the annual report reflected new insights that the SEC had developed regarding money market funds and open-end bond funds. He stated that the SEC would incorporate economic analysis and public feedback when examining Treasury market resiliency, stock market resiliency, and other projects to shorten settlement cycles, in addition to interagency work on crypto-assets. He said that while the crypto-asset class was not the largest asset class, it was largely operating outside of the remit of the banking and market regulators. Chair Gensler said that Council member agencies should continue to evaluate how to address potential growing instability in crypto markets within the agencies' jurisdictions and authorities. He stated that the SEC was also working on consistent, comparable and decision-useful climate risk disclosures. Finally, he stressed the importance of the LIBOR transition. He expressed his concern that some parts of the market might rely on a replacement rate for LIBOR that could prove inadequate in the event of market stress. He stated that the Bloomberg Short-Term Bank Yield Index (BSBY) rate had infirmities and would not stand the test of time or be conducive to financial stability.

Rostin Behnam, Acting Chairman of the CFTC, expressed his support for the report. He stated that derivatives markets continued to experience substantial volatility and, at times, turbulence driven by a multitude of factors. He said that weather impacts, supply-side constraints, and fluctuating demand levels in the past few years had moved markets in unprecedented ways. After briefly summarizing the CFTC's jurisdiction, he noted that overall risk levels remained elevated and continued to receive monitoring and attention by the CFTC. He welcomed the focus in the annual report on the LIBOR transition, climate-related financial risks, and stablecoins, areas which he indicated would continue to be focuses for the CFTC.

Rohit Chopra, Director of the CFPB, expressed his support for the report, and stated that its release provided an opportunity for the CFPB to look ahead and chart its priorities for 2022. He said that the CFPB and other Council member agencies were evaluating the consumer protection implications of the entry of large technology platforms into financial services. He stated that these companies understand that surveillance of transaction activity can be used to monetize their broader business model, and he noted that this trend raised questions and concerns about consumers and data and also about the separation of banking and commerce. He said that given their large user bases, network effects, and access to troves of data, these firms could rapidly scale their financial services activities, potentially posing underappreciated risks to financial stability. Director Chopra stated that these firms could become dominant financial services providers almost overnight, and he recommended that Council member agencies assess the implications of this potential development. He said that his immediate concern was the financial system's increased reliance on three cloud services providers. Director Chopra stated that operational disruptions at these providers could paralyze communications in web platforms. He said that if operational issues were to impact the core services that banks and other institutions provide, it could undermine confidence in the financial system. He noted that the risks posed by concentration in cloud services have implications for nearly every sector of the economy. He stated that, as noted in the annual report, the Council supported the efforts of the Financial and Banking Information Infrastructure Committee (FBIIC) Technology Working Group on this topic. He said that it was worthwhile to evaluate risks specific to financial markets and U.S. financial stability to determine whether any of the Council's tools should be deployed to mitigate them.

Sandra Thompson, Acting Director of the FHFA, stated that the annual report's identification of climate-related financial risk as an emerging threat to U.S. financial stability was important to implementing the Council's recommendations in its climate report. She said that the FHFA was committed to improving public awareness of climate risks, particularly those related to the housing sector, and would work with other Council member agencies on this issue. Acting Director Thompson also welcomed the discussion in the annual report on the efforts by FHFA and its regulated entities to provide relief to borrowers and renters affected by the pandemic, as well as FHFA's efforts to expand affordable and sustainable housing. She said that improving housing affordability in a sustainable manner remained a key priority for FHFA. She also welcomed the recommendation in the annual report that FHFA and the NCUA be granted examination and enforcement authority to oversee third-party service providers. She stated that there was a continued discrepancy in authority among financial regulators in this area that should be addressed. She said that examination and enforcement authority over third-party service providers was an important tool to help FHFA ensure the safety and soundness of FHFA's regulated entities.

Todd Harper, Chairman of the NCUA, expressed his support for the report, including the Council's recommendation to Congress that the NCUA have examination and enforcement authority over third-party service providers. He stated that this authority was especially needed now. He said that in October 2021, the NCUA board, without his support, had adopted a final rule to expand the permissible activities and services of credit union service organizations. He noted that while he voted against this rule, it had been issued by the NCUA. He expressed concern that the credit union system would be vulnerable to new risks. He said that this issue presented a regulatory blind spot that had widened and should be addressed.

Thomas Workman, the Council's independent member with insurance expertise, expressed his support for the report's statement encouraging pension regulators and the Financial Accounting Standards Board to improve the quality, timeliness, and depth of disclosures of pension financial statements and portfolio holdings.

Dino Falaschetti, Director of the OFR, stated that OFR was supporting several efforts outlined in the report, including recommendations related to climate-related financial risk, short-term wholesale funding, and central counterparties. He said that the OFR would continue to monitor, analyze and share information with other Council member agencies.

Melanie Lubin, Securities Commissioner in the Office of the Attorney General of Maryland, Securities Division, stated that the pandemic had presented novel issues in retail markets, consumer finance, and asset valuation. She stated that the work of the Council and its member agencies had helped to protect investors and maintain orderly and efficient markets. She expressed her intent to continue working collaboratively on the issues highlighted in the report, including climate-related risks, digital assets, and cybersecurity concerns.

The Chairperson then presented to the Council the following resolution approving the Council's 2021 annual report:

WHEREAS, the Financial Stability Oversight Council (Council) under section 112 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (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 to (a) enhance the integrity, efficiency, competitiveness, and stability of U.S. financial markets; (b) promote market discipline; and (c) maintain investor confidence; and

WHEREAS, the staffs of the Council members and their agencies prepared the attached 2021 annual report of the Council (2021 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 2021 Annual Report and authorizes the Chairperson, or her designee, to take such action as they may deem necessary or appropriate to transmit the 2021 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 her designee, to make technical, nonsubstantive, or conforming changes to the text of the 2021 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. Climate-related Financial Risk Committee

The Chairperson turned to the next agenda item, the establishment of the Climate-related Financial Risk Committee (CFRC). She introduced Sandra Lee, Deputy Assistant Secretary for the Council at Treasury, to provide an overview of the proposed committee.

Ms. Lee stated that the Council's report on climate-related financial risk, which the Council published in October, stated that the Council would establish the CFRC within 60 days. She said that the proposed committee charter would establish the CFRC and formalize its purposes, duties, and operating structure. She stated that the CFRC would play a central role in interagency collaboration, to identify, assess and mitigate climate-related risks to the financial system. She said that through this committee, staff from across the Council members and member agencies would meet and share information, as they work to implement the recommendations in the Council's climate report.

Ms. Lee stated that the proposed structure of the CFRC was similar to the charters of the other five Council staff-level committees that the Council adopted in 2015. She said that, based on the Council's experience with those existing committees, the Council would expect the CFRC to leverage each Council member agency's expertise, and promote shared responsibilities among the member agencies. She noted that the proposed committee charter set forth the duties of the CFRC, based on the needs identified in the Council climate report. She said that these duties included identifying priority areas for assessing and mitigating climate-related risks to the financial system, facilitating information sharing in coordination among staff of Council members and member agencies relating to climate-related risks to the financial system, coordinating efforts among Council members and member agencies to address data gaps and to develop data standards regarding climate-related risks to the financial system, and providing updates to the Council at least semiannually on the status of efforts by staff of Council members and member agencies to identify and address climate-related financial risks.

She stated that the CFRC would also be responsible for overseeing the Council's climate-related financial risk advisory committee, which staff were currently working to establish. She said that this advisory committee would provide the Council with input on climate-related financial risks from a broad array of stakeholders. She concluded by stating that staff recommended that the

Council vote to establish the CFRC and adopt the proposed charter, which would then be posted on the Council's website.

The Chairperson then noted that when the Council issued the report on climate-related financial risk in October 2021, she stated that the report was a first step, not the Council's final word. She noted that the vote on the proposed CFRC charter represented another step forward, and the CFRC would help Council member agencies collaborate on the recommendations they agreed to in the Council's climate report. She stated that addressing climate-related financial risks was an urgent priority that would require collective effort.

The Chairperson called on other Council members to comment on the CFRC.

Michael Hsu, Acting Comptroller of the Currency, stated that he supported the Council's vote to create the CFRC. He said that the CFRC would play an important role in identifying priority areas for assessing and mitigating climate-related risks to the financial system, coordinating information sharing, aiding in the development of common approaches and standards, and facilitating communications across Council members and interested parties. He stated that addressing climate-related risks to the financial system required the collaboration of multiple parties and partnerships, using many strategies and mechanisms. He also noted that, consistent with the OCC's safety and soundness mandate and the recommendations of the Council in the climate report, the OCC issued for public feedback draft principles for climate-related financial risk management for large banks on December 16, 2021. He said the OCC was hopeful that the principles would promote and accelerate improvements in banks' climate risk management practices.

Chair Powell stated that the Federal Reserve looked forward to reviewing comments on the draft principles the OCC released on December 16, as banking regulators continued to formulate an interagency set of supervisory expectations for the management of climate-related financial risks, with a focus on large banks. He said that a consistent approach across bank regulatory agencies would best support the effective management of these risks. He stated that the CFRC would help all of the financial regulatory agencies share information and findings on climate-related financial risk. He stated that the Federal Reserve was committed to ensuring that these supervised firms have strong risk management capabilities to promote their resilience to all risks, including climate-related financial risks.

The Chairperson then presented to the Council the following resolution adopting the CFRC charter:

WHEREAS, section 111(e)(2) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) provides that the Financial Stability Oversight Council (Council) shall adopt such rules as may be necessary for the conduct of the business of the Council; and

WHEREAS, on October 21, 2021, the Council approved a Report on Climate-related Financial Risk (Climate Report), which stated that the Council would form a Climate-related Financial Risk Committee (CFRC) within 60 days of the publication of the report; and

WHEREAS, the staffs of the Council members and their agencies have prepared the attached charter for the CFRC (CFRC Charter); and

WHEREAS, the staffs of the Council members and their agencies recommend that the Council approve and adopt the CFRC Charter.

NOW, THEREFORE, BE IT RESOLVED, that the Council hereby approves and adopts the CFRC Charter; and

BE IT FURTHER RESOLVED, that the Council hereby authorizes the CFRC Charter to be published on the Council's website, in a form and manner acceptable to the Chairperson or her designee; and

BE IT FURTHER RESOLVED, that the Council hereby delegates authority to the Chairperson, or her designee, to make technical, nonsubstantive, or conforming changes to the text of the CFRC Charter, and to take such other actions as they may deem 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. LIBOR Transition

The Chairperson then turned to the next agenda item, an update on the LIBOR transition. She introduced Michael Gibson, Director of the Division of Supervision and Regulation at the Federal Reserve.

Mr. Gibson stated that as a result of collective efforts on the LIBOR transition, a nearly decade-long effort involving market participants and regulators from around the world, U.S. and global financial markets were now stronger and more resilient. He said that trillions of dollars in financial contracts now rested upon reference rates that were transparent, well-designed, well-managed and grounded in market transactions. He said that the efforts of the Alternative Reference Rates Committee (ARRC), the private-sector group leading the transition in the United States, had largely addressed the key risks presented by LIBOR: that it was based on fragile and thinly traded markets, was subject to manipulation, and often relied on judgments rather than market transactions.

Mr. Gibson stated that the ARRC recommended the Secured Overnight Financing Rate (SOFR) as its preferred rate, because it is transparent and resilient, resting on one of the deepest and most liquid markets in the world. He said that the Federal Reserve, along with its fellow supervisors, had told banks that entering new LIBOR contracts after December 31, 2021 would create safety and soundness risks and that the Federal Reserve would supervise firms accordingly. He said that with this date approaching in two weeks, the Federal Reserve was encouraged by the progress it had seen in markets.

He stated that open interest in linear swaps referencing SOFR had increased sevenfold from just under $1 trillion in September 2020 to over $7 trillion in November 2021. He said that cross-currency swaps between the U.S. dollar and other major currencies had almost completely transitioned to SOFR and other risk-free reference rates. He noted that 90 percent of recent floating-rate note issuance had been linked to SOFR and all newly issued floating-rate agency mortgage-backed securities were based on SOFR. He said that while the loan market had been slow to transition to alternative rates, firms were reporting that a majority of new business loans in the fourth quarter 2021 had been utilizing alternative rates, primarily SOFR.

Mr. Gibson said that over the next year, the Federal Reserve would be expecting a decline in outstanding LIBOR exposures, as firms stop entering into new LIBOR contracts and existing LIBOR contracts mature. He said that although the Federal Reserve's supervisory guidance directly impacts banking organizations, other market participants should also prepare for the end of LIBOR. He stated that liquidity in U.S. dollar LIBOR instruments would likely fall during 2022. He said that all market participants should transition soon to alternative reference rates.

Mr. Gibson then turned to transition planning for existing, or so-called "legacy," LIBOR contracts. He said that there were currently more than $200 trillion of legacy LIBOR contracts. He noted that to assist with the transition of these contracts, U.S. dollar LIBOR would be available in most tenors through June 2023. He said that the ARRC estimated that this would allow approximately two-thirds of legacy contracts to mature according to their original terms. He said that some legacy LIBOR contracts nevertheless would mature after June 2023. He noted that many of these contracts would fall back to alternative reference rates, but some contracts did not include workable fallback language. He said that while a small number of states had enacted legislation to allow the "tough legacy" contracts governed by these states' laws to transition to SOFR-based rates, federal legislation would establish a clear and uniform solution on a nationwide basis. He stated, in conclusion, that the transition away from LIBOR was advanced and accelerating, and that the financial system would be more stable as a result.

The Chairperson stated that since the Council last discussed this topic, the market had made considerable progress in the transition away from LIBOR. She said that the share of new issuance and secondary market activity tied to LIBOR continued to decline. She noted that the pace of transition to more durable rates, like SOFR, had accelerated in the past few months. She said that the CFTC-sponsored "SOFR First" initiative had been helpful at driving the transition in interdealer markets. She also noted that the ARRC's formal recommendation of a term SOFR rate had helped contribute to a recent uptake in SOFR for business loans. She said that despite this progress, more work remained to be done. She said that with only two weeks remaining before two year-end LIBOR deadlines, it was important that market participants continue to prepare for the cessation of several LIBOR currency-tenor pairs, and also ensure that they are ready to meet supervisors' expectations regarding new LIBOR exposures. She said that more progress was also needed on the transition to more durable exchange-traded derivatives. Finally, she stated that she had encouraged Congress to adopt legislation to facilitate a smooth transition from LIBOR and eliminate potential uncertainty.

The Chairperson then called on other Council members to comment on the LIBOR transition.

Chair Powell noted that supervisory guidance stated that LIBOR would not be available after December 31, 2021. He stated that the transition was a complex and ongoing process that had been underway for more than a decade, and was making progress. He said that the Federal Reserve welcomed supporting legislation to help facilitate the smooth transition from LIBOR.

Chairman McWilliams stated that the FDIC remained focused on the LIBOR transition. She said that FDIC-supervised institutions continued to move in the right direction to address the LIBOR transition and adopt a replacement rate by December 31. She said that banks were also addressing the challenges of legacy contracts and making adequate preparations for LIBOR's discontinuation. She stated that the FDIC had not noted significant outliers among FDIC-supervised institutions. Chairman McWilliams stated that the FDIC had found that many FDIC-supervised institutions, particularly smaller community banks, did not have material LIBOR exposures. She said that institutions that did have such exposures generally had made concerted efforts to transition away from LIBOR and were on track to issue new contracts in another reference rate by year-end. She stated that for several years, the FDIC had conducted industry outreach on the LIBOR transition to encourage the identification of exposures, timely implementation of a replacement rate, and amendments to legacy contracts. She said that the FDIC also participated in the issuance of several interagency statements emphasizing supervisory expectations, most recently in October 2021. Chairman McWilliams stated that the FDIC would continue to monitor the LIBOR transition during safety and soundness examinations in 2022 to ensure that a replacement rate had been implemented for new contracts and that legacy contracts were being appropriately addressed.

Acting Chairman Behnam stated that the CFTC had worked closely with the ARRC and the Federal Reserve Bank of New York on the LIBOR transition. He said that the most critical step in the transition involved exchange-traded derivatives, principally the Eurodollar contract, which moves based on LIBOR. He said that the CFTC had established a guide for this final phase. He stated that the main message of the guide was that all market participants should ensure operational capability to transact in SOFR exchange-traded derivatives as soon as possible. He said that all market participants were also encouraged to adopt the best practice of replacing the use of LIBOR with SOFR in new contracts, including exchange-traded derivatives, after year-end 2021. He stated that bank and nonbank market participants alike should promptly transition away from LIBOR. He noted that the transition of exchange-traded contracts would be the last but most significant step in the LIBOR transition.

Chairman Harper stated that through the Federal Financial Institutions Examination Council, the NCUA had maintained clear, coordinated and consistent messaging to its regulated entities. He stated that the NCUA would continue to ensure that its regulated entities make use of new and appropriate reference rates that are both transparent and reliable. He noted that the NCUA also sought to ensure that new contracts have robust fallback language. He concluded by expressing his support for the ongoing LIBOR transition.

Chair Gensler stated that he supported changes to the Trust Indenture Act, which the SEC administers, to help facilitate the LIBOR transition. He expressed his support for the transition to SOFR and stated his opposition to transitioning to rates that he said are frail and rely on commercial paper and certificates of deposit, such as BSBY. He said that he did not believe that

BSBY was compliant with the principles laid out in the Principles for Financial Benchmarks published in 2013 by the International Organization of Securities Commissions.

Director Chopra stated that he wanted to provide comments about consumer loans. He noted that on December 7, 2021, the CFPB finalized a rule facilitating the transition away from LIBOR for consumer financial products. He said that the rule established requirements for how creditors should select replacement indices for existing LIBOR-linked consumer loans after April 2022. He said that no new financial contracts may reference LIBOR as the relevant index after the end of 2021. He said that starting in June 2023, LIBOR could no longer be used for existing financial contracts in consumer loans. He noted that approximately $1.4 trillion in consumer loans are tied to LIBOR. He said that in most circumstances, lenders can replace the LIBOR index with new indices based on SOFR or the prime rate. He expressed his support for this approach and stated that it would be less vulnerable to the problems underlying the use of LIBOR.

4. Resolution Approving the Minutes of the Meeting Held on November 15, 2021

BE IT RESOLVED, by the Financial Stability Oversight Council (the Council), that the minutes attached hereto of the meeting held on November 15, 2021 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 11:55 A.M.