

**Minutes of the Financial Stability Oversight Council**

July 28, 2023

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)

Martin Gruenberg, Chairman, Federal Deposit Insurance Corporation (FDIC)

Gary Gensler, Chair, Securities and Exchange Commission (SEC)

Rostin Behnam, Chairman, Commodity Futures Trading Commission (CFTC)

Rohit Chopra, Director, Consumer Financial Protection Bureau (CFPB)

Sandra L. Thompson, 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) (via videoconference)

Thomas E. Workman, Independent Member with Insurance Expertise

James Martin, Acting Director, Office of Financial Research (OFR), Department of the Treasury (non-voting member) (via videoconference)

Steven Seitz, Director, Federal Insurance Office (FIO), Department of the Treasury (non-voting member)

Adrienne Harris, Superintendent, New York State Department of Financial Services (non-voting member) (via videoconference)

Elizabeth K. Dwyer, Superintendent of Financial Services, Rhode Island Department of Business Regulation (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

Sandra Lee, Deputy Assistant Secretary for the Council

Laurie Schaffer, Principal Deputy General Counsel

Eric Froman, Assistant General Counsel (Banking and Finance)

Sean Hoskins, Director of Policy, Office of the Financial Stability Oversight Council

Nicholas Steele, Director of Analysis, Office of the Financial Stability Oversight Council

Board of Governors of the Federal Reserve System

Michael Barr, Vice Chair for Supervision (via videoconference)

Nami Mukasa, Associate Director and Chief of Staff, Division of Financial Stability

Federal Deposit Insurance Corporation

Susan Baker, Corporate Expert, Systemic Risk

Securities and Exchange Commission

Corey Frayer, Senior Advisor

Commodity Futures Trading Commission

David Gillers, Chief of Staff

Consumer Financial Protection Bureau

Gregg Gelzinis, Advisor to the Director

Federal Housing Finance Agency

George Sacco, Senior Analyst, Division of Housing Mission and Goals

Comptroller of the Currency

Jay Gallagher, Senior Deputy Comptroller for Supervision Risk and Analysis

National Credit Union Administration

Andrew Leventis, Chief Economist (via videoconference)

Office of the Independent Member with Insurance Expertise

Charles Klingman, Senior Policy Advisor

Federal Reserve Bank of New York

John Williams, President

Richard Crump, Financial Research Advisor, Macrofinance Studies (via videoconference)

Office of Financial Research

Michael Passante, Chief Counsel

Federal Insurance Office

Philip Goodman, Senior Insurance Regulatory Policy Analyst

New York State Department of Financial Services

Karen Lawson, Executive Vice President for Policy and Supervision, Conference of State Bank Supervisors (via videoconference)

Rhode Island Department of Business Regulation

Ethan Sonnichsen, Managing Director, National Association of Insurance Commissioners (NAIC)

Maryland Office of the Attorney General, Securities Division

Dylan White, Associate General Counsel, North American Securities Administrators Association

PRESENTERS:

*Nonbank Mortgage Servicing Task Force*

- *Anna Watson-Mwangi, Senior Financial Analyst, FHFA*

- *Greg Keith, Senior Vice President and Chief Risk Officer, Ginnie Mae*
- *Sandra Lee, Deputy Assistant Secretary for the Council, Treasury*
- *Alanna McCargo, President, Ginnie Mae (available for questions) (via videoconference)*
- *Sam Valverde, Executive Vice President and Chief Operating Officer, Ginnie Mae (available for questions) (via videoconference)*
- *Kevin Silva, Associate Director, Enterprise Counterparty Financial Standards, FHFA (available for questions) (via videoconference)*
- *Michael Opsahl, Principal Analyst, FHFA (available for questions)*
- *Karen Pence, Deputy Associate Director, Division of Research and Statistics, Federal Reserve (available for questions)*

*Climate-related Financial Risk Committee Update (Executive Session)*

- *Sini Matikainen, Senior Policy Advisor, Office of the Financial Stability Oversight Council, Treasury*
- *Terri Barger, Acting Technical Expert for Commercial Credit Policy, OCC*
- *Yue (Nina) Chen, Chief Climate Risk Officer, OCC (available for questions)*
- *Daren Purnell, Associate Director for Data Products, OFR (available for questions) (via videoconference)*

*Developments in the Banking Sector*

- *Michael Barr, Vice Chair for Supervision, Federal Reserve (via videoconference)*
- *Lisa Ryu, Senior Associate Director, Division of Supervision and Regulation, Federal Reserve*
- *Doriana Ruffino, Manager, Division of Supervision and Regulation, Federal Reserve*

*Climate-related Financial Risk Committee Update (Open Session)*

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

*LIBOR Update*

- *Michael Barr, Vice Chair for Supervision, Federal Reserve (via videoconference)*
- *David Bowman, Senior Associate Director, Division of Monetary Affairs, Federal Reserve*

**Executive Session**

The Chairperson called the executive session of the meeting of the Council to order at approximately 9:58 A.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 included (1) an update on the work of the Council’s Nonbank Mortgage Servicing Task Force, (2) an update on the work of the Council’s Climate-related Financial Risk Committee, and (3) an update on developments in the banking sector.

## 1. Nonbank Mortgage Servicing Task Force

The Chairperson introduced the first agenda item, an update on the work of the Council's Nonbank Mortgage Servicing Task Force. She noted that in the April 2023 Council meeting, staff had presented to the Council on risks in the nonbank mortgage servicing sector. She welcomed representatives of Ginnie Mae participating in the meeting, including Alanna McCargo, President of Ginnie Mae. She then introduced Anna Watson-Mwangi, Senior Financial Analyst at the FHFA; Greg Keith, Senior Vice President and Chief Risk Officer at Ginnie Mae; and Sandra Lee, Deputy Assistant Secretary for the Council at Treasury.

Ms. Watson-Mwangi began by highlighting certain points from the presentation at the Council's April 2023 meeting on challenges related to nonbank mortgage servicing. She noted that an increase in mortgage interest rates and a decrease in refinancings had strained the nonbank business model. She also noted that there had been structural changes in the market over the last 10 years, and that the current regulatory structure was not necessarily designed for the risks faced today. She stated that federal and state agencies were working to address the risks, but she noted that they faced challenges in doing so. She said that the staff analysis was focused on four components of the regulatory framework: risk monitoring; promoting safe and sound operations; contingency planning for a stress event; and resolution planning. She then described work being done by agencies, including Ginnie Mae, FHFA, the Federal Reserve, and state regulators, regarding these four issues. Among other things, she cited counterparty risk analysis and monitoring; the development of a stress-testing framework and a risk dashboard; the approval of model state regulatory prudential standards; examinations; the establishment during the COVID-19 pandemic of the Pass-Through Assistance Program to advance principal and interest obligations for mortgage-backed securities issuers; and sub-servicing contracts and default readiness playbooks in the context of resolution planning. She also described actions that could be taken based on current authorities and practices.

Mr. Keith then stated that significant work was underway to mitigate the identified risks, but he noted that limitations may prevent the risks from being sufficiently addressed without reforms. He said that, notwithstanding the robust supervisory and enforcement actions of state regulators, challenges remained, including the fragmented oversight of nonbank mortgage servicers; the lack of federal prudential supervisory and enforcement authority; a lack of liquidity available in an emergency context; and the lack of a central coordinator to facilitate the bankruptcy or resolution process.

Ms. Lee stated that since April, staff had assessed actions federal and state agencies had taken to address the identified risks in the nonbank mortgage sector and what additional steps could be taken to mitigate the risks. She concluded by outlining potential next steps for the Council to consider, including further interagency coordination and additional public communications.

The Chairperson stressed the importance of agencies being prepared to respond in the event of stress and encouraged further analysis regarding potential structural reforms. She then turned to Ms. McCargo for comment.

Ms. McCargo stated that Ginnie Mae works with issuers to monitor identified risks. She said that nonbank mortgage issuers are critical to the sector and pose certain risks. She stated that Ginnie Mae, in its efforts to promote a stable and resilient nonbank mortgage sector, was working to support liquidity but lacks the tools needed to sufficiently address liquidity concerns. She noted that Ginnie Mae was managing the default of a reverse mortgage lender and mortgage-backed securities issuer. She said that the default of this issuer had been an isolated event so far, but pointed to broader structural challenges in the reverse mortgage market and the general tightening of liquidity for nonbank mortgage issuers across the market.

The Chairperson then turned to Sandra Thompson, Director of the FHFA. Director Thompson noted the interdependencies between the housing and banking sectors, and she said that large banks withdrawing from the mortgage service industry had led to an increase in nonbank mortgage origination and servicing. She noted the need for increased coordination and communication with respect to planning for any potential default by nonbank mortgage servicers.

Council members then asked questions and had a discussion, including regarding the need for interagency coordination and the limitations of existing authorities of state and federal agencies to address the identified risks.

## 2. Climate-related Financial Risk Committee Update

The Chairperson then turned to the second agenda item, an update on the work of the Council's staff-level Climate-related Financial Risk Committee (CFRC). She introduced Sini Matikainen, Senior Policy Advisor in the Office of the Financial Stability Oversight Council at Treasury, and Terri Barger, Acting Technical Expert for Commercial Credit Policy at the OCC.

Ms. Matikainen noted that the charter of the CFRC states that its duties include identifying priority areas for assessing and mitigating climate-related risks to the financial system; facilitating information sharing and coordination among staff of Council members and member agencies; coordinating efforts among Council members and member agencies to address data gaps; and overseeing the Council's Climate-related Financial Risk Advisory Committee (CFRAC).

Ms. Matikainen stated that staff had made significant progress since the most recent staff update to the Council on the work of the CFRC. She noted that the CFRC had continued to serve as a forum for interagency cooperation and coordination, particularly through the use of working groups. She said that the CFRC's Scenario Analysis Working Group had provided a valuable forum for technical discussions related to scenario analysis. She also noted that in October 2022 the Council had established the CFRAC, which is holding regular meetings. She said that Council member agencies continued their progress in advancing recommendations in the Council's 2021 climate report. She noted that the OFR had launched a new platform, the Joint Analysis Data Environment (JADE), for improving regulators' access to data and computing tools. She highlighted that the Federal Reserve had launched a pilot climate scenario analysis for six large bank holding companies, and that federal banking agencies had proposed for public comment principles regarding large banks' management of climate-related financial risks. She

also noted that FIO had issued a report assessing climate-related issues and gaps in the supervision and regulation of insurers and that the SEC had proposed rules on climate-related disclosures.

Ms. Barger noted that the CFRC had created a Risk Assessment Working Group to identify and assess climate-related financial risks, and she described the group's efforts to develop a framework to evaluate both physical risk and transition risk. Regarding physical risk, she noted that climate-related economic impacts can impact the financial system through credit losses, market disruptions, and other mechanisms. She noted that the working group was continuing to develop its climate-related financial risk monitoring capabilities, and she described examples of how to monitor credit, market, and operational risks.

Ms. Matikainen concluded by describing further anticipated CFRC efforts to serve as a forum for interagency collaboration, discussion, and analysis, including regarding the intersection between physical risk, housing, and insurance.

Council members then had a discussion regarding the importance of member agencies continuing to gather and share data, collaborate regarding climate-related financial risks, and advance efforts to address climate-related financial risks within their authorities.

### 3. Developments in the Banking Sector

The Chairperson then introduced the next agenda item, an update on developments in the banking sector, including the results of the 2023 bank stress tests. She turned to Michael Barr, Vice Chair for Supervision at the Federal Reserve, for the first update.

Mr. Barr stated that overall, the banking system was strong and resilient, and that most banks had substantial capital and liquidity. He noted that the actions taken by the FDIC and Federal Reserve in March 2023 had limited the stress from spreading. He noted that markets for repurchase agreements and commercial paper were functioning appropriately. He also noted that a reduction in deposits meant that many banks were getting more expansive market-based funding, compressing their net interest margins. He noted that investors continued to monitor banks with large unrealized losses or commercial real estate exposures, especially those with concentrated exposures to office properties. He noted that the FDIC, OCC, and Federal Reserve had issued proposed rules to implement the so-called Basel III endgame, and that the Federal Reserve had also issued proposed refinements to the risk-based capital surcharges for global systemically important banks (G-SIBs).

The Chairperson then turned to Martin Gruenberg, Chairman of the FDIC. Chairman Gruenberg stated that the actions taken in March to protect uninsured deposits had a market-stabilizing effect, and he said that since then, there had been a stabilization of liquidity in regional banks. He noted the continuing need to monitor for risks. He also noted the recent issuance of the Basel III proposed rules, and he said that the FDIC expected to propose a long-term debt rule for midsized banks. With respect to supervisory issues, he noted a focus on banks with concentrations of uninsured deposits.

The Chairperson then turned to Michael Hsu, Acting Comptroller of the Currency. Acting Comptroller Hsu stated that it was important to remain vigilant in monitoring risks, including those related to commercial real estate. He also noted the importance of ensuring uniform supervision across the banking sector, to promote a level playing field and high standards.

The Chairperson then introduced Lisa Ryu, Senior Associate Director of the Division of Supervision and Regulation at the Federal Reserve, and Doriana Ruffino, Manager in the Division of Supervision and Regulation at the Federal Reserve, for the presentation on the 2023 bank stress test results.

Ms. Ruffino described the results of the Federal Reserve's stress tests. She first stated, in sum, that in the stress tests, no bank's post-stress minimum common equity tier 1 capital ratio fell below 4.5 percent under the severely adverse scenario. She stated that for the 23 banks subject to the tests, preliminary stress capital buffers increased for eight, decreased for nine, and remained at the 2.5 percent floor for six. She also noted that for the U.S. G-SIBs, market losses in the tests under the exploratory market shock were lower than losses under the global market shock.

Ms. Ruffino then described certain assumptions in the stress tests, including a 6.4 percentage-point increase in the unemployment rate, a 38 percent decline in the House Price Index, and a decline in the Treasury bill rate of 3.9 percentage points. She then summarized the results, noting that in the stress tests the aggregate common equity tier 1 capital ratio fell by 2.5 percent to a minimum of 9.9 percent, with gains on available-for-sale securities partly offsetting the decline in pretax net income. She noted that mortgages and credit card loans drove higher consumer losses, and that business loan loss rates declined. She noted that projected pre-provision net revenue was similar to the previous stress tests. She then described the Federal Reserve's exploratory market shock, which applied to the eight U.S. G-SIBs and did not affect the firms' capital requirements. She stated that the exploratory market shock featured moderate increases in interest rates, the U.S. dollar, and commodity prices in the opposite direction of the global market shock from the stress tests, and other market price moves that were less severe than the global market shock. She stated that for most G-SIBs, the exploratory market shock resulted in lower losses, but the composition of the losses varied. She concluded by noting that scenario shocks should be designed holistically to capture risks.

The Chairperson stated that the stress tests showed that the participating banks have sufficient capital to absorb losses from significant downside macroeconomic scenarios. She stated that the information gathered from the exploratory market shock also illustrated the usefulness of continued innovation in stress tests. She also stated that the banking sector events earlier in 2023 indicated how important it is to think creatively about potential shocks to U.S. banks.

The Chairperson adjourned the executive session of the meeting at approximately 11:12 A.M.

### **Open Session**

The Chairperson called the open session of the meeting of the Council to order at approximately

11:19 A.M.

The Chairperson outlined the agenda for the open session, which included (1) an update on the Council's Climate-related Financial Risk Committee, (2) an update on the transition from LIBOR to alternative reference rates, and (3) a vote on the minutes of the Council's meeting on June 16, 2023.

#### 1. Climate-related Financial Risk Committee Update

The Chairperson introduced the first agenda item, an update on the Council's Climate-related Financial Risk Committee. She stated that addressing climate-related financial risk is a priority for the Council, and she said that she appreciated the significant progress Council members had made since the Council published its climate report in October 2021. She introduced Sandra Lee, Deputy Assistant Secretary for the Council at Treasury, for an update on efforts by the Council and its members to identify and address climate-related financial risks.

Ms. Lee stated that since the update to the Council in July 2022 on the CFRC's progress, the Council and its members had continued to advance the recommendations in the Council's climate report. She said that the CFRC had begun meeting in February 2022 and had served as a valuable forum for Council members to share information on climate-related financial risk, facilitate the development of common approaches and standards, and foster communication across Council members. She stated that the CFRC and its working groups were advancing key themes from the Council climate report, particularly on data sharing and risk assessment.

Ms. Lee stated that following the meeting, the Council would release a staff progress report with additional details on the work of the CFRC and related topics. She noted that member agency staff on the CFRC were developing a framework to identify and assess climate-related financial risk and develop a preliminary set of risk indicators for banking, insurance, and financial markets. She said that member agency staff on the CFRC were collaborating with the OFR on its new platform, JADE, to improve regulators' access to data, high-performance computing tools, and analytical and visualization software. She stated that staff's work in this area was grounded in the Council's mandate to assess and address the financial stability implications of climate-related financial risk. She said that staff's efforts to improve data sharing and risk assessment would advance the Council's understanding of climate-related financial risks and promote the resilience of the financial system. She said the staff progress report highlighted both the work being done collectively through the Council and significant actions undertaken by individual Council members since the publication of the Council climate report. She said that these included actions by FIO, which issued a request for comment on a proposed collection of data from property and casualty insurers regarding current and historical underwriting data on homeowners' insurance. She said the request for comment seeks to assess the potential for major disruptions of private insurance coverage in regions of the country that are particularly vulnerable to the impacts of climate change. She stated that the OCC, FDIC, and Federal Reserve had each released for public comment proposed principles for climate-related financial risk management for certain large financial institutions. She said that the Federal Reserve had also launched a pilot climate scenario analysis exercise for six large bank holding companies and



that the SEC had issued a proposed rule that would require registrants to include certain climate-related disclosures in their registration statements and periodic reports.

Ms. Lee stated that member agency staff would continue to use the CFRC as a forum for interagency engagement and coordination, with a focus on addressing data gaps and the development of key risk indicators for risk-assessment purposes. She said that staff would also further explore the intersection between physical risk, real estate, banking, insurance, and household finance. She said that acute and chronic physical risks can lead to sharp falls in property values and incomes in certain areas, with implications for real estate markets, households, and financial institutions. She stated in conclusion that staff would evaluate the interconnections and spillovers in this area and work to better understand the transmission channels through which these risks could affect the financial system.

The Chairperson noted that work on climate-related financial risk was a priority for the Council. She said that since the update to the Council on this topic in 2022, the physical impacts of climate change had continued to worsen. She stated that in the previous month, average global temperatures had set new records for the hottest temperatures in recorded history, and she noted that during the summer of 2023 millions of Americans had been exposed to both record-breaking heat and wildfire smoke. She said that climate disasters had grown in frequency and intensity in recent years. She noted that according to the National Oceanic and Atmospheric Administration, since 1980 the United States had experienced over 360 weather or climate disasters where overall damages or costs had reached or exceeded \$1 billion, averaging approximately eight such disasters per year. She said that in the previous three years alone, there had been a total of 60 such events, an average of 20 per year, which she noted is two and a half times greater than the long-term average. She said that American households were already experiencing the impacts, even if their own homes had not been damaged.

The Chairperson stated that as the frequency and intensity of climate-related disasters increases, some insurers had begun raising the rates for homeowners' insurance or were stepping back entirely from offering coverage in higher-risk areas. She said that as a result, more households were turning to residual markets for coverage or were foregoing insurance entirely. She said that while recent news coverage had focused on high-profile insurer withdrawals from California and Florida, insurer withdrawals, insolvencies, and significant premium increases were occurring in multiple states. She said that the United States experienced \$165 billion in total economic losses from climate-related disasters in 2022, only 60 percent of which were covered by insurance, suggesting the need to understand how to narrow this protection gap. She said that these climate-related impacts had the greatest impacts on underserved and disadvantaged communities, which are already less resilient to financial shocks. She stated that it was important to better understand not only the challenges to households, but also the implications of changes in property insurance for real estate markets and financial institutions that rely on insurers to help manage risks. She said that she welcomed staff's intent to expand its analysis on the interconnectedness of real estate, insurance, and other financial markets and the implications for systemic risk, alongside current staff efforts to expand capacity and improve data and management of climate-related financial risks. She expressed her support for the progress on these topics and other areas identified in the staff progress report, and she invited other Council members to provide updates on the efforts at their agencies in this area.

Jerome Powell, Chair of the Federal Reserve, stated that the staff progress report highlighted the range of work on climate-related financial risks by Council members. He said that it was important that Council members continue to work to ensure that the financial system understands and appropriately manages the financial risks of climate change. He said that the Federal Reserve would continue to collaborate with other Council member agencies on this issue. Chair Powell then turned to Michael Barr, Vice Chair for Supervision at the Federal Reserve.

Mr. Barr stated that the staff progress report summarized Council member agency activities in implementing the recommendations of the October 2021 Council climate report. He said that climate change poses significant challenges for the global economy and the financial system, with implications for the safety and soundness of financial institutions and the stability of the financial sector more broadly. He said that it is important that the Council continues to work to ensure the financial system understands and appropriately manages the financial risks of climate change. He said that while further work remained, the report indicated that the Council is moving in the right direction.

Mr. Barr stated that the responsibilities of the Federal Reserve with respect to climate change are important but narrow, and derive from its existing mandate to promote the safety and soundness of financial institutions and the stability of the financial sector more broadly. He noted that the staff report highlighted progress on scenario analysis. He said that the Federal Reserve was conducting a pilot climate scenario analysis exercise to help large banks and supervisors better understand the effects of various hypothetical climate scenarios on individual banks. He said that the goal of the pilot exercise was to deepen understanding of risk-management practices in this area and enhance the ability of the largest banks and supervisors to identify, measure, monitor, and manage climate-related financial risks. He noted that because climate scenario analysis is an emerging risk-management tool, the exercise was exploratory in nature and there were no consequences for bank capital or supervisory implications. He stated that the Federal Reserve anticipated publishing information on an aggregated, not firm-specific, basis by the end of 2023, to provide insights into how large banking organizations were incorporating climate-related financial risks into their risk-management frameworks and to highlight how participants were approaching and addressing practical and conceptual challenges with understanding climate-related financial risks. He said that the Federal Reserve would continue to work with other member agencies to increase their collective understanding of the financial impacts of climate change, and to contribute to the increased resiliency of supervised firms and the stability of the broader financial system.

Gary Gensler, Chair of the SEC, noted the reference to the work of the SEC in the staff progress report, and provided additional context on the SEC's proposal regarding climate risk disclosure. He said that in response to the Great Depression and the fraudulent practices of those times, President Roosevelt and Congress collaborated to develop the federal securities laws, under which investors may choose to decide which risks they take, so long as public companies make complete and truthful disclosure. He stated that the SEC was assigned an important role. He said that the SEC focuses on disclosures regarding investments but remains neutral regarding the merits of investments. He said that while the SEC was not assigned any role with respect to climate risk itself, it does have an important role in helping to ensure that public companies make full, fair, and truthful disclosure about the material risks they face. He said that issuers were

already making climate risk disclosures and investors were making investment decisions based on those disclosures. He noted that a majority of the top 1,000 issuers by market capitalization already make such disclosures, including disclosures regarding scope 1 and scope 2 greenhouse gas emissions. He also noted that investment firms representing tens of trillions of dollars in assets under management were making decisions relying on those disclosures. He stated that the SEC, in fulfilling the role assigned by Congress, had issued a proposal for comment regarding climate-related disclosures to improve consistency and comparability of the disclosures that the SEC currently requires. He said that the SEC was carefully considering the more than 15,000 comments it had received on the proposal. He stated that the agency, taking into account relevant economic and legal considerations, would consider adjustments to the proposed rule that SEC staff, and ultimately the SEC itself, determine are appropriate in light of those comments.

Martin Gruenberg, Chairman of the FDIC, stressed the important role that the Council plays in fostering collaboration among the financial regulatory agencies in their response to climate-related financial risks. He said that each of the Council member agencies is devoting significant resources within its scope of responsibility to better understand and engage with the financial risks of climate change. He stated that the FDIC had established an interdivisional working group to evaluate the responsibilities of the FDIC for supervision, resolution, and deposit insurance, and to consider how the financial risks of climate change might impact those responsibilities. He said that the three banking agencies had proposed guidance that they intended to jointly finalize in the near future. He said that the Council plays a unique role in assisting member agencies to gather, share, and analyze information regarding climate-related financial risks.

Michael Hsu, Acting Comptroller of the Currency, stated that he supported the publication of the staff progress report. He highlighted the efforts of the CFRC Risk Assessment Working Group, and he noted that staff participating in that group were developing a framework to identify and assess climate-related financial risk, which included a preliminary set of risk indicators for banking, financial, and insurance markets. He stated that the goal of the working group was to improve understanding of how physical and transition risks arising from climate change may manifest as financial risk. He noted that each of the federal banking agencies had proposed high-level principles underpinning a risk-management framework to address climate-related financial risk. Finally, he said that, while more work remained, many large banks had been proactive in incorporating climate-related financial risk in their risk-management frameworks and policies. He said that these efforts included updating their strategic-planning processes, incorporating climate risk into their risk-appetite statements, and using scenario analysis to better understand the risk profiles. He said that the OCC, as it pursued next steps regarding its proposed climate risk management principles, would continue to monitor progress and encourage safe and sound practices at large banks.

Rostin Behnam, Chairman of the CFTC, expressed his support for the staff progress report. He said that CFTC staff continued to use a broad set of stress-testing scenarios to ensure that registered entities were prepared to meet their financial obligations during periods of elevated market risk. He stated that CFTC staff intended to monitor the growth of derivatives markets that may be affected by physical or transition risk over time and identify areas where additional or adjusted scenarios may be needed. He said that the CFTC, in addition to its collaboration with

the CFRC, had hosted a convening on voluntary carbon markets, in which several federal agencies had participated. He said that, following the convening, he anticipated that the CFTC would consider issuing guidance addressing standards in voluntary carbon markets. He also noted that the CFTC's Whistleblower Office in the Division of Enforcement issued an alert notifying the public how to identify and report potential Commodity Exchange Act violations connected to fraud or manipulation in carbon markets. He stated that the CFTC's Division of Enforcement had announced the establishment of two new task forces, one of which would focus on environmental fraud and misconduct in derivatives and relevant underlying spot markets. He said that the new environmental fraud task force would investigate, among other matters, potential fraud with respect to the purported environmental benefits of purchased carbon credits.

Rohit Chopra, Director of the CFPB, stated that the previous weekend, 118 million Americans had experienced a heat index above 100 degrees. He noted that a few weeks ago, the hottest July 4 on record was recorded across the world, only to be surpassed on July 5 and then again on July 6. He said that Canadian wildfire smoke surrounding the Washington Monument was a visible sign of the conditions that the United States must prepare for. Noting that thousands of records had been shattered across the world, he said that these conditions were adversely impacting ordinary Americans. He said that loan losses associated with climate events and natural disasters had led many property insurers to decline offers to renew policies, most notably in California and Florida. He noted that many small insurers in Florida had gone out of business. He said that a reduction in available insurers, combined with the increased climate risk in these areas, had led to drastically higher insurance costs. He noted, in addition, that in certain circumstances if a homeowner's insurance coverage lapses and is not promptly replaced, the lender may acquire insurance for the homeowner and then charge them for it. He stated that such force-placed insurance policies could be more than double the price of regular insurance, since they are generally not underwritten to the specifics of the home. He said that CFPB rules require a servicer to notify a homeowner whose policy has lapsed at least 45 days before charging the borrower for this insurance. He said that increased costs compound other home affordability costs and can make it difficult for homeowners to satisfy other debt payments and living expenses. He noted that such trends can also lead to declining home values and force homeowners to sell their home.

Director Chopra stated that homeowners have some options, including making use of state-backed plans, if their private homeowners' insurance is to be cancelled or their premium has become unaffordable. He said they may also be able to access their state's Fair Access to Insurance Requirements plan, although he noted that such plans are typically expensive and have more limited coverage. He said that homeowners can also shop for alternatives by contacting their state's insurance regulator to determine which insurers are operating in their area. He noted that homeowners can ask their agent why they are receiving notice from their insurer and if there is a possibility for the insurer to reconsider their decision. He said that homeowners should maintain contact with their mortgage servicer and notify them of any change in insurance to avoid the possibility of expensive force-placed insurance. He stated that the CFPB had provided guidance on how homeowners can remove such insurance, and he said that the CFPB would continue to monitor mortgage market participants. Noting that these problems were likely to worsen, he said that it is incumbent on state and federal regulators and policymakers, including

insurance regulators, consumer protection regulators, and banking regulators, to collaborate to ensure that homeowners are not seriously impacted and the mortgage system remains safe.

James Martin, Acting Director of the OFR, stated that he updated the Council in 2022 about a pilot the OFR was preparing to launch, called the Climate Data and Analytics Hub. He said that OFR built the hub partly in response to a request from the Federal Reserve, which had asked the OFR to leverage its data hosting and analytical capabilities to support research on climate-related financial risk. He said the resulting pilot also advanced President Biden's Executive Order on Climate-related Financial Risk, which called on the OFR to assist the Council in assessing and identifying climate-related risks to financial stability. He stated that this request also presented an opportunity for the OFR to test its ability to create a scalable model of a data hub environment that Council member agencies could use for research on various financial stability topics.

Acting Director Martin said that, given the success of the pilot, the OFR announced in April 2023 that it was developing an expanded and enhanced version of the climate hub. He said that the OFR had launched its Joint Analysis Data Environment, or JADE, an OFR-hosted platform designed for Council agencies to access, integrate, and jointly analyze data. He said that its secure, cloud-based environment provides access to analysis-ready data, analytical software, and high-performance computing tools. He stated that while climate-related financial risk was the first use case for JADE, the OFR had designed JADE to be responsive to the evolving nature of risks to financial stability. He said that the financial system faces threats from multiple sources, and he noted that such threats do not adhere to regulatory boundaries, but rather travel from one regulated space to another. He said that the stability of the financial system is best promoted when regulators work together. He stated that regulators would benefit from the JADE platform's capacity to access, integrate, and analyze data. He said that JADE would enable regulators to produce interdisciplinary research that identifies emerging risks.

Steven Seitz, Director of FIO, stated that the staff progress report demonstrated the substantial progress in addressing the recommendations of the Council's climate report. He said that FIO supports the work of the CFRC and would continue to prioritize this collaboration. He noted that FIO continued to make progress in responding to the Council's climate report recommendations. He stated that in June 2023, FIO published its report on insurance supervision and regulation of climate-related risk, which highlighted current efforts by the NAIC and state insurance regulators to incorporate climate-related risk into supervision and regulation, while also noting potential opportunities for further progress. He said that the FIO report provided 20 recommendations to help improve the management and supervision of climate-related risk within the state-regulated insurance sector, some of which could also bear on the recent decisions of several large carriers to scale back their exposure in parts of the country that are vulnerable to climate-related losses. He said that it is also important for regulators and other stakeholders, when assessing climate-related financial risk, to have access to consistent, comparable, and granular data. He said that to facilitate this goal, in October 2022, FIO published a request for comment proposing the collection of current and historical underwriting data on homeowners' insurance from certain insurers. He said that FIO was continuing to consider the comments it received. He stated in conclusion that FIO would continue its engagement with member agencies as the Council examines the interconnections between the insurance market, physical risk, and real estate markets.

Elizabeth Dwyer, Superintendent of Financial Services for the Rhode Island Department of Business Regulation, stated that state insurance regulators have extensive expertise and knowledge in property insurance, including regarding some of the topics mentioned by Director Chopra. She said that state insurance regulators had begun discussions with the CFPB and FHFA on these topics, and she welcomed collaboration with other regulators on property insurance issues.

Later in the meeting, Thomas Workman, the Council's independent member with insurance expertise, expressed his support for the staff progress report, and noted the importance of data gathering, risk analysis, and transition analysis in relation to climate-related risk.

## 2. LIBOR Update

The Chairperson then introduced the next agenda item, an update on the transition from LIBOR to alternative reference rates. She turned to Mr. Barr to provide the update.

Mr. Barr stated that, following 10 years of preparation, the end of U.S. dollar LIBOR had occurred without significant issues on June 30. He said that it was useful to consider what had been accomplished in connection with the transition from LIBOR. He said that the Council had focused on the transition because LIBOR represented a significant risk to financial stability. He noted that LIBOR had been replaced methodically and smoothly. He said that with a transition to the overnight Secured Overnight Financing Rate (SOFR), a major vulnerability had been eliminated and the U.S. and global financial system now rested on a resilient and sound key benchmark. He stated that this complex risk to the financial system had been successfully resolved through collaboration with the Alternative Reference Rates Committee (ARRC), the private-sector body leading the transition in the United States, and other private-sector participants. He said that had this effort not been undertaken, the end of LIBOR could have caused many parts of the financial system to come to a halt. He said that this process had been a model of public-private sector collaboration, involving collaboration across all the Council member agencies as well as with authorities in the United Kingdom and the Financial Stability Board's Official Sector Steering Group, among others. He said, however, that the official sector should not have had to intervene to do this work. He stated that in the future, market participants should avoid repeating the mistakes they made with LIBOR. He said that in light of the recent announcement by the International Organization of Securities Commissions (IOSCO) that certain credit-sensitive rates were not compliant with IOSCO's principles for a stable and reliable benchmark, market participants should re-evaluate whether those rates are appropriate for their use and for their customers. He then turned to David Bowman, Senior Associate Director in the Division of Monetary Affairs at the Federal Reserve, to provide additional detail on the transition.

Mr. Bowman reiterated that the transition from LIBOR on June 30 passed without incident. He said that LIBOR contracts would continue to roll off into SOFR when they reach their first post-June resets over the next several months. He stated that a few borrowers that had been unable to satisfactorily remediate loans beforehand opted into one further six-month LIBOR interest period in order to further negotiate with their lenders. He said that most of the approximately 10,000 to 20,000 remaining securities that had not already registered rate changes in the Depository Trust

and Clearing Corporation's communication tool before June 30 had resets in July or August and would need to communicate their new rates by that time. He said that loans referencing synthetic LIBOR had effectively already become SOFR loans, but they would need to be more formally remediated before September 2024, when synthetic U.S. dollar LIBOR is expected to end publication.

Mr. Bowman stated that a new, much more stable system had emerged, with SOFR as the dominant interest rate benchmark in derivatives and now referenced in almost all floating-rate capital products and consumer loans. He said that while most business loans now reference CME Group's term SOFR rates, he anticipated that use of term SOFR would remain appropriately limited to supporting this market, as recommended both by the Council and the Financial Stability Board, given that CME Group had incorporated most of the ARRC's recommendations directly into its licensing agreement for term SOFR. He stated that while the ARRC would wind down, its recommendations in regard to term SOFR would remain, and he noted that any uses of term SOFR outside of the ARRC's recommendations would represent a violation of a contractual agreement with CME Group.

Mr. Bowman stated that the ARRC's recognition of somewhat wider trading of term SOFR-SOFR basis swaps by non-dealers appeared to be having its intended effect. He said that there had been a small number of these trades, and he noted that while this market would likely never be very large or very liquid, it was already allowing dealers to lay off a portion of their term SOFR risk, ensuring the use of term SOFR can remain sustainable in supporting the business loan market. He said that market participants would need to avoid repeating the mistakes that they made with LIBOR. He said that contracts need to incorporate robust fallback language, even for SOFR and term SOFR. He stated that the International Swaps and Derivatives Association had created one example of such fallback language for SOFR in its definitions, and he noted that this example can be used in other SOFR products as well. He said that fallback language for other reference rates, including term SOFR, is best served by referring to explicit fallback rates at the top of the rate waterfalls, which might be SOFR or an average of SOFR set in advance or in arrears, rather than relying on the discretion of one counterparty to select a new benchmark.

Mr. Bowman stated that market participants also need to adequately assess the rates they use and ensure these rates are appropriate for their intended uses. He said the ARRC had spent two years analyzing all the potential markets and rates that could serve as the basis for the recommended benchmark before the ARRC selected SOFR. He said that every day, the Federal Reserve Bank of New York publishes a full set of volumes and rate distribution statistics for each of the market components underlying SOFR, allowing market participants to assess SOFR's construction and robustness daily. He stated that in publicly establishing the reasons behind the choice of SOFR, the ARRC had warned that it believed that certificate of deposit and commercial paper markets were too thin to serve as the basis for a robust rate. He said that IOSCO had now finished a review that arrived at the same conclusion, and he noted that IOSCO had asked certain administrators setting benchmarks based on these markets that had previously represented that the benchmarks were compliant with IOSCO's principles to remove all statements that they are compliant. He said that these rates had relatively limited use, although there were no use restrictions embedded in their license agreements. He noted that many market participants using

these rates had pointed to statements that the rates were compliant with IOSCO principles to justify this use. He said that those market participants would need to re-evaluate their choices in light of IOSCO's statement. He said that accounting firms that previously attested that these rates were compliant with IOSCO's principles would also need to re-evaluate their understanding of the principles.

Mr. Bowman concluded by saying that while the ARRC would wind down, its recommendations would not. He said that the new system was designed to last, but he noted that the official and private sectors would need to continue to monitor the use of interest rate benchmarks to ensure that the problems with LIBOR do not recur. He stated that the Financial Stability Board would continue to monitor the reference rate environment in conjunction with IOSCO and other international groups.

The Chairperson stated that the Council had identified LIBOR as a significant risk to financial stability for over a decade and had supported actions to transition away from LIBOR toward alternative reference rates. She said that the final publication of U.S. dollar panel-based LIBOR had occurred on June 30, which she noted occurred without market disruption. She said that, given the substantial time and effort invested by Council member agencies, market participants were well-prepared for the transition. She said that the LIBOR transition served as an example of how industry participants and regulators can collaborate to solve complex issues. She said that it was now important to build on the progress made following nearly a decade of official sector involvement to transition safely from LIBOR. She said that market participants should ensure that the issues that led to problems in LIBOR are not recreated. She said that it was important to incorporate robust fallback language in financial contracts and adhere to the ARRC's recommendations, such as limiting the use of term SOFR to the suggested areas and ensuring that the vast majority of transactions are rooted in the overnight rate. She noted that a small portion of the U.S. loan market still referenced LIBOR, and she encouraged market participants to finish transitioning their contracts, especially given that the publication of synthetic U.S. dollar LIBOR is not expected to continue after September 2024. The Chairperson then invited other members of the Council to comment on the LIBOR transition.

Chair Powell expressed his appreciation for the contributions of Mr. Bowman in the transition from LIBOR. Surveying the history of the transition, he noted that the ARRC was convened at the end of 2014 and identified SOFR as the preferred replacement following a market-wide consultation. He said that SOFR had gone into production in 2018, and he noted that the ARRC had successfully encouraged voluntary take-up of SOFR in consumer mortgages, floating-rate debt, derivatives, and securitizations over the next several years. He stated that the ARRC had also supported more robust fallback language in legislation in several states to help address legacy LIBOR contracts, which he noted served as a template for the federal legislation that was ultimately enacted. He said that Mr. Bowman played an important role in this process.

Chair Gensler stated that LIBOR was an innovation of the 1970s to facilitate businesses borrowing from banks at a rate that adjusted based on market interest rates. He said that by the 1980s, to determine LIBOR, banks were using a rate at which banks were lending to each other without taking collateral. He said that LIBOR became so popular that it was embedded in hundreds of trillions of dollars of financial contracts around the world, encompassing not only



traditional business contracts, but also mortgages and car loans. He said it was therefore critical that LIBOR be based on an accurate and reliable indicator. He noted, however, that there were few transactions underpinning LIBOR. He said that in 2008, staff at the CFTC began investigating LIBOR. He stated that CFTC staff, working with law enforcement partners around the globe, had identified multiple cases of banks manipulating LIBOR for their own profit and defrauding the public. He said that policymakers and central banks, including the Federal Reserve, collaborated to address the issue. He noted that the Council, the Financial Stability Board, and market regulators, including the CFTC and SEC, played an important role in the response. He noted that Congress took legislative action to facilitate the LIBOR transition. He said that in the United States, the main replacement for LIBOR is SOFR. He cautioned that regulators must continue to be vigilant and guard against the emergence of new rates that are not robust. He said that certain alternatives being considered in the markets presented many of the same flaws as LIBOR, such as thin markets with few underlying transactions, which created a system vulnerable to collapse and manipulation.

Chair Gensler stated that he believed that credit-sensitive rates, such as the Bloomberg Short-Term Bank Yield Index, have infirmities and would not stand the test of time or be conducive to financial stability. He noted that IOSCO had recently conducted a review of certain alternatives to U.S. dollar LIBOR and concluded that the credit-sensitive rates reviewed were not found to meet IOSCO's principles for stable and reliable benchmarks in the areas of benchmark design, data sufficiency, and transparency. He concluded by noting that the reliance on LIBOR represented a cautionary tale.

Chairman Behnam highlighted the work of CFTC staff in identifying the infirmities of LIBOR and the efforts of Mr. Bowman in the transition from LIBOR. He said that a CFTC subcommittee had worked closely with the ARRC to raise awareness regarding potential challenges, identify risks to financial markets and individual consumers, and develop solutions within the derivatives space. He stated that the CFTC had collaborated with the Federal Reserve and the Federal Reserve Bank of New York, in addition to the ARRC, and he noted that the collaboration yielded successful results, from plain-English disclosures to tabletop exercises to prepare for the SOFR transition by central counterparties. He said that the derivatives industry had transitioned in a smooth and orderly fashion. He said that a more stable system had emerged, with SOFR as the dominant interest rate benchmark, and he stated that market participants should continue to incorporate robust contractual fallbacks. He said that the LIBOR transition had shown the importance of robust, workable fallback provisions. He emphasized the importance of using SOFR, term SOFR, and any other reference rates that continue to align with the recommendations of the ARRC, the Financial Stability Board, and the Council. He said that use of term SOFR rates in derivatives and in most other cash markets must be limited to avoid the types of problems created by LIBOR. He said that market participants should ensure that their choice of reference rates is fit for purpose, robust, and rooted in deep, credible, and liquid markets. He said that as products utilizing these rates and credit-sensitive rates are reviewed by the CFTC, the agency would evaluate them to ensure they are consistent with these principles.

Director Chopra stated that following the global financial crisis, the public learned that several global financial institutions had conspired to rig LIBOR. He noted that some of these institutions would later admit to criminal misconduct and pay billions of dollars in penalties. He said that for

years, the interest rate that underpinned hundreds of trillions of dollars of financial contracts, including many of the adjustable-rate mortgages that harmed homeowners across the country in the 2008 crisis, was fraudulent. He said that the CFPB had worked alongside other agencies to support the ARRC in its efforts to transition financial markets away from this faulty rate, by providing analysis on the interplay between LIBOR and any successor reference rate on consumers and on consumer finance markets more broadly. He said that the CFPB had issued rules and guidance for industry to implement the transition of these consumer financial products, including in the nonbank sector, away from LIBOR. He stated that the CFPB had published information to help consumers understand and prepare for the transition and had updated its Consumer Handbook on Adjustable-Rate Mortgages. He said the criminal manipulation of LIBOR by financial institutions had been extremely costly. He said that the CFPB would continue working to ensure that companies complete an orderly transition away from LIBOR. Noting that financial history repeats itself, he said that policymakers must guard against the emergence of future reference rates that could be exploited by bad actors.

### 3. Resolution Approving the Minutes of the Meeting Held on June 16, 2023

*BE IT RESOLVED, by the Financial Stability Oversight Council (Council), that the minutes attached hereto of the meeting held on June 16, 2023 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 12:12 P.M.