

## Minutes of the Financial Stability Oversight Council

July 17, 2018

### PRESENT:

Steven T. Mnuchin, Secretary of the Treasury and Chairperson of the Financial Stability Oversight Council (Council)  
Jerome H. Powell, Chairman, Board of Governors of the Federal Reserve System (Federal Reserve)  
Jelena McWilliams, Chairperson, Federal Deposit Insurance Corporation (FDIC)  
J. Christopher Giancarlo, Chairman, Commodity Futures Trading Commission (CFTC)  
J. Michael Mulvaney, Acting Director, Bureau of Consumer Financial Protection (Bureau)  
Melvin Watt, Director, Federal Housing Finance Agency (FHFA)  
Joseph Otting, Comptroller of the Currency, Office of the Comptroller of the Currency (OCC) (by telephone)  
J. Mark McWatters, Chairman, National Credit Union Administration (NCUA)  
Thomas E. Workman, Independent Member with Insurance Expertise  
Steven Dreyer, Director, Federal Insurance Office, Department of the Treasury (non-voting member)  
Ray Grace, Commissioner, North Carolina Office of the Commissioner of Banks (non-voting member)  
Peter Hartt, Director, Insurance Division, New Jersey Department of Banking & Insurance (non-voting member)  
Melanie Lubin, Securities Commissioner, Maryland Office of the Attorney General, Securities Division (non-voting member) (by telephone)

### GUESTS:

#### Department of the Treasury (Treasury)

Craig Phillips, Counselor to the Secretary  
Bimal Patel, Deputy Assistant Secretary for the Council  
Eric Froman, Principal Deputy Assistant General Counsel (Banking and Finance) and Executive Director of the Council  
Stephen Ledbetter, Director of Policy, Office of the Financial Stability Oversight Council

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

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

#### Federal Deposit Insurance Corporation

Jason Cave, Special Advisor to the Chairman for Supervisory Matters

#### Securities and Exchange Commission (SEC)

Hester Peirce, Commissioner  
Adam Glazer, Counsel to Commissioner Hester Peirce

Commodity Futures Trading Commission  
Susan Milligan, Deputy General Counsel

Bureau of Consumer Financial Protection  
Brian Johnson, Acting Deputy Director

Federal Housing Finance Agency  
Sandra Thompson, Deputy Director, Division of Housing Mission and Goals

Comptroller of the Currency  
Grace Dailey, Senior Deputy Comptroller for Bank Supervision Policy and Chief National Bank Examiner

National Credit Union Administration  
Ralph Monaco, Chief Economist

Office of the Independent Member with Insurance Expertise  
Diane Fraser, Senior Policy Advisor

Federal Reserve Bank of New York  
John Williams, President and Chief Executive Officer (by telephone)

Office of Financial Research (OFR)  
Stacey Schreft, Deputy Director for Research and Analysis  
Matthew Reed, Chief Counsel

Federal Insurance Office  
Steven Seitz, Deputy Director

North Carolina Office of the Commissioner of Banks  
Margaret Liu, Senior Vice President and Deputy General Counsel, Conference of State Bank Supervisors

New Jersey Department of Banking & Insurance  
Mark Sagat, Assistant Director, Financial Policy and Legislation, National Association of Insurance Commissioners

Maryland Office of the Attorney General, Securities Division  
Christopher Staley, Counsel, North American Securities Administrators Association

PRESENTERS:

*Federal Reserve Stress Tests*

- *Lisa Ryu, Associate Director, Division of Supervision and Regulation, Federal Reserve*

*Application to the Council Under Section 117 of the Dodd-Frank Act*

- *Bimal Patel, Deputy Assistant Secretary for the Council, Treasury*
- *Stephen Ledbetter, Director of Policy, Office of the Financial Stability Oversight Council, Treasury*
- *Stephen Milligan, Attorney-Advisor, Treasury (available for questions)*

*Update on Annual Reevaluation of Nonbank Financial Company Designation*

- *Stephen Ledbetter, Director of Policy, Office of the Financial Stability Oversight Council, Treasury*

**Executive Session**

The Chairperson called the executive session of the meeting of the Council to order at approximately 4:35 P.M.

The Chairperson began by welcoming Hester Peirce, Commissioner at the SEC; Steven Dreyer, the new Director of the Federal Insurance Office at Treasury; and Stacey Schreft, Deputy Director for Research and Analysis at the OFR, to the meeting. He then outlined the meeting agenda, which had previously been distributed to the members together with other materials. The agenda for the executive session of the meeting included (1) an application to the Council under section 117 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), (2) the Federal Reserve's stress tests, (3) an update on the annual reevaluation of the designation of a nonbank financial company, and (4) a vote on the minutes of the Council's meeting on June 15, 2018.

1. Application to the Council Under Section 117 of the Dodd-Frank Act

The Chairperson then introduced the first agenda item, an application to the Council from ZB, N.A., a subsidiary of Zions Bancorporation, under section 117 of the Dodd-Frank Act. The Chairperson thanked all the agencies that had worked on the Council's analysis of the application. The Chairperson turned to Bimal Patel, Deputy Assistant Secretary for the Council at Treasury, and Stephen Ledbetter, Director of Policy in the Office of the Financial Stability Oversight Council at Treasury.

Under section 117 of the Dodd-Frank Act, if certain entities cease to be bank holding companies, they will be treated as nonbank financial companies subject to Federal Reserve supervision and enhanced prudential standards unless the Council grants an appeal. Mr. Patel stated that the Council had heard a presentation at its previous meeting regarding the staff's preliminary analysis of Zions Bancorporation and ZB, N.A., which had submitted an appeal to the Council under section 117 of the Dodd-Frank Act. Mr. Patel noted that the OCC and the FDIC had recently approved the companies' application for ZB, N.A. to merge with Zions Bancorporation. Mr. Patel also described revisions to the staff's written analysis since the previous Council meeting. He then explained the timeline under section 117 of the Dodd-Frank Act if the Council voted to make a proposed decision regarding the ZB, N.A.'s application to the Council. Mr. Patel stated that if the Council made a proposed decision, the Council would provide its written explanation of the proposed decision to the company. He stated that the Council would also

provide the written proposed decision to the Senate Banking and House Financial Services Committees and publish it online, subject to redactions of confidential information the company had submitted to the Council. Consistent with the requirements under the Dodd-Frank Act, he explained that after the Council's proposed decision, the Council would make a final decision regarding ZB, N.A.'s application to the Council within 60 days unless one of the two Congressional committees indicated within that period that it intended to hold a hearing regarding the Council's proposed decision.

Members of the Council then had a discussion regarding the company, including regarding its size, complexity, derivatives activities, and supervision.

The Chairperson then presented to the Council the following resolution regarding the application of ZB, N.A. to the Council.

*“WHEREAS, section 117 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “DFA”) applies to any entity that (i) was a bank holding company with total consolidated assets of at least \$50 billion as of January 1, 2010, and (ii) received financial assistance under or participated in the Capital Purchase Plan (the “CPP”) established under the Troubled Asset Relief Program authorized by the Emergency Economic Stabilization Act of 2008, and any successor entity to any such entity; and*

*WHEREAS, section 117 of the DFA provides that if any entity subject to such section ceases to be a bank holding company at any time after January 1, 2010, then such entity shall be treated as a nonbank financial company supervised by the Board of Governors of the Federal Reserve System (the “Federal Reserve”), as if the Financial Stability Oversight Council (the “Council”) had made a determination under section 113 of the DFA with respect to that entity; and*

*WHEREAS, section 117 of the DFA provides that an entity may request an opportunity for a written or oral hearing before the Council to appeal its treatment as a nonbank financial company supervised by the Federal Reserve; and*

*WHEREAS, Zions Bancorporation, a Utah corporation, was a bank holding company with total consolidated assets of at least \$50 billion as of January 1, 2010, and received financial assistance under the CPP; and*

*WHEREAS, Zions Bancorporation and ZB, N.A., a national bank and wholly owned subsidiary of Zions Bancorporation, entered into an agreement and plan of merger, dated as of April 5, 2018, pursuant to which Zions Bancorporation will merge with and into ZB, N.A. (the “Merger”); and*

*WHEREAS, the Federal Reserve has determined, in consultation with the Council, that ZB, N.A. would be the successor to Zions Bancorporation under section 117 of the DFA upon the consummation of the Merger; and*

*WHEREAS, ZB, N.A. submitted a request for a written hearing before the Council to appeal its treatment, upon the consummation of the Merger, as a nonbank financial company supervised by*

*the Federal Reserve; and*

*WHEREAS, the Council held a written hearing regarding ZB, N.A.'s appeal under section 117 of the DFA; and*

*WHEREAS, section 117 of the DFA provides that the Council shall submit a report to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives on the proposed decision of the Council regarding an appeal under such section, which report shall include a statement of the basis for the proposed decision of the Council; and*

*WHEREAS, the Council has considered a broad range of information available through existing public and regulatory sources, as well as information submitted to the Council by ZB, N.A.; and*

*WHEREAS, based on their analysis, the staffs of the Council members and their agencies recommend that the Council make a proposed decision to grant the appeal of ZB, N.A.; and*

*WHEREAS, the members of the Council have considered the issues and the record in connection with the following actions.*

*NOW, THEREFORE, BE IT RESOLVED, that, based on the information, considerations, and analysis set forth in the attached "Proposed Decision of the Council Regarding the Appeal by ZB, N.A. Under Section 117 of the Dodd-Frank Act" (the "Proposed Decision"), and on a review of the administrative record, the Council hereby makes a proposed decision to grant the appeal of ZB, N.A.*

*BE IT FURTHER RESOLVED, that the Council has considered and hereby approves the Proposed Decision and authorizes the Proposed Decision to be sent to ZB, N.A.*

*BE IT FURTHER RESOLVED, that the Council hereby authorizes the Proposed Decision, with such redactions of confidential, sensitive, or nonpublic information as the Chairperson or his designee deems appropriate, to be submitted to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Financial Services of the House of Representatives and released to the public.*

*BE IT FURTHER RESOLVED, that the Council hereby delegates authority to the Chairperson, or his designee, to make technical, nonsubstantive, or conforming changes to the text of the Proposed Decision."*

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

## 2. Federal Reserve Stress Tests

The Chairperson then introduced the next agenda item, the Federal Reserve's stress tests. He turned to Lisa Ryu, Associate Director of the Division of Supervision and Regulation at the

Federal Reserve, to provide an overview of the Federal Reserve's recent bank holding company stress-tests, including the Dodd-Frank Act stress tests (DFAST) and the Comprehensive Capital Analysis and Review (CCAR).

Ms. Ryu began by explaining the stress-testing procedures under DFAST and CCAR. She noted that these stress tests are run on the largest bank holding companies each year, and that the Federal Reserve develops independent projections of participating firms' income and losses in stress scenarios. She stated that participating firms submit capital plans that the Federal Reserve may object to on quantitative or qualitative grounds. With respect to the quantitative exercise, she stated that the estimated amount of post-stress capital a firm would have depends on a number of factors, including the firm's starting capital, the amount of losses it would experience under stress, and the firm's capital distributions. With respect to a firm's projected capital distributions, she noted that DFAST assumed dividends at the level from the previous year and no share repurchases, while CCAR applied the firm's capital plans, which typically include proposed distributions and share repurchases. She stated that the Federal Reserve compared the firm's projected post-stress, post-payout capital ratios to regulatory minimums.

Ms. Ryu then described the timeline for the stress tests. She stated that the starting point was the fourth quarter of 2017. She stated that in February 2018, the Federal Reserve published scenarios to be applied in the stress tests, including assumptions for a global market shock and a macroeconomic shock. She stated that participating firms then submitted their capital plans in April 2018. She stated that on June 21, 2018, the Federal Reserve disclosed the DFAST results, which she stated were intended not to determine which firms were above or below regulatory minimums, but instead to compare firms. She stated that firms then received a preliminary result under CCAR, followed by public disclosure of final CCAR assessments on June 28.

She then described the stress test scenarios. She stated that the global market shock scenario was applied to the trading books of six U.S. bank holding companies with large market risk positions. She stated that the Federal Reserve also applied a simplified version of the market shock scenario to certain intermediate holding companies with significant trading activity. She said that the global market shock scenario involved instantaneous moves in approximately 40,000 risk factors, based roughly on the experience in the second half of 2008. She said that the 2018 CCAR scenario included three notable changes from the 2017 scenario: larger shocks to corporate bond and certain sovereign credit-default swap spreads; a rise and steepening in the U.S. yield curve; and U.S. dollar depreciation. She then described the scenario design and variables for the macroeconomic scenario, which applied to all 35 firms in CCAR. She said that compared to the 2017 scenario, the countercyclical features of the 2018 scenario included a larger increase in the unemployment rate; larger asset price declines; a larger and more persistent increase in the corporate bond spread; and a steeper yield curve.

Ms. Ryu then highlighted changes to supervisory projections that benefited or had a negative impact on firms in the stress tests. She noted that beneficial scenario changes included a steeper yield curve (which resulted in higher net interest income) and improved portfolio risk characteristics. With respect to changes in scenario assumptions that negatively impacted firms, she stated that the Tax Cuts and Jobs Act reduced firms' starting capital ratios; wider corporate bond spreads resulted in higher losses on commercial loans; larger home and commercial real

estate price declines resulted in higher losses on real estate loans; and declines in capital ratios were more pronounced at the largest firms.

She then described the aggregate results of the stress tests. In particular, she noted that under the stress test scenarios, aggregate projected pre-provision net revenue was much higher in 2018 than in 2017 because of the changed assumptions regarding the yield curve.

Ms. Ryu then described the effects of the Tax Cuts and Jobs Act, which was enacted in December 2017 and led to a reduction in starting and projected post-stress capital ratios due to a one-time repatriation tax on off-shore earnings and a revaluation of firms' tax assets. She noted that lower corporate tax rates do not benefit firms that experience negative net income before taxes over the stress tests' projection horizon. She also noted that the tax legislation curtailed firms' ability to offset operating losses during the stress tests' projection horizon with taxes that were previously paid. She stated that while the tax law change is expected to have a positive effect on participating firms' after-tax income in the long term, firms had not yet had time to accrue the benefit, so it had reduced the firms' capital ratios as of the end of 2017.

Ms. Ryu then described the DFAST and CCAR results regarding firms' common equity tier 1 capital ratios. She noted that these capital ratios had a lower starting point in the 2018 stress tests than in the 2017 stress tests. She stated that on a post-stress basis, seven firms breached required minimum capital ratios. Of those seven firms, she stated that three received conditional non-objections and six firms had used a one-time downward adjustment in their proposed capital distributions after receiving the Federal Reserve's preliminary CCAR results. She also described the results regarding certain individual bank holding companies under CCAR, and noted that the Federal Reserve had required two firms to limit their distributions to the levels of the previous year.

With respect to the qualitative assessment under the CCAR, she explained that the stress test involves an evaluation of each participating firm's capital-planning processes. She noted that the Federal Reserve had objected to the capital plan from one firm due to deficiencies in the firm's capital-planning processes.

The Chairperson stated that the Federal Reserve had done a thorough analysis regarding the effects of the Tax Cuts and Jobs Act.

### 3. Update on Annual Reevaluation of Nonbank Financial Company Designation

The Chairperson then introduced the next agenda item, an update on the annual reevaluation of a nonbank financial company that the Council had previously designated under section 113 of the Dodd-Frank Act. The Chairperson introduced Stephen Ledbetter, Director of Policy in the Office of the Financial Stability Oversight Council at Treasury. Mr. Ledbetter provided an update regarding several aspects of the preliminary analysis in the Council's annual reevaluation of the company. He also described certain additional information that the company had submitted to the Council. Members of the Council then asked questions and had a discussion, including regarding the anticipated timeline of the Council's review.

4. Resolution Approving the Minutes of the Meeting Held on June 15, 2018

*BE IT RESOLVED, by the Financial Stability Oversight Council (the “Council”), that the minutes attached hereto of the meeting held on June 15, 2018 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.

5. Other Business

The Chairperson then asked J. Christopher Giancarlo, Chairman of the CFTC, to provide a market update. Chairman Giancarlo noted that markets were functioning well, and stated that the CFTC would be conducting an internal cybersecurity exercise the following day with agencies including Treasury, the Federal Reserve and the SEC.

The Chairperson then stated that in recent Congressional testimony he had been asked about the important difference between regulations and agency guidance. He noted that guidance plays an important role but that it is not intended to replace formal rulemaking.

The Chairperson adjourned the meeting at approximately 5:19 P.M.