SEMI-ANNUAL TESTIMONY ON THE FEDERAL RESERVE'S SUPERVISION AND REGULATION OF THE FINANCIAL SYSTEM

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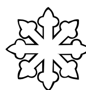

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SEMI-ANNUAL TESTIMONY ON THE FEDERAL RESERVE'S SUPERVISION AND REGULATION OF THE FINANCIAL SYSTEM

Wednesday, November 14, 2018

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:06 a.m., in room 2128, Rayburn House Office Building, Hon. Jeb Hensarling [chairman of the committee] presiding.

Present: Representatives Hensarling, McHenry, Royce, Lucas, Posey, Luetkemeyer, Huizenga, Stivers, Hultgren, Pittenger, Wagner, Barr, Rothfus, Tipton, Williams, Poliquin, Hill, Emmer, Zeldin, Trott, Loudermilk, Mooney, MacArthur, Davidson, Budd, Kustoff, Hollingsworth, Waters, Maloney, Velazquez, Sherman, Meeks, Lynch, Scott, Green, Moore, Perlmutter, Foster, Kildee, Delaney, Beatty, Vargas, Crist, and Kihuen.

Chairman HENSARLING. The committee will come to order.

Without objection, the Chair is authorized to declare a recess of the committee at any time, and all Members will have 5 legislative days within which to submit extraneous materials to the Chair for inclusion in the record.

This hearing is for the purpose of receiving the "Semi-annual Testimony on the Federal Reserve's Supervision and Regulation of the Financial System."

Before beginning my opening statement, don't turn on the clock quite yet. I wish to make a couple of introductory comments.

I have been in Congress for 16 years now and seen a number of elections come and go. Sometimes my party wins; sometimes it loses. It is a little bit more fun when we win. But I want to acknowledge and congratulate my friends on the other side of the aisle for their victory. Although I am retiring and will not be here in the next Congress, I know that not all of my side will acquiesce in your agenda. But please be assured I will do everything today to ensure that there will be an efficient and peaceful transfer of power. We respect the will of the people.

I do not wish to get involved in the inner sanctum of the Democratic Caucus, so I know that we do not yet know who will chair this committee, although I have a pretty good idea. And I would just like to acknowledge the Ranking Member's long time participation, her leadership on this committee, her leadership of the other party. And should that be the will of her caucus, I certainly would congratulate her on her accomplishment. And enjoyed those times.

Wish it would have been a few more where we have managed to work on a bipartisan basis.

But, again, privately I told her that the majority side stands ready and prepared to do everything possible for there to be an efficient and peaceful transfer of power on this committee, and I wish to acknowledge that and, again, congratulate my friends on the other side of the aisle.

I now recognize myself for 3 minutes to give an opening statement.

This morning we welcome back, for his semi-annual testimony, the Honorable Randy Quarles, the Federal Reserve's Vice Chairman for Supervision.

As we know all too well, the Dodd-Frank Act dramatically increased the Fed's power way beyond its traditional monetary policy and responsibilities. Through so-called heightened prudential standards, the Fed can functionally now control the largest financial institutions in our economy, which is most disconcerting. Increased capital and liquidity standards, as long as they are not counterproductive or duplicative, add to stability. Regulatory complexity and micromanagement do not. If not properly tailored and calibrated, both hinder economic growth.

Two weeks ago, the Fed proposed changes to the supervisory requirements for some financial institutions. These proposals are the direct result of the House-led deregulatory and pro-growth provisions contained in the Economic Growth, Regulatory Relief, and Consumer Protection Act. These proposals are a most welcome sign of progress. But to be clear, they do not yet represent success. If they represent the Fed's final offerings, it is pretty thin gruel.

There is clearly a direct connection between sluggish economic growth and the regulatory tsunami we experienced for nearly 2 decades prior to President Trump taking office. Studies, including one by the Mercatus Center, found that regulatory drag on the economy can be attributed to a loss in real income of approximately $13,000 for every American, a staggering figure.

We should note that, while total overall regulatory restrictions have increased by nearly 20 percent since 1997, regulatory restrictions on finance and insurance have increased by a whopping 72 percent. This is why this committee has devoted so much time and attention to legislation, much of it bipartisan, that properly tailors financial regulation.

Certainly, we can never lose site of systemic risk, but neither can we lose site of economic growth which today has led to the lowest unemployment rate in 50 years, the greatest wage increases in a decade, and a resurgence of optimism by both consumers and businesses.

The Vice Chairman previously has expressed his support for a comprehensive evaluation and improvement of the post-crisis regulatory regime. Guided by the principles of transparency, efficiency, and simplicity of regulations, these are indeed laudable principles. I would suggest including one other. The principle that the rule of law not be supplanted by the arbitrary discretion of regulators. That means keeping regulators out of the Boardroom, both literally and figuratively, and kept out of management decisions.

While I am pleased to see the Fed's willingness to better tailor, perform cost benefit analysis, implement prudential regulatory risk adjustments, and propose amendments to the Volcker Rule, each of these as they stand should again be viewed simply as first steps and insufficient to truly propel our economy to sustain 4 percent economic growth.

Vice Chairman Quarles, again, I look forward to your testimony today and exploring with you the importance in assuring each of the Federal Reserve's proposals arrive at results that truly are transparent, efficient, and simple.

The Chair now recognizes the Ranking Member of the committee, the gentlelady from California, for 4 minutes for an opening statement.

Ms. WATERS. Thank you very much, Mr. Chairman. And allow me to take a few minutes to say that I have appreciated the opportunity to work with you. We did not always agree on everything, but I am always amused that the press can't seem to get our relationship right. Sometimes our Members can't even get it right. We have Members from the opposite side of the aisle who say I am the worst thing since you know what, and others who say, well, you know, I get along with her pretty well, and she keeps her word.

And so let me just say this, let's keep them confused. I like it that way. As a matter of fact, the more confused they are, the better I have an opportunity to have some wins.

But I thank you for your offer to be of assistance in transition. And as you know, while it is thought that I would chair this committee, we have not gone through our formal processes yet, and I welcome the opportunity and appreciate it, certainly, to have the support from my colleagues on this side of the aisle to chair this committee.

And I look forward to working with you in any and every way that I can, and other Members of our committee, to make sure that we have the kind of transition that serves the people of this country.

Thank you very much.

So, Mr. Chairman, this is the first hearing since the 2018 midterm election in which voters gave Democrats the majority in the U.S. House of Representatives' next Congress. Of course, that also means changes in committee leadership and in the agenda for the committee.

Given the expressed desire by the American people for a change, I do feel it is appropriate to discuss Dodd-Frank and the harmful effects of the current committee majority to weaken and roll back parts of this law.

These efforts include those by some to weaken capital standards for our largest banks. As we can see in one of the slides before us, capital standards are an effective method to prevent bank failures. Make no mistake, come January in this committee, the days of this committee, weakening regulations and putting our economy, once again, at risk of another financial crisis will come to an end.

Dodd-Frank created the position of Vice Chairman for Supervision at the Fed as one of the several actions in the law to help rectify the Fed's inadequate supervision and enforcement prior to the financial crisis. It is essential that the Fed keeps a watchful

eye on the financial institutions it supervises and makes strong use of its existing enforcement tools to crack down on institutions that break the law.

I must say that I am concerned about proposals the Fed has put forth this year to reduce capital and liquidities requirements for the largest financial institutions, which would weaken strong safeguards established by Dodd-Frank to protect the U.S. economy from another costly financial crisis. That is why, in September, I and 18 other Democratic Members sent a letter to Federal Reserve Board Chairman Powell urging the Fed to maintain strong capital requirements for global systemically important banks.

The current higher capital standards and related regulatory improvements required by Dodd-Frank have strengthened the resiliency of the largest banks as well as the entire financial system without undermining economic growth.

In fact, bank lending to businesses has increased 80 percent since 2010, and banks of all sizes are making record profits. On average, they have made $167 billion in profit annually the last 3 years. As we saw in the last crisis, it is the average hardworking Americans that will suffer the consequences if Washington deregulates Wall Street mega banks again.

I look forward to discussing these and other matters with Vice Chairman Quarles today, and I thank you. And I yield back the remainder of my time.

Chairman HENSARLING. The gentlelady yields back.

The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, the Chairman of the Financial Institutions and Consumer Credit Subcommittee, for 1 minute.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. And welcome, Vice Chairman Quarles. Thank you for joining us today and for the steps you have taken to rightsize regulation.

As we have discussed, it is imperative we take a more practical approach to supervision, one that extends from the top down to each member of your staff in D.C. and to every examiner in the field. On the topic of enhanced Prudential Standards, the Federal Reserve has a strong system in place with a systemic risk score indicator. Your latest proposal goes in a different direction, but I am glad to see you are taking a more risk-based approach to regulation.

More should be done. And I encourage you to remain flexible going forward to revisit arbitrary thresholds and drive Federal Reserve supervision to an even more risk-based approach taken on an institution-by-institution basis. That should include tailoring for U.S. intermediate holding companies of foreign banks and more accommodations for smaller institutions that do not pose any systemic risk.

I thank you for taking on this responsibility, and I yield back to the Chair.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Michigan, Mr. Kildee, the Vice Ranking Member, for 1 minute.

Mr. KILDEE. Thank you, Mr. Chairman.

I first want to say that I appreciate the comments you and the Ranking Member made about this committee and about one an-

other. And on behalf of the confused, I am happy to hear that you are working well together.

I would like to welcome Vice Chairman Quarles. We are looking forward to your testimony.

When you were here in April, I asked about how the Federal Reserve could ensure the effectiveness of the Community Reinvestment Act (CRA), because it is so important that there is equity in how the financial system works. To that end, the recent move by the Office of the Comptroller of the Currency (Office of the Comptroller of the Currency) to update the Community Reinvestment Act is concerning. I would like to hear from you how the Federal Reserve will use its authority to ensure that, in this update, the Community Reinvestment Act is not weakened.

The CRA is important to ensuring credit availability in older industrial communities, in particular, like my hometown of Flint that I know the Members here have heard me discuss in the past. That community is really a troubled community and could benefit greatly from the efforts under the Community Reinvestment Act.

It is important that in a time of reduced supervision of community and regional banks that financial agencies modernize and strengthen the CRA to ensure that banks meet their obligations to provide credit and economic development opportunities to these underserved low- and moderate-income communities.

So thank you for being here. I look forward to your testimony and particularly addressing those questions.

I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, the Chairman of the Capital Markets Subcommittee, for 1 minute.

Mr. HUIZENGA. Thank you, Mr. Chairman. And I echo the—at least the confused part of my colleague from Michigan as well, so I look forward to working with him on trying to unclutter those things.

But earlier this year, Vice Chair Quarles, you mentioned that the Federal Reserve and other regulatory agencies had completed the bulk of the work in this post-crisis regulation. And on February 22 you said, quote, “now is an imminently natural and expected time to step back and assess those efforts. It is our responsibility to ensure that they are working as intended. And given the breadth and complexity of this new body of regulation, it is inevitable that we are available to improve them, especially with the benefit of experience and hindsight,” closed quote.

So moving forward during your appearance in this committee in April, you discussed the Fed’s commitment to tailoring regulations for these smaller financial institutions to ensure that regulations are not overly burdensome and while also ensuring safety and soundness.

Last month, the Federal Reserve voted 3-1 to honor that commitment by streamlining and tailoring those enhanced supervision requirements for both regional and larger banks. These reforms take into consideration banks based on size as well as other risk factors instead of an arbitrary $50 billion threshold regardless of any actual risk to the financial system.

We have also seen positive movement on reforming Section 619, the Volcker Rule, which you called detrimental to our capital markets here in the U.S. I agree with your assessment that Volcker is, quote, "an example of a complex regulation that is not working well," end quote.

It is my hope that regulators, including the Fed, will continue to work toward a more simplified rule that is better tailored to our financial institutions.

And I look forward to working with you. Thank you, and I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

We now again welcome the Vice Chairman for Supervision of the Board of Governors of the Federal Reserve System, Mr. Randy Quarles. He has appeared before our committee before, so needs no introduction. Again, Mr. Quarles, welcome. You are now recognized for 5 minutes for your testimony.

You need to turn on the microphone there. And bring it close to you, please.

There we go.

STATEMENT OF THE HONORABLE RANDAL K. QUARLES

Mr. QUARLES. Does this work?

Chairman HENSARLING. That will work. Thank you.

Mr. QUARLES. Thank you, Chairman.

Chairman Hensarling, Ranking Member Waters, Members of the committee, I appreciate this opportunity to testify on the Federal Reserve's regulation and supervision of the financial system.

My prepared remarks address two main topics: Our efforts to improve regulatory transparency and our progress in making the post-crisis regulatory framework simpler and more efficient.

I am mindful that this semi-annual testimony, like my position as Vice Chairman for Supervision, is grounded in Congress' efforts to strengthen and improve the Nation's regulatory framework following the financial crisis.

This testimony reflects a critical element of those efforts, the desire, and a need for greater transparency. Transparency is part of the foundation of public accountability and a cornerstone of due process, as the Chairman referred to in his remarks this morning. It is also a key to a well-functioning regulatory system and an essential aspect of safety and soundness as well as financial stability.

Transparency provides firms clarity on the letter and spirit of their obligations, it provides supervisors with exposure to a diversity of perspectives, and it provides markets with insight into the condition of regulated firms which fosters market discipline. Transparency increases public confidence in the role of the financial system to support credit, investment, and economic growth.

The Federal Reserve has taken a number of steps since my last testimony to further increase transparency and to provide more information about our supervisory activities to both regulated institutions and to the public.

We recently improved our supervisory rating system for large financial institutions, better aligning our ratings with the supervisory feedback that those firms receive. With our fellow banking agencies, we clarified that supervisory guidance is a tool to en-

hance the transparency of supervisory expectations and should never be the basis of an enforcement action.

And we expect shortly to make final a set of measures to increase visibility into the Board's supervisory stress testing program, including more granular descriptions of our models, more information about the design of our scenarios, and more detail about the outcomes we project.

The report that accompanies my testimony today is another tool to keep Congress and the public informed about our work, about the banking system, and about the role that both play in supporting the broader economy. As the report shows and as my written testimony discusses, the banking sector remains in strong condition in line with strong U.S. economic performance with lending growth, fewer nonperforming loans, and strong overall profitability.

We are, however, very much aware of the dangers of complacency, and our report lists several priority areas of risk we will continue to monitor closely, including cyber and IT risks, that supervise firms of all sizes.

Improving regulatory efficiency is another core element of our current efforts. Tailoring regulation and supervision to risk has been a programmatic goal of Federal Reserve policy for more than 2 decades. The motivations are clear. Supervisory resources are not limitless, and supervision is not costless either to the public or to supervised institutions. Activities and firms that pose the greatest risk should receive the most scrutiny. And where the risk is lower, the regulatory burden should be lower as well.

This principle-guided Congress and the agencies in designing the post-crisis regulatory framework, and it has guided our implementation of the Economic Growth Regulatory Relief and Consumer Protection Act.

On this front, as my written testimony details, we have made substantial progress. Our most significant step came 2 weeks ago when then Board issued two proposals to better align prudential standards with the risk profile of regulated institutions.

These proposals would significantly reduce regulatory compliance requirements for firms in the lowest risk category, including most institutions with between $100 billion and $250 billion in assets. Firms with $250 billion or more in assets or firms with assets between $100 and $250 billion that meet a risk threshold will face reduced liquidity requirements. The proposals would largely maintain existing requirements for the largest and most complex firms.

These new categories draw on our experience administering enhanced prudential requirements and other post-crisis measures, and they move toward a more risk-sensitive nuanced framework where riskier activities and a larger systemic footprint correspond to higher supervisory and regulatory requirements.

I have detailed several other efforts to improve regulatory efficiency in my written testimony including simplifying and tailoring requirements under the Volcker Rule. Our work to improve regulatory efficiency is not done, and we expect to make additional progress in the months ahead on a number of issues. In particular, we are working with our counterparts at the OCC and FDIC (Federal Deposit Insurance Corporation) on a community bank leverage ratio proposal.

I look forward to making progress on that and other efforts and to participating in the committee's oversight of our work.

Thank you, and I look forward to answering your questions.

[The prepared statement of Mr. Quarles can be found on page 48 of the Appendix.]

Chairman HENSARLING. Thank you, Mr. Chairman.

Before yielding to myself for questions, I failed to announce to the committee that we will excuse the witness no later than 1 o'clock today.

I now yield myself 5 minutes for questions.

Again, Vice Chairman Quarles, thank you for your appearance today. I could spend my limited 5 minutes heralding your progress, or I can spend my 5 minutes talking about your shortcomings. I think I will talk about your shortcomings.

So in your last appearance before the committee, you said that the Board of Governors had the authority to jettison the qualitative aspect of CCAR. And what I have noticed is that the qualitative aspect has only fallen off for the lowest of the four tiers that we now operate under. I am disappointed to find this. I don't understand why that qualitative aspect is there. I do not understand why the quantitative aspect of the test is not sufficient.

Can you, please, illuminate to me, if you have the power to jettison, why is it still there?

Mr. QUARLES. So I guess the short answer is we do have the power to jettison, and I believe that the time has come for us to move the qualitative objection into our regular supervisory engagement with firms as opposed to a separate process. We have already done that, as you know, for the smaller firms. There has been significant progress among all the firms with their capital planning measures, with the seriousness and ability that they approach their part of the stress test. And given that, I think that it is appropriate for us to look at that part of the firm's practices, as we look at many other of their practices, as part of our general evaluation of the firm's risk management, of their capital planning, and include that in their overall ratings, but not as a separate process. I think—

Chairman HENSARLING. Well, again, many are still fearful that it is subject to abuse and can intertwine the Fed and management decisions of the banks.

Next, we have spoken about this matter both publicly and privately. Many on this side of the aisle have advocated that we have full transparency with respect to the models of the stress test. And I must admit that I am still somewhat uncertain as to exactly what will be released about these tests. And a foundational principle is the rule of law, and the rule of law works best when you actually know what the law is. We haven't known. It has been a gotcha kind of game.

So can you be more precise? Because after I have seen the proposed rule, I think many people are still unclear what the Fed intends to share with respect to the stress test.

Mr. QUARLES. So I break that into two or three areas. One is transparency about our models. And up to now there has been limited transparency about the models that the Fed uses to evaluate the performance of banks' portfolios in the stress test.

We have proposed being much more granular about what we reveal about those models, and specifically the loss function with respect to different categories of assets and what losses we expect to see in response to particular stresses. Banks will be able to have a better understanding, then, of how their models compare with at least those loss functions of ours.

We have also described in the measures that we have proposed and are making final that this process will continue. We will continue to get more transparent with each iteration of the stress test. So there will be certain models about which more transparency is given in the next cycle. After that, more transparency about certain other aspects of our models.

Another aspect, though, as to which transparency is important, is the design of the scenarios themselves as opposed to the models. That is a more complicated question, and we will be seeking very vigorous input from the public about how we can get, in a practical way, more input on the scenario design. We will be doing that over the course of this coming year.

Chairman HENSARLING. So in your tenure on the Fed, Vice Chairman Quarles, have you concluded that there is a nexus between fixed-income markets, volatility, and illiquidity in the Volcker Rule?

Mr. QUARLES. Yes. So I couldn't quantify it for you. I think that the efforts that various economists have made to quantify that have pointed in different directions. But I think it is inarguable from the experience of market participants.

Chairman HENSARLING. Are you familiar with H.R. 4798, legislation by Mr. Hill and Mr. Foster, bipartisan legislation that passed the House with over 300 votes that would help simplify Volcker by unifying under one rulemaking authority and one regulatory authority? Are you familiar with that legislation?

Mr. QUARLES. I am.

Chairman HENSARLING. Is that something that the Fed, through an interagency agreement, could enter into on its own?

Mr. QUARLES. It would require interagency agreement, but, certainly, the agencies could agree to operate in that fashion.

Chairman HENSARLING. I think it is your term and not mine, but I think that you haven't quite demurkified the Volcker Rule yet.

And I see my time has expired.

The Chair now recognizes the Ranking Member for 5 minutes.

Ms. WATERS. Thank you very much.

Before I get into my question, as you know, California residents have been dealing with some of the most devastating wildfires it has ever seen in the past few years. In communicating with banks you regulate, I believe the Fed and other regulators have previously encouraged flexibility to help customers who have been affected by the disasters.

Do you know of any steps that the Fed is taking to be helpful in this emergency?

Mr. QUARLES. I don't know that we have taken any steps yet, but those are logical things for us to consider.

Ms. WATERS. I would certainly encourage that.

Mr. QUARLES. I will be happy to report to you on what that is we—

Ms. WATERS. Thank you very much.

Vice Chairman Quarles, response to a follow up question from our April hearing, you wrote, and I quote, "the regulatory reforms that were in place in the wake of the financial crisis have helped to make the U.S. financial system stronger and more resilient. As I have stated publicly on several occasions, I believe that the core regulatory reforms, heightened capital, and liquidity standards, stress testing, and resolution planning should be preserved. My focus is not deregulation," end of quote.

Now—and yet the Fed appears to be deregulating the largest banks anyway. Regulatory experts on both sides of the aisle, as well as community banks and others, have criticized several of the Fed's proposals arguing that they will materially reduce bank capital and liquidity reserves for the largest banks.

Former Governor Brainard voted against these proposals noting the recent tailoring proposal would reduce high quality liquid assets held by large banks by about $70 billion.

Former FDIC Chairman Gruenberg and Vice Chair Hoenig opposed the leverage proposal as it would reduce bank capital by more than $120 billion. And just the other day, former Fed Vice Chair Fischer said the deregulation effort is, and I quote, "something that I find extremely worrisome."

What is your response to the many critics that argue that those proposals ignore lessons from the last crisis and will make our financial system less safe?

Mr. QUARLES. So I think that quantitatively those assessments are off the mark. It has been a principle of ours, as we focus on recalibrating, in order to ensure that the incentives that face the financial sector are appropriately lined and that they don't actually increase risk in the sector, that we not reduce the resiliency, including the capital resiliency or the liquidity resiliency of the system. And I think that we have done that.

The various proposals, for example, that affect capital affect it by less than 1 percent, 1 percentage point. One of the criticisms that you pointed out from the FDIC that was with respect to a measure that would reduce the capital in the aggregate system by 4/100 of 1 percent. These are not material amounts.

The liquidity tailoring that we proposed just a couple of weeks ago, for example, I think that that is an implementation of the instruction from Congress that we shall tailor. I think it is a recognition of differing risk. It does not affect the largest banks in the system. And it would reduce the overall high quality liquid assets in the system by 2 to 2–1/2 percent.

There is still trillions of dollars more liquidity in the system than there was before the crisis. We have added $3 trillion of liquidity. Multiples of liquidity that existed before the crisis. And these tailoring proposals, I think, have a significant benefit in reducing compliance burden on less complex and less systemically risky firms. But they do not materially affect the resilience of the system.

Ms. WATERS. Well, that is interesting.

Now, did you work with Governor Brainard to resolve her concerns?

Mr. QUARLES. Yes.

Ms. WATERS. You just made a very strong argument here that there is no significant reduction in capital based on what you are doing.

So you had that conversation with Governor Brainard?

Mr. QUARLES. Absolutely. And we have taken her comments into account. I would be quite confident that she would say we have a robust process.

Ms. WATERS. As you know, I and 18 of my Democratic colleagues wrote the Fed urging you not to weaken capital rules for the globally systemically important banks. And since you are saying that you are not doing that, will you commit to this committee here today that you will not be reducing capital levels at the global systemically important banks in any significant way?

Mr. QUARLES. So it is not our intention. Indeed, it is the opposite of our intention, to affect the total loss-absorbing capacity of the largest firms. Capital is an important part of that, and there is a general framework that affects their resiliency and their loss absorbancy. And I think that we should not be looking to change that. Both Chairman Powell and I have said a number of times we think it is just about right.

Ms. WATERS. Thank you very much.

In the Fed's Supervision and Regulation Report released last week, it was troubling to see the report noted that there are 795 pending supervisory actions against the 12 biggest banks. And most of these supervisory actions relate to shortcomings with the banks' governance and controls, including the lack of compliance with laws and regulations. While the report claims progress has been made since the number of pending supervisory actions is down from about 1,000 in 2013, nearly 800 pending supervisory actions is still a lot. That averages out to 66 pending supervisory actions at each of these mega banks.

Does this data suggest that mega banks are too large to manage? Why or why not?

Mr. QUARLES. So I think that if you look at that information in context over the—since the financial crisis, there has been very material progress in the banks on their capital and liquidity, which is exactly what we would have wanted them to focus on in the first instance. And there has been a dramatic improvement in that.

Now that that is in a much better place, they are turning their resources to addressing questions of governance. And we have seen those MRAs and MRIAs about governance begin to come down. I think we would expect to see them continue to come down at a strong clip given that their resources can now be focused principally on those.

Ms. WATERS. Thank you.

I yield back the balance of my time.

Chairman HENSARLING. The time of the gentlelady has expired.

The Chair now recognizes the gentleman from North Carolina, Mr. McHenry, Vice Chairman of the committee.

Mr. MCHENRY. Thank you, Vice Chair Quarles. Thank you for being here.

So I just want to tick through a couple of these questions about your speech in particular.

So removing the leverage ratio from the stress test capital requirements, is that more or less regulation or just different regulation?

Mr. QUARLES. So I would not view that as a—in any way, as a weakening of regulation. I think that is an appropriate alignment of regulation.

Mr. MCHENRY. In light of the fact that we are so far distant from the financial crisis, and you have economic data to indicate you can make that change?

Mr. QUARLES. Yes. I think that—I think that conceptually there is a difference between—the stress test is a very—is a firm specific risk-based test. The leverage ratio is intended to be nonrisk sensitive and to serve as a backstop. And so when you put that into the stress test, you are really confusing the two things.

Mr. MCHENRY. Which, basically, admits that your stress test isn't as good as you think it is in many respects.

Mr. QUARLES. It is not doing what it was designed to do if you have a post stress—

Mr. MCHENRY. So two more things, just very quickly.

Greater transparency for the stress test process, is that more or less regulation?

Mr. QUARLES. That is just more transparency.

Mr. MCHENRY. OK. More transparency.

And the end game of the public shaming for those that pass or fail stress tests and this public ingredient, is that more or less or just different regulation?

Mr. QUARLES. I think that is refinement. It is not relaxation.

Mr. MCHENRY. So I appreciate your speech. And I think outlining the updates that you are seeking to make post-crisis and now with Dodd-Frank as fully implemented as it is going to be and having this economic data so you can actually shift and make sure that the Fed is doing the right and appropriate thing given the current market.

But one thing in particular. I noticed in your inaugural report on supervision and regulation, a great deal of discussion about the Bank Secrecy Act (BSA) and anti-money laundering (AML) and the compliance and data and information technology pieces of that, which I find really interesting. Can you walk us through the basic challenges banks are facing regarding technology, and particularly partnering with technology companies.

Mr. QUARLES. Well, I think there are both challenges and opportunities. Particularly in this area of Bank Secrecy Act and anti-money laundering compliance, there are a lot of opportunities for banks to use machine learning and big data management that did not exist at the time that our current regulatory framework was put into place that would be of benefit to us as the government, to law enforcement. Would be more efficient use of bank resources.

So I am very supportive of efforts to help the banks do that, which I think they are quite willing to do.

Mr. MCHENRY. So, in admission that banks are struggling to manage data and IT risk as well as this BSA/AML compliance, why not encourage banks to actually partner with technology companies to get ahead of the curve? Why not the Fed lean in on encouraging

that so that we can have banks keep pace with the rest of the technology sector?

Mr. QUARLES. Well, that is an interesting thought. We certainly are trying not to be a disincentive to business decisions that banks might make in that respect. We do want to be sure that where there are those partnerships that we, as regulators and all those responsible for the system, understand what risk there might be in those partnerships. But I don't think there is any reason for us to stand in the way of those partnerships.

Interesting question of whether we should encourage them as to how we ought to effect those business decisions of the firms. But certainly, at the very least, we should not discourage them.

Mr. MCHENRY. Right. But there is a mixed message here.

So you have Governor Brainard discouraging banks and partnering with innovation companies and the admission that with AI and the technology sector moving dramatically forward. And this dissident piece of information, or dissident voices in the Fed around technology, it seems like, for banks, it is damned if you do, damned if you don't, right? That the Fed will take a harsh look at new technology.

But their consumers, my constituents, their customers are desirous of the best technology and that technology ensuring these institutions are safe and sound. So I think you have to do better in encouraging the use of technology, or we are going to have a riskier banking sector.

I yield back. Thank you.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentlelady from New York, Mrs. Maloney, Ranking Member on our Capital Markets Subcommittee.

Mrs. MALONEY. Thank you, Mr. Chairman, and Ranking Member Waters. And thank you, Vice Chairman Randal Quarles, for your public service.

Very painful to many of us is the memory of a financial crisis where we lost $13 trillion of household wealth, 9 million jobs, millions of homes, and unemployment was at 10 percent. And I am proud of the way that we bounded back as a country. Our economy is getting stronger every day. Bank profits are now higher than they have ever been, $173 billion, I believe the highest ever.

So we bounded back. And it is good that the banks are working and that the economy is humming. But I am very concerned about any effort to roll back the stress test that, in many ways, has guaranteed this financial success in safety and soundness in our banking system.

So my first question is, in the Fed's recent tailoring proposal, the Fed proposed to give regulatory relief to banks that are over $250 billion in assets, the so-called Category 3 banks. And one of the main ways the Fed is proposing to give these banks relief is by allowing them to hold less liquidity by scaling back two liquidity rules for the Category 3 banks. So I am concerned about this. If the system is working, why do we want to deregulate?

First, what evidence do you have that Category 3 banks are currently holding too much liquidity? And second, seeing as one of the liquidity rules that the Fed is proposing to scale back has not even been finalized yet, how did you conclude that a regulation that

hasn't even been implemented was already too burdensome for the banks for Category 3?

Mr. QUARLES. So to begin, the first point, I guess I would make in response to that question, is that we have, in thinking about our tailoring proposals for banks of any size and any level of complexity, had, as a first principle, that we do not want to affect the resiliency of the system. We are not seeking to relax or impair the resiliency of the system, including overall liquidity.

And the quantitative consequence of our liquidity proposals is, as I had said to Ranking Member Waters, our expectation is that, depending on where we finally calibrate that liquidity tailoring, it would be between 2 and 2–1/2 percent of the overall liquidity in the system.

So I don't think that we have, again, in any material way effected that liquidity. There has been a huge increase in liquidity in the system since before the crises. Trillions of dollars. This is a small reduction.

But I do think that tailoring is something that applies across the continuum of banks. The legislation requires us now to tailor. The language in Section 1652a was changed from we may tailor to we shall tailor.

And in thinking about appropriate tailoring, I do think that liquidity for that category of banks is somewhere we could do it. And we saw that we could do it in a way that would be a reduction of burden and implementation of congressional intent but not an impairment of resiliency of the system.

Mrs. MALONEY. Well, in your speech last Friday, you said that you wanted to remove the so-called stress leverage buffer from the Fed's proposed overhaul of the stress test regime. But the leverage buffer was intended to replace the requirement for banks to meet a minimum leverage ratio even in a period of stress. And so my question is: By removing the leverage buffer, wouldn't you be saying that banks are—no longer have to meet any leverage environment in the stress test?

Mr. QUARLES. Well, banks would still be subject to a leverage requirement, so I may have—I certainly don't want to have confused that issue.

Mrs. MALONEY. But not in the stress test. I am talking about the stress test.

Mr. QUARLES. That's right, because—

Mrs. MALONEY. In the stress steps there would still be a leverage requirement?

Mr. QUARLES. No, because the stress test is one thing, and a leverage requirement is another. The leverage requirement is designed to be a backstop to our risk-based measures.

Mrs. MALONEY. Right. So why take the backstop out?

Mr. QUARLES. But we are not. So the backstop would remain. The leverage ratio would still be there as a backstop. It is just that in the risk stress test, the risk measures would be risk measures and the leverage measures would be leverage measures.

Mrs. MALONEY. I have to say that I find that troubling. The leverage ratio has been the binding capital requirement for all of our largest banks in the past two stress tests. So removing this lever-

age buffer could significantly weaken the stress test, in my view, and I am opposed to it.

Chairman HENSARLING. The time of the gentlelady has expired.

The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, Chairman of our Financial Institutions Subcommittee.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

Vice Chairman Quarles, again, thank you for being here.

As you know, this committee passed a bill introduced by Mr. Lucas to require financial regulators to recognize the exposure-reducing nature of client margin for clear derivatives. The Fed's SA-CCAR proposal recognizes that client margin for clear derivatives reduces the bank's exposure, yet the Federal Reserve chose to propose a rule without recognition of that fact.

This is a priority for me and for other Members of this committee. And I hope you will work on this issue. I think that, if I am not mistaken, Mr. Lucas has some questions with regard to that, so I won't go into detail on it. But this is a concern I just want to put on your radar.

My first question deals with their inter-affiliate margin requirements. This a conversation we had recently. And I appreciate you taking my call and discussing it with me.

As you know, I am a firm believer in capital requirements. But I think it is important those requirements make sense and don't necessarily tie up capital. We have a system in place that requires firms to post margin multiple times on the same transaction. The amount of unnecessary locked-up capital is even more concerning when you consider that U.S. financial institutions are isolated.

European and Asian regulators do not similarly propose initial margin, as you well know. Nor does the CFTC (Commodity Futures Trading Commission) for non-bank entities. To that extent, I think it is important that you look at this issue. And along that line, I guess the question is, do you believe this initial margin is still warranted? Would you agree that the policy needs to be revisited? And would you commit to making this a regulatory priority in reducing or eliminating inter-affiliate initial margin?

Mr. QUARLES. So as we have discussed, and as you note, we are isolated in doing this. No other country has that treatment of inter-affiliate margin. The CFTC doesn't have that treatment. I do think that it is something that we have to look at closely. We are still having discussions internally at the Federal Reserve. But for me it is a priority to address that question, and I personally share your view.

The Fed, as you know, has rules, Section 23 of the Federal Reserve Act and Regulation W that implements that deal with affiliate transactions and protecting against exposures that are created by affiliate transactions. And it may be—may well be possible that that which has existed for decades, that framework, may be entirely satisfactory and allow us to move into compliance with the rest of the world.

Mr. LUETKEMEYER. One of the reasons for the question, as you know, is to get you on record here so we can begin the discussion so we can continue to follow up on it. And we appreciate your response.

Thank you very much.

With regards to CECL (current expected credit loss), which is, to me—I am extremely concerned about it. This rule fundamentally changes accounting practice of banks, especially small banks. And I think we had—that can have, I think, serious consequences.

We have roughly 5,200 banks altogether, and there is roughly probably over 5,000 of them that are smaller banks. Most of those probably are privately owned, not publicly owned. And yet this is what this standard is supposed to be focusing on is investment—the ability of investors to better see a picture of the financial institution's standing, which really makes no sense when you have a bank that is privately held.

This—again, I just can't get my head wrapped around it. So I guess my question to you is seeing the impact on most of our banks, would be, I think, a negative, what is your concern with it? Do you have any concerns with it? Where do you think we need to go with this? Are you willing to work with us? Or do you think it is a great thing? And I want to move on.

Mr. QUARLES. Well, I am always in favor of measures that make more transparent the position of any financial institution. But I do agree with you that the implications of CECL for small firms, for large firms are not currently deeply understood. And we need to have time to understand them.

So we have proposed a phased-in implementation of CECL in how that affects—how that works with our regulatory capital regime. And we think that will give us time to see how it is working in operation before it gets plugged into the regulatory capital regime—allow us to see whether there are any changes. I don't know that there are. Continue to work with you and the committee on questions of what CECL implementation means.

For the larger firms, I think that—it is a little interesting. Those firms that are affected by the stress test, CECL could actually be a wash, because to the extent it means a larger reserve at the outset of the period of stress, then you will chew through that reserve before you chew through other things in the stress test, and it can be a one-to-one offset.

Mr. LUETKEMEYER. I see some ramifications of this that, here we have increased costs for doing business for banks. And when they increase costs, they have one of two things that they do. Either they pass those costs along to the consumer, or they do away with certain services that cost them this extra money, as we have seen with small-dollar lending, as we have seen with home mortgages.

So are we going to restrict the ability of banks to offer services? When that happens, you are talking about hurting the CRA regulation, our compliance.

And so to me it has lots and lots of ramifications. I am very concerned about it, and we are certainly going to follow up.

Thank you very much. I yield back.

Mr. QUARLES. Thank you.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from New York, Ms. Velazquez.

Ms. VELAZQUEZ. Thank you, Mr. Chairman.

Vice Chairman Quarles, when you last came here before this committee in April, you and I spoke about the Community Reinvestment Act. During our conversation, you told me that you expect there to be a joint rulemaking between the OCC, the Fed, and the FDIC to modernize the CRA.

When the OCC released its ANPR (advanced notice of proposed rulemaking) in August, the Fed and the FDIC choose not to sign on. Why was there not a joint rulemaking like you originally anticipated? And what can you tell us about the Fed's decision not to sign on?

Mr. QUARLES. Well, actually, I do still expect there to be a joint rulemaking. The OCC has come out with an advanced notice of proposed rulemaking, a series of questions. And both the Fed and the FDIC—well, I guess I shouldn't speak for the FDIC. But we did participate in the crafting of that ANPR, and we certainly will work with the OCC in developing an NPR post that is—

Ms. VELAZQUEZ. And that includes FDIC?

Mr. QUARLES. Well, I can't speak for the FDIC. But we are working together on it. We have been, and so I expect that to continue.

It has been a joint process. The OCC did go out singly with its ANPR, but we are encouraging people to comment on the ANPR. We are receiving comments, although we haven't signed on to the ANPR, people who are commenting on the OCC's ANPR are sending in those comments to us effectively. And we will work together on further CRA work with the OCC.

Ms. VELAZQUEZ. Would that mean that you will not release your own proposal? It will be a joint rulemaking?

Mr. QUARLES. That is my expectation currently, yes. We are all expecting that that would be a joint rulemaking.

Ms. VELAZQUEZ. In public remarks made earlier this year, Comptroller Otting stated that the OCC will be working with the FDIC and the Fed to update and improve the BSA/AML's rules and processes.

What is the current state of that joint effort, and what are the prospects for reform?

Mr. QUARLES. Well, I think the prospects for reform are good. Again, we are working together. The banking agencies together with Treasury and FinCEN have a very active process in reviewing both the banking agencies' examination and enforcement practices with respect to BSA/AML as well as Treasury and FinCEN's rulemaking on BSA/AML. And I think we will see some material benefit out of that.

Ms. VELAZQUEZ. Sure.

Going back to your exchange with Congressman McHenry, I would like to ask you, based on the report, the Fed's Supervision and Regulation Report on those areas where it discusses witnesses such as governance and controls, including BSA/AML programs internal audit functions, IT risk management, and cybersecurity, what can you tell us about the results of that study? And do you find them disturbing?

Mr. QUARLES. Well, as I indicated, there is a lot to be done that the banks still need to do with respect to risk management and some of these governance and controls issues. But I don't find—I don't find it surprising that there is still much to be done. The

banks are making progress on addressing our supervisory expectations in those areas. They did devote, appropriately and with our encouragement, the most resources initially to capital and liquidity ensuring that those foundational aspects were taken care of to resolution issues, enormous amounts of resources devoted to resolution.

So now that we move into these governance matters, we are seeing those come down. We are obviously not complacent about it. We are very engaged with the banks on it. But it is not as though there is foot dragging or impossible management problems at these firms at all, it is a question of prioritization and things moving about, I think as we all would have expected.

Ms. VELAZQUEZ. Do you think that better coordination between foreign banks and the Fed is needed?

Mr. QUARLES. We have pretty good—I would say that our—again, our supervision of foreign banks is not deficient. We have good cooperation with their home country supervisors, which is important in understanding their overall positions.

The foreign banks, because we only recently imposed the so-called intermediate holding company requirement, which requires them to organize their non-banking activities in a way that applies many of these Fed rules, that is fairly recent. And so they haven't had as much experience as the domestic banks, but I think they are getting there.

Ms. VELAZQUEZ. Thank you.

I yield back.

Chairman HENSARLING. The time of the gentlelady has expired.

The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, Chairman of our Capital Markets Subcommittee.

Mr. HUIZENGA. Thank you, Mr. Chairman. And Chair Quarles, thank you. I appreciate you being here.

I want to touch on two things: Volcker Rule and then covered funds.

Needless to say, many people believe that the Volcker Rule was a solution in search of a problem and that the implementation of it—I have deep concerns about how the implementation of the rule has been affecting U.S. financial institutions and ultimately liquidity in the market. We have seen it—definitely have seen a decline in the market liquidity while not really experiencing actual market stability that was promised, right?

So earlier this year, as part of 2155, the banking regulatory relief bill that was passed and signed into law, a provision was included to relieve banks under $10 billion in total assets from having to comply with the Volcker Rule, which I think was absolutely on target. And even though the Volcker Rule is part of the Bank Holding Company Act, it also applies to industrial banks. And that is where I am concerned, because it is another type of banking charter that has its own statutory framework and a separate set of rules.

But these industrial banks are used by a variety of different companies, and where it is actually oftentimes a small part of it. Michigan, we have an energy company that has a small ILC (industrial loan company). It is the larger companies that might have this as a portion of what they do. And the overall consolidation of the industry, really, I think has made these even more important.

So I am aware that some of these banks have not been able to take advantage of the relief that we have provided, because under a total consolidated asset test, the parent companies exceed the thresholds themselves.

So the intent of making sure that these smaller industrial banks have the same relief as community banks and these other institutions below $10 billion hasn't actually come into effect. So you are now burdening these companies with still having to comply with Volcker.

So I am curious, what are your plans to address this? Do you think—first of all, do you think this makes sense? Do you see that there is a problem there? And then what are we going to be doing to change that? And I just want to encourage you to do so, but I would like to have some concrete steps on how that might happen.

Mr. QUARLES. Sure. I appreciate that.

So I do think that is an issue. What you have described is an issue. We are working through how to address it given the restrictions of the law and the terms of the law. But I do think that it is something that—it is an anomaly. Related to that, though, are questions of control. And one of the—so there is the question of the application of the Volcker Rule to these ILCs, but there are also questions of interpretations of control around the ILCs. I have heard that from some people who are concerned about this issue. And we do have a separate project that is underway at the Federal Reserve to rationalize and make more transparent some of these control rules. I think the two together—I don't know what the answer is as we talk about here, but I think we should continue to talk about it. And we are thinking about this question in both of those contexts.

Mr. HUIZENGA. And do you believe that you currently are able to address this? Or do we need to address this legislatively for clarity?

Mr. QUARLES. I don't know the answer to that question today, but I'll get back to you with—

Mr. HUIZENGA. Let's make sure we continue to work on that.

And real quickly in the last minute here. Covered funds. Working together Chairman Hensarling and Subcommittee Chairman Luetkemeyer and I wrote a letter to—including to Chair Powell, the various regulators outlining our concerns with that. And without objection, Mr. Chair, I would like submit that letter to the record.

Chairman HENSARLING. Without objection.

Mr. HUIZENGA. Thank you to my friend from Colorado. You may be jumping the gun a little bit, but the—I am eating into my own time here.

So while the—we stated—or, I am sorry, Chairman Powell, when he was before the committee, stated that the banks' engagement in covered funds does not pose safety and soundness concerns and that our banks are able to invest in any number of companies—both credit and equity investments via their balance sheets.

Can you explain to me the rationale that would exist for allowing banks to make an investment on their balance sheet while preventing it in a fund structure. And wouldn't doing it through a fund structure make the investment even safer because the investment has more investors than just one bank alone?

Mr. QUARLES. No. I think that is a very sensible way to think about it. It would be, and we have in our Volcker Rule proposal, as you know, we have requested questions, asked for comments on how to treat covered funds, and that is an important part of what the next step will be.

Mr. HUIZENGA. Hopefully we have your commitment you are going to continue to work on the covered funds and address this. Thank you.

And, Mr. Chairman, I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from California, Mr. Sherman.

Mr. SHERMAN. I wonder if we could put up the charts that we have arranged. Yes, Mr. Quarles, behind you are going to be two charts during the next 5 minutes. I have a friend who I don't take theological advice from very often who claims that there is a special place in hell for those who used statistics that are not inflation adjusted. The Fed has now hit its 2-percent inflation target, and this chart shows that if you use the unadjusted phony statistics, you can show that, from the first quarter of this Administration, we have seen an increase in wages for those with high school degrees or diplomas. But if you inflation adjust the statistics and use the real numbers, the real wage for high school graduates has slightly declined over this Administration. We will also see a chart later about our trade deficit with China, which has increased over the last 7 months.

Now for some bipartisan questions.

In recent years, there has been a growing number of cybercriminals targeting real estate transactions using wire fraud to steal home buyers' down payments. Cybercriminals do this by hacking into the email accounts of home buyers, real estate agents, lenders, et cetera, and send false wire instructions to home buyers to steal their downpayment. Under these spoofing email cybercrimes, consumers have been scammed out of about $12 billion since 2013, and the FBI says that these scams are up sharply.

Mr. Quarles, you may know that fraud in real estate transactions is a growing problem, and much of it is done through wire transfers. These scams are effective because there is no requirement that the name of the individual intended to receive a wire transfer actually matches the name on the account that the funds are deposited into. Has the Federal Reserve considered requiring banks and other financial institutions to apply payee matching when initiating a wire transfer?

Mr. QUARLES. So we have not implemented that, but we are considering that. We have a number of active efforts within the payment system group at the Fed to address questions related to wire transfer.

Mr. SHERMAN. I hope you would go back and light a fire under them because this is important.

Mr. QUARLES. Absolutely.

Mr. SHERMAN. We have provided in legislation significant relief to small community banks, but for that to work, you have to define the term, "tangible equity capital." When are you going to provide a definition?

Mr. QUARLES. Soon.

Mr. SHERMAN. Very soon would be the better answer.

Mr. QUARLES. So we are working on that as part of our implementation.

Mr. SHERMAN. OK. Another similar question, Congress provided the Federal Reserve with clear instructions to remove regional banks from the enhanced prudential standards unless they designated that bank as systemically risky. For that to work you need to address capital and liquidity rules in a comprehensive manner. You have provided clear liquidity rules for the large banks. When will you propose new capital rules for regional lenders?

Mr. QUARLES. For the smaller banks, we have. Our proposal—

Mr. SHERMAN. But my focus here is on the regional banks.

Mr. QUARLES. And for the whole continuum, our tailoring proposal at the end of October was intended at least—and so, if it is deficient, please let us know—but it was intended to create a framework, if we will, for all banks as to when enhanced prudential standards would apply to them.

Mr. SHERMAN. In the questions for the record, I will detail the areas that still need to be fleshed out for these regulations to be effective.

Mr. QUARLES. I appreciate that.

Mr. SHERMAN. And, finally, I think you need to codify the activities-based approach to nonbank SIFI (systemically important financial institution) designations, and I wonder whether that is on track.

Mr. QUARLES. So the FSOC (Financial Stability Oversight Council) is very much engaged in a pretty robust process in thinking about how to implement an activities-based approach.

Mr. SHERMAN. Do you think they will get there soon?

Mr. QUARLES. I do, yes. I both think they will get there soon and that the process will be well done. It is a tricky thing to do, but I think that it will be done well.

Mr. SHERMAN. So summarize your answers to my questions with the word "soon."

Mr. QUARLES. Soon.

Mr. SHERMAN. Thank you.

Chairman HENSARLING. The time of the gentleman is expired.

The Chair now recognizes the gentleman from Kentucky, Mr. Barr, Chairman of our Monetary Policy and Trade Subcommittee.

Mr. BARR. Thank you, Governor Quarles, for returning to the committee as required by the Dodd-Frank law, and I appreciate your work, and I appreciate your commitment to reviewing and correcting some of these perhaps well-intentioned regulations but obviously overly burdensome regulations that are making it more expensive for Americans to access the capital they need to continue to grow our economy. There was no doubt that, in the wake of the financial crisis, some of these financial rules were needed to change, but in some instances, Congress and the Federal Reserve overcorrected, as you have acknowledged. Your efforts and those of others at the Federal Reserve fixing these problems are to be applauded, and we appreciate that work. I do want to focus on the October 31 tailoring proposal. And in particular one of the areas where we saw maybe an overcorrection was the impact that these

new post-Dodd-Frank regulations were having on small business lending by banks. We have seen that, because of the strict capital liquidity requirements that were put into place, we have seen a pretty significant decline in small business lending. C&I lending maybe remained healthy, but what we saw was that loans less than a million dollars dropped from 2–1/2 percent of GDP in 2001 to 1.7 percent in 2017, and such loans make up a smaller proportion of total bank assets, dropping from 4 percent in 2001 to 2.1 percent in 2016.

So, given that small business formation and access—small business access to capital is really critical, can you tell us what you anticipate the new proposals, the impact of the new proposals, tailoring, could have on banks' capacity for small business lending?

Mr. QUARLES. So I can't quantify that for you today, but we would be happy to try to do that so you have some quantification. I think that it is unarguable, however, that small business lending, a particular source of small business lending comes from smaller and regional banks and that, to the extent that we have subjected those institutions to levels of regulation that are more appropriate for much larger institutions, you are going to have a disproportionate effect on small business lending, and so our proposal should address that.

Mr. BARR. Is your tailoring proposal enough to revive small business lending back to levels that we saw previously?

Mr. QUARLES. There are a number of reasons for the decline in small business lending or the effects on small business lending, so I wouldn't want to say that these tailoring proposals—they will have an effect. Will they be enough to completely address the issue? I wouldn't want to say here today.

Mr. BARR. Let me move on to the absence in the tailoring proposal to address foreign banking organizations. As you know, international banks represent approximately 20 percent of banking assets and one third of all loans to businesses in the United States. Obviously, they contribute in major ways to U.S. economic growth. International banks comprise two of the top three commercial agricultural lenders in the United States and as the former acting comptroller of the currency noted, international banks, and I am quoting here, are also an important potential source of stability to our economy. In times of financial stress in the United States, the global operations of international banks may well be healthy and stable.

As you know, in recent years, international banks have been subjected to duplicative and overlapping regulations. You responded to a letter to several Members of Congress. Recently, in a letter dated October 26, you noted that the Board recognizes the important role of FBOs in the U.S. financial sector. You said that the Board's enhanced prudential standards generally treat an intermediate holding company of a foreign banking organization similarly. But is that the case and are you all in your proposal to level the playing field—tell us a little bit more about your intentions in that regard because we want to be able to, number one, facilitate that foreign direct investment and not disadvantage the U.S. in very competitive global marketplace.

Mr. QUARLES. So I completely agree with all of the points you made about the importance of foreign banks to our domestic economy, and that has been true for decades, and it is, therefore, very much in our interest to ensure that their participation is facilitated.

We—but they are different cats, so they aren't identical to domestic banks, and we are going to go through a process where we consider how to ensure we have a level playing field but that takes account of their differences.

Mr. BARR. Thank you.

I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from New York, Mr. Meeks.

Mr. MEEKS. Thank you, Mr. Chairman.

First, I would like to submit for the record a letter that I sent with a number of my Congressional Black Caucus colleagues, as well as a letter from Senator Van Hollen, urging the Fed to move quickly on its faster payment initiative.

Chairman HENSARLING. Without objection.

Mr. MEEKS. Thank you.

Mr. Vice Chairman, the Federal Reserve recently solicited comments on its proper role in implementing a faster payment system in the United States. Given the potential consumer benefits, I urge the Fed move more quickly on this initiative, but I am also sympathetic though to some concerns that some of the consumer groups and advocates brought to my attention who argue that faster payments may also mean faster fraud, especially for vulnerable individuals like our seniors. So my question to you is, from a supervisory standpoint, what do you believe the Fed's proper role will be in preventing fraud within a faster payments regime?

Mr. QUARLES. So, obviously, it is up to the Federal Reserve to enforce the antifraud laws on those institutions that we supervise, that we have the legal authority to do that for. We have been very active in doing that and will continue to do so, whether those payments are being affected through the traditional payment system or through a new technologically advanced payment system.

Mr. MEEKS. Let me also, one of the issues that—I want to move with the time that I have. The OCC has issued an ANPR on modernizing CRA, and the agency solicited opinions on the concept of a more metric-based system for CRA ratings. And while consistency in CRA ratings is important, there are important qualitative factors that CRA examiners consider that cannot fully be measured by a formula ratio. Would you concur with that?

Mr. QUARLES. I think those are important considerations.

Mr. MEEKS. So, in fairly assessing the qualitative factors required at a certain level of an examiner's discretion, a purely metric-based CRA rating system, in fact, can tie the hands of examiners. Are you concerned with the CRA's proposals that are overly prescriptive and can limit examiner discretion when it comes to assessing the innovativeness and responsiveness of CRA lending?

Mr. QUARLES. So I do think we need to think carefully about how to ensure that we have uniform treatment as well as how to ensure that we have a real reinvigoration of the CRA. My concern with re-

spect to the current administration of the CRA is, as I think I said in my last appearance here, it has become a little ossified and formulaic. And communities themselves will benefit if we can be more creative about that.

At the same time, we do also want to ensure that we have regulatory measures that treat similar banks similarly and that we have a framework that does that.

Mr. MEEKS. And, last, Mr. Vice Chair, we have been working very closely because we know I am seeing a lot of banking deserts coming up, and the cure to that is to make sure we can keep small and community banks in communities and make sure that they are able to afford it. And in my conversations with a few of them, BSA becomes very costly, and I am concerned, therefore, about the impact that these costs may have on these banks and credit unions also, which have higher compliance costs relative to their larger competitors, and I know that the Fed has sent some recent guidance on how the banks can share BSA, but to a lot, it is still not clear. Do you think the Fed can do more to—as far as a guide to the institutions? Because they are nervous. They want to make sure it is clear to them, especially the smaller banks with less exposure on how to lawfully share a BSA office.

Mr. QUARLES. So we do intend having taken that joint action with the other regulators and allowing sharing of resources with suspected BSA/AML, we will be engaged with our supervisors and with the banks to ensure that they understand what it is that they can do, but we are very supportive of efforts to both take advantage of the cost reductions that come from using new technologies and reducing the costs in general of effective BSA/AML compliance.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Pennsylvania, Mr. Rothfus.

Mr. ROTHFUS. Thank you, Mr. Chairman.

Vice Chairman Quarles, one of the key provisions in S. 2155 that was intended to help spur economic growth is the Home Owners Loan Act (HOLA) flexibility provision, Section 206, that originated with legislation I introduced. That section gives institutions chartered under HOLA greater flexibility in meeting the changing borrowing needs of the communities that they serve. I want to commend Comptroller Otting and his staff for moving quickly on regulations to implement this provision with a proposed rule already published and comments due next week. I also understand that the Federal Reserve is considering what issues, if any, may exist when institutions that are organized as savings and loan holding companies exercise the provisions under Section 206. I would hope that both the OCC and the Fed would adhere as closely as possible to the congressional intent to provide meaningful flexibility to HOLA-chartered institutions, including S&L holding companies, while avoiding unnecessary costs or legal complications that would impede the provision of needed services to their communities. To that end, I would urge the staff at the Federal Reserve to work closely with the OCC staff to ensure a coordinated approach that provides the flexibility intended by the statutory provision. Can you share any detail on the issues the Board is reviewing and how you might address them?

Mr. QUARLES. Well, we are working closely with the OCC on that question. We haven't come to detailed views as to how we will implement that provision, but we certainly intend to hew to the congressional intent.

Mr. ROTHFUS. I appreciate that and look forward to following up. In your testimony, you highlighted the importance of improving regulatory inefficiency. You also wrote that, quote, "supervisory resources are not limitless, and supervision is not costless either to the public or to supervised institutions." I certainly agree with this view. That is why I introduced the legislation, H.R. 5059 with Representative Beatty, to address inefficiencies in the supervision of insurance savings and loan holding companies (ISLHCs). As you may know, this bill passed the House of Representatives by a voice vote earlier this year. Unfortunately, the regulatory inefficiency continues to drive ISLHCs out of business of banking. Though your support on Fed supervision and regulation claims that the Fed has worked closely with departments of insurance and the National Association of Insurance Commissioners to tailor supervision of ISLHCs, I have not seen much evidence of this. Are you concerned that ISLHCs continue to debank?

Mr. QUARLES. It certainly isn't the objective of our supervision to have that effect. There is no reason that it should, and we need to continue to work at the Fed to ensure that our, again, as part of our general tailoring that our supervisory engagement with these firms is appropriate to the actual size—

Mr. ROTHFUS. Are there any specific actions that can be taken to that end to ensure that these institutions aren't debanking?

Mr. QUARLES. Other than ensuring again that our supervisory engagement is appropriate, I don't think that there are specific changes, but I am aware of issues that we have had that we are trying to address. They aren't regulatory or quantitative. They are more in the nature of qualitative, and we are trying to address them.

Mr. ROTHFUS. I appreciate your awareness of the issue and look forward to following up.

S. 2155 contains Section 402(b) the provision that exempted cash deposits placed at central banks by custody banks from the supplemental leverage ratio. The provision was not only part of S. 2155 but also passed the Financial Services Committee as H.R. 2121, the Pension Endowment and Mutual Fund Access to Banking Act, by unanimous vote. Given the strong support for this provision, can you give us an update on when Section 402(b) will be implemented?

Mr. QUARLES. An exact date I can't give you, but we do expect that to be soon.

Mr. ROTHFUS. Any update on the Federal Reserve Board's enhanced supplemental leverage ratio proposal and how that proposal would work with section 402(b)?

Mr. QUARLES. So what we need to do in thinking about our proposal with respect to the enhanced supplemental leverage ratio is to ensure that if we implement that, that there isn't double counting. So there is a statutory provision that affects some firms. Our provision would have affected all firms. If we simply implement that without any adjustment, then you would have some double counting for the firms that are covered by the congressional action.

That would not be our intention. That is also a little tricky to figure out. My expectation would be that we will first implement the clear congressional instruction and then work on refining ours to address that double counting issue.

Mr. ROTHFUS. Thank you.

I appreciate that, and I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Massachusetts, Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman, and thank you, Vice Chairman. Let me follow up on the gentleman from Pennsylvania's question there regarding the bill we passed recently. Our version was 2121. The Senate bill was 2155. And the idea was that we would reduce the—we would count—we would exempt deposits made by custodial banks when they park their money at the Fed, which you got 60 votes in this committee, which is highly unusual, and we are still waiting for that to happen. So I just want to register my support for Mr. Rothfus' comments and urge you to be diligent in making sure that that happens.

Mr. QUARLES. So I appreciate that, and while I would only offer the—behind my "soon" with respect to implementation that on the tailoring proposal that was the heart of EGRRCPA, I do think that our implementing—our proposal to implement that was done with a speed that was almost unprecedented in the history of the Fed. So "soon" is not a way of putting things off but of generally saying I do think that will be implemented soon.

Mr. LYNCH. All right. Fair enough. Let me ask you, do you think there are any nonbank systemically important financial institutions in the country?

Let me give you a for-instance. OK. So, for instance, Prudential, largest insurance company in the United States, approaching a trillion dollars in assets, FSOC recently dedesignated them as a SIFI, and yet when you look at Prudential, they hadn't undertaken any large-scale restructuring since their SIFI designation. In fact, they got considerably larger. I think they have grown 17 percent in the last 5 years. And in its dedesignation, FSOC found that Prudential had not significantly increased its total market exposure investment—I am sorry, did not significantly decrease its total market exposure. They didn't decrease their investment portfolio or market share, and they didn't address issues of resolvability in case something went wrong. And yet they were dedesignated. And I am just curious what is the thinking there?

Mr. QUARLES. Well—

Mr. LYNCH. Let me ask you, what I see is—because Prudential did little to nothing except get bigger and more complicated, more complex, but FSOC changed. FSOC changed, the people on FSOC changed, and I think that is the difference here. That is the difference, and that is not good for America. That is not good for the United States' economic system, and you can tell me why I am wrong, if you will.

Mr. QUARLES. So, one of the principles that we have been talking about here is that it is not merely size, but that there are a variety of other factors that need to be taken into account in determining the systemic—

Mr. LYNCH. Let me just say that Fortune magazine says that Prudential Insurance Company is changing the world. They are interconnected. They are complex. They are huge, like I say, approaching a trillion dollars in assets. And if they are not a systemically important financial institution—nonbank, but they certainly have the exposure, the market share, all the things that made us designate it to begin with, and, not unlike—well, not unlike AIG, although AIG was making some bad bets, but they are still colossal, and I just—it just—

Mr. QUARLES. They are big, but size alone does not determine systemic importance. It was a very careful decision. I was actually very pleased with the precision and depth of the analysis that went into the decision to dedesignate Prudential. As I had indicated earlier, I am, with the work that is being done on thinking about how we could look at activities that would cut across all firms—because it certainly is the case that nonbanking firms can be engaged in activities that have systemic consequence, we need to have a good framework for understanding when that would be and how we would—

Mr. LYNCH. Let me just reclaim a little bit of time I have left. The two-step analysis is that we look at the nature, scope, size, scale, concentration, interconnectedness on mix of activities of the nonbank financial company that might pose a threat to the financial stability of the United States, and none of that analysis that you came up with at all addressed the first question and nobody—we put a two-step procedure, and FSOC never addressed the second step that Congress laid out there.

I yield back. Thank you.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Oklahoma, Mr. Lucas.

Mr. LUCAS. Thank you, Mr. Chairman. Vice Chair Quarles, I am curious as to the Fed's progress on the mortgage servicing rights (MSRs) rulemaking. Last year, regulators passed a proposed rule that allowed banks to keep a greater portion of the MSRs under Basel III, but it seems the rule was placed on the back burner during the Senate 2155 debate. I also hear from my constituent banks there may be more relief coming in the rule. I would like to be able to tell my constituents that help is on the way. Is it possible to release something close to last year's proposed rule as an interim rule while you and the OCC work on something more final? Barring that, I would love to hear of when you think the rule will be completed.

Mr. QUARLES. So you are actually—it is quite astute that in our effort to ensure that we implemented 2155 promptly, that a lot of resources went into that and some things stepped to the side, but we are reengaging with all of those now, and I do expect that we can make that rule final soon—not too distant future.

Mr. LUCAS. That would be good. My next question was previewed earlier by Mr. Luetkemeyer, and I had mentioned to you that I serve on both this committee and the Ag Committee, and as you know, my many farmers and ranchers use derivative markets to hedge their bets. When they need to access the cleared market, they must post margin to a clearing member, such as bank, and

I have argued for a while that the capital rules covering this margin lead to unhealthy derivatives markets. Prudential regulators should offset such margin when calculating the supplemental leverage ratio. And as you mentioned earlier, this committee has approved a bill by Mr. Luetkemeyer to legislatively mandate such an offset. This idea has bipartisan support too, and the current Democratic CFTC members have publicly identified capital rules as inhibiting a healthy cleared market—derivatives market, I should say. And even further, the Europeans have found a solution to this issue that is expected by the end of the year. I was wondering or I am wondering why the Fed's recent leverage ratio methodology includes merely a question asking for input on the idea of an offset for cleared margin client. It seems like the Fed has enough evidence already to solve this on its own. Given everything Congress, the CFTC, and the Europeans have stated about the need for this policy, what information does the Fed hope to receive that it does not already have?

Mr. QUARLES. Well, I think that there is always more information that we can gain, but I agree with you that my personal view is that we ought to be open to changing our treatment of initial margin in this way. We have rules at the Fed, in particular 23(a) and (b) and regulation W that implement them, that address some of these concerns, and we ought to use those.

Mr. LUCAS. Absolutely, and I would agree with you on the need to be fully prepared for the next step, but it seems to me like we are ready for that step to be taken care of.

One last note regarding margin rules: Mr. Luetkemeyer mentioned inter-affiliate margin. I appreciated your response to him about making this a priority for you, and I will note further that not only is the United States isolated in requiring this, but even other regulators here, like the CFTC, don't require it. In fact, former Chairman, CFTC Chairman, Massad identified initial margin as a very costly and not very effective way to enhance risk management that was better meant for lowering risk on trades between unaffiliated parties. I admit to having my disagreements with the Chairman on many things, but his opinion on this topic speaks volumes for me. So please make it a priority going forward during your tenure because I truly believe relief is needed.

And with that, Mr. Chairman, in the spirit of brevity, I will yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Georgia, Mr. Scott.

Mr. SCOTT. Thank you very much, Mr. Chairman.

Chairman Quarles, let me just ask you, as you noticed, several Members of our committee are concerned about the Fed's interpretation of what we passed in S. 2155, and you may have addressed some of this along the way, but I want to get a little clarity here regarding regional banks and what the intent was so that we are clear. Most of the regional banks in our country are in the South, where I come from, and so we want to make sure that it is clear. And in that bill, we ask you to remove them from that requirement of the enhanced prudential standards, and you did this: You propose a tailored framework, but you didn't remove the EPS designa-

tion, and you only clearly address liquidity rules, but you did not do anything specific about capital planning. And capital planning is extremely important, but you failed to provide the clarity for our regional bankers, and in that way, it could be interpreted you really sidestepped the intent of the bill. So I want to give you a chance to respond to that. And very quickly, let us know, when can we expect the Fed to propose new capital rules for our regional banks?

Mr. QUARLES. So I appreciate the opportunity to clarify that. It is our—I think that that will come as we make final the tailoring proposal, which again, it is our intention to move as promptly on that at making it final as we did in proposing it. We are gathering comments right now on questions such as how we ought to approach capital planning for the firms that are in that category. We will evaluate those comments, but it is also very, very much our intent to hew to the congressional intent in making it final.

Mr. SCOTT. Absolutely. We certainly want you to clarify that. Now let me go to your speech to the Brookings Institute regarding the stress test. And our stress tests are very important for the financial stability of our country. Now, what you said in your speech was that your proposals will give the banks more information about the test in advance, including, and I quote here, you said "additional details on the supervisory stress test models and results of and portfolios of hypothetical loans and associated loss ratios," and this sounds very much like you are going to be giving away the exact questions on the stress test ahead of time. Can you explain how you are not doing that?

Mr. QUARLES. So there are a couple of—I think there are maybe three important things to say about that. One, it is because we are a democracy and the due process requirements of people who are subject to rules from the Fed, because of our accountability our need to be clear to you and to the public about what it is that we are doing, I think it is a very high bar for us to be less than fully transparent around anything we do, and that includes the stress test. I do think that that bar is met in the case of some lack of transparency around the stress test. I won't chew up your time by going into all the details about that, but I think we can be much more transparent than we have been in the past without giving away the test. We are only talking about making clear broad categories of assets, what our loss function is on broad categories of assets, not every single, not with deep precision as to each category, but broader categories of assets.

And, second, we are talking about the models as opposed to the scenarios, and the scenario design, the differing scenarios each year, is really what is more akin to the test that is being provided, and the models are more akin to the textbook.

Mr. SCOTT. Well, let me ask you, but doesn't that mean that if you are going to give out hypothetical portfolios ahead of time, that they will be able to figure out exactly the questions that are going to be on the test ahead of time?

Mr. QUARLES. No, I don't think so because that will—the scenarios each year that we test them against will differ from year to year. So they won't really be able to respond to that.

Mr. SCOTT. Well, thank you. Give my regards to Chairman Powell, won't you?

Mr. QUARLES. I will do that.

Mr. SCOTT. He is doing a great job.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Colorado, Mr. Tipton.

Mr. TIPTON. Thank you, Mr. Chairman.

And, Vice Chairman Quarles, thank you for being here. I come from rural Colorado.

Mr. QUARLES. So do I.

Mr. TIPTON. Great spot to be from. And a lot of our banks are obviously community banks, small businesses that are there, and as the Chairman has often noted, capitalism will not work without capital. But our small banks have had a terrifically difficult time being able to deal with a lot of the regulatory burdens from the trickle down of Dodd-Frank. During your testimony, you cited that the Federal Reserve is working diligently with the OCC and the FDIC to be able to reduce some of the reporting burdens coming down to our community bank organizations while preserving the effective oversight. And would you describe a little bit how these efforts to be able to reduce the compliance burdens on our smaller institutions will extend past banks to the benefit of the everyday consumers, the people that I worry about in my district that are just trying to be able to earn a living for the financial service products that they need?

Mr. QUARLES. Sure. Absolutely. The ability, particularly of smaller banks, to provide credit to small businesses—and in rural areas, we know that small banks have a particular role in doing that—and the purpose of these banks is to provide support to the real economy to everyday people who are engaged in their businesses. To the extent that we can reduce the compliance burden, the cost that these banks face in their businesses without in any way undermining the safety and soundness of the system, then we increase their ability to provide credit to the real economy and particularly in these areas of the economy—small business and rural areas.

Mr. TIPTON. So you are comfortable we are going to be able to make sure that we do have the regulatory compliance in place for these small banks, but also recognizing those costs will be passed on to the consumers, so the more we can reduce that the better we can create a win-win for our communities.

Mr. QUARLES. Absolutely.

Mr. TIPTON. Great. The Federal Reserve has also recently put forward some proposals to be able to tailor the prudential standards, and the model that has been laid out by the Board has several different tiers, as I know you are aware, from the smaller institutions above $50 billion in assets scaled all the way up to our global institutions, as well. These scaled requirements, could you explain why you feel that that is important for the supervisory scheme of the Fed to be able to divide it up into the tiers?

Mr. QUARLES. Because I think that it is important generally that the nature and character of our regulation match the nature and character of the firms that are being regulated so that firms that have more systemic consequence, that are more complex, that are engaged in riskier activities should be subject to regulation that ad-

dresses those, and firms that are simpler, smaller, and less systemically consequential should be subject to regulation that is appropriate to that. That will inevitably be less costly regulation, and yet, even though you can have less costly regulation, then you ensure that the system as a whole is operating most efficiently, that you get the safety in the system that you want with the least cost across the horizon of firms.

Mr. TIPTON. Great. I appreciate that. And you know, in September, Craig Phillips, Counselor to Treasury Secretary Mnuchin, he argued that the U.S. fintech industry risks being left behind if regulators don't provide proper coordination guidance to the industry to be able to keep it competitive with the rest of the world, and speaking about the growth of opening banking regimes globally, Phillips stated, "There is a huge competitive threat if we don't get the investment right. There is a risk that the U.S. will fall behind, and with that, a risk that jobs will go elsewhere."

What measures do you believe we can take to make sure that the U.S. fintech industry does stay competitive with the rest of the world, and do these need to be statutorily or regulatorily implemented?

Mr. QUARLES. Oh, I do think there could be measures that are both statutory and regulatory that help that. The main thing I think the regulators can do is try to ensure that the regulatory steps that we take to ensure the safety of the firm—the safety of the system are again calibrated to be as efficient as possible and to not impose unnecessary costs, particularly on small startup firms. Obviously, we do need to be concerned about compliance. There will be some costs that are inevitable, but we always ought to be looking to ensure that we again have calibrated the measures to the real risks that we perceive as opposed to being excessively costly.

Mr. TIPTON. Thank you.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes another gentleman from Colorado, Mr. Perlmutter.

Mr. PERLMUTTER. Mr. Vice Chair, great to have you here.

A statement and then a couple, three questions for you. So the first statement, and I would disappoint the Chair if I didn't bring this up, is now we are at about 47, 48 States that have some level of marijuana use, and our banking laws and generally the Controlled Substances Act are not in line with all of these different States. And it is something that I want to make sure we get the State laws and the Federal laws to be aligned. And a lot of this comes to the intersection of the banking sector and to the Board of Governors of the Federal Reserve. Number one.

Number two, just some very general questions. We have had about 100 months of job growth, 80 or so under President Obama, the last 20 under President Trump. One, is this sustainable, and, two, what clouds do you see on the horizon, if any?

Mr. QUARLES. So I do think that is sustainable with the right measures. We have a very strong economy currently. We are bringing people back into the labor force. We have a low unemployment rate, but that has not been associated with excessively high inflation, really high inflation at all. We have hit our target, but we are

not exceeding it. There are—there is some interesting work that has been done that changing educational attainment of the U.S. workforce has actually been affecting the natural rate of unemployment, the level of unemployment—the level at which unemployment can fall without increasing inflation. It may be materially less than we have estimated in the past, and that may explain some of what we are seeing, but my general assessment certainly is that we can continue this strong economy and this strong labor market for some period of time.

Mr. PERLMUTTER. OK. So let's go into this education question and the workforce generally. So, obviously between globalization but primarily automation, we see tremendous technological strides being made. Do you as the Vice Chair or does the Federal Reserve generally, are you keeping an eye and are you concerned about the potential for automation, in particular eliminating whole occupations, really having a dampening effect on the labor force that could be harmful generally?

Mr. QUARLES. So, obviously, we do look at that. That is I think more of a much longer-term issue. History would tell us to be optimistic about that, that the application of technology in the past, although it has changed the character of the labor force—it has changed what people do—it generally hasn't eliminated the need for human work, but it has made humans much more productive. I think that that, at least in the early stages, is what we are continuing to see here, and certainly, in the very near term, the very strong demand for labor in our current economy would cause us to be optimistic as well.

Mr. PERLMUTTER. Last question on cryptocurrencies and digital currencies. How does the Federal Reserve take in these new currencies, bitcoin or Ethereum or whatever it might be, how do you—does that get added into the monetary supply, subtracted from the monetary supply? How do you look at that in terms of liquidity and how much there is to spend out there?

Mr. QUARLES. So, currently, the characteristics of all those cryptocurrencies would not lead one to consider them—

Mr. PERLMUTTER. As a currency.

Mr. QUARLES. —money yet. They really aren't money yet. They are an asset. In fact, I think internationally we have taken to calling them crypto assets as opposed to cryptocurrencies. They are an asset that has been highly volatile in price, which makes them less appealing even as a store of value and certainly not as a payment mechanism. There are issues, and because of that, there are issues around criminal activity and consumer protection that I think we ought to be appropriately concerned about. Ten, 20 years down the road, do either some of these assets or some assets like these, do they have a role in the payment system? They could evolve some way. There is nothing inherently defective about them, I don't think, but at this point, they don't really factor into our consideration of the money supply.

Mr. PERLMUTTER. Thank you. I yield back.

Chairman HENSARLING. The time of the gentleman is expired.

The Chair now recognizes the gentleman from Ohio, Mr. Stivers.

Mr. STIVERS. Thank you, Mr. Chairman.

Thank you Mr. Vice Chair. I am over here. Good to see you. Right behind Mr. Hill there. I appreciate you being here. I saw one of your speeches earlier in the year where you talked a little bit about the cybersecurity threat and you talked about—you attributed it in part to poor technology hygiene and said we need to work to be a step ahead of those who would steal or have other nefarious intents with cyber, and I totally agree with you. If you look at the history of the industrial revolution, what we did was we created as a society worker's compensation insurance that increased and improved industrial hygiene. I believe that there is a way to use cybersecurity insurance to do the same thing. The problem with the static standard is the day that you create a static standard, it is essentially out of date. So we have to figure out how to create a dynamic standard, and one of the benefits of cyber insurance, if we create the right safe harbors for folks and create the right coverages that make sure that it really covers the liabilities, then it can create—the underwriting for that cyber insurance can create that dynamic standard, and I would ask that you guys think of that, and I am curious if it is something that you have looked at as a way to mitigate and create a dynamic standard in cybersecurity protections and avoid some of these petty jurisdictional issues we are fighting now between the committee across the hall.

Mr. QUARLES. So I think that is a really interesting idea. I myself have not given thought to it. I am sure there must be some folks on the staff of the Fed who have, and I am actually adding it to my to do list now to go back and find them because I think that many aspects of what you just said are interesting.

Mr. STIVERS. I would love to sit down privately and talk to you guys and work with you guys on this. I think it is something that will help build private capacity. I think it is something that will help increase the technology hygiene and create active and passive defenses that we can price so people understand how much they want to invest in that based on what their premiums would be. It creates a pricing mechanism to create the right incentives in cyber investment, and that is one of the concerns that some companies have had is, how do you price what you are willing to do? And it would put a price on it. So just an idea that is one of the things obviously insurance does; it is a pricing mechanism. So I hope you will go back and take a look at it, and I love the dynamic nature of it. And I know from your speeches, you have talked about that.

Switching subjects to one other thing that I know Mr. Luetkemeyer and Mr. Lucas brought up, the inter-affiliate margin issue. I just want to ask you to look at that. While inter-affiliate swaps don't have all the hassles that other swaps do, this whole idea of additional counterparty exposure that isn't really there has led to $29 billion being locked up in margin that doesn't really need to happen, and that is money that could be used to help those firms create jobs and help those firms create capital in our system that would echo and help our economy that is now growing, but there is still a great need for capital, and I hope you will take a look at it. And we are ready to work with you. It has been a bipartisan issue, and I want to work with you guys going forward to try to get to the right answer on that.

Mr. QUARLES. I appreciate that. Very much looking forward to working with you on it, and as I had indicated, I do think that it is something that is ripe for us to consider.

Mr. STIVERS. Thank you. I yield back the balance of my time, Mr. Chairman, now that Mr. Royce is here.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Texas, Mr. Green.

Mr. GREEN. Thank you, Mr. Chairman.

I thank the Ranking Member as well, and I thank the witness for appearing today.

I would like to visit with you briefly about the CRA. As you know, it was developed and put in place, if you will, in 1977 to deal with redlining, and I think that it has been quite effective. I am looking at at least one indication that some $2 trillion in small business and community development loans have been made since 1996.

The CRA is used to evaluate applications for future merging, charters, acquisitions, bank openings, and deposit facilities. Do we have a record that you can share with us of the number of mergers that have been held up or that have been denied because of the CRA?

Mr. QUARLES. I don't have those figures for you today, but they are obtainable.

Mr. GREEN. I would like to have them, if I may. Do you know of any merger currently—this would just be from your recollection—that is being held up because of CRA?

Mr. QUARLES. I am not aware of one that is currently being held up.

Mr. GREEN. A charter that is being held up because of CRA?

Mr. QUARLES. No.

Mr. GREEN. Acquisition?

Mr. QUARLES. Again, I am not aware of anything.

Mr. GREEN. Bank opening?

Mr. QUARLES. No.

Mr. GREEN. Deposit facility? I mention these to you, Mr. Vice Chairman, because we hear a lot of complaints about the CRA, but I am not finding the empirical evidence to indicate that there is a lot of suffering because of it. I think that it is doing a lot of good, and I think that banks are—most of them are getting satisfactory reports about 98 percent. So, if the banks are getting satisfactory reports and CRA seems to be working fairly well, the question becomes why would we change it such that it might be weakened to some extent? Now weakened depends upon your point of view, of course, but I am concerned about the OCC and some of the actions that are taking place. I want to see businesses blossom, especially small businesses, but I am also concerned about the other aspects of CRA, and I just don't see the need to make the changes. I am open to a review and someone working with me, but I am not finding the empirical evidence of the necessity to weaken it, and perhaps you can give me some additional thoughts.

Mr. QUARLES. So I would completely agree with you. I don't think that we should be weakening the CRA. My view is almost because of—I mean, the banks do comply with the CRA, and they have a good record of compliance for all the reasons that you cite,

but it has become a little formulaic. Both our supervisors and the banks themselves know that if they do X, Y, and Z, they will pass. And X, Y, and Z has become just a little unimaginative. And I think that you can actually have more effect in really supporting the low- and moderate-income portions of the communities that banks serve by taking this opportunity to reinvigorate the CRA. So I view this CRA reform movement that the OCC has taken the lead on but that the other banking agencies, including the Fed, have participated in and not reluctantly from that viewpoint as a way to really make the CRA achieve the objectives that were identified in 1977 in a way that is continuing to be relevant in the 21st century, not to weaken it at all. I do think that if we work together, we can do that, and I would be delighted to work with you on that.

Mr. GREEN. Well, I am appreciative, and I respect your response. The term that you have used is "reinvigorate," and I think that is a good term. I tend to think of strengthening it, and maybe we are saying the same things, and it may be a question of semantics, but I am amenable to working with you and others to strengthen it. I think that you are right, we can do more. It can better serve the communities. Especially given that we are going to online banking now, there will be some questions that we will have to resolve that we haven't confronted, and also we are losing a lot of the brick-and-mortar facilities. Banks are moving to centralized locations for the most part, and then they will have online facilities. So I think that we do have to think about these things, but I want to think about them from the rationale that we had in 1977 when we instituted the CRA. Thank you.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from California, Mr. Royce, Chairman of the House Foreign Affairs Committee.

Mr. ROYCE. Thank you, Mr. Chairman, very much, and just to recap here in September 2008, your former boss Treasury Secretary Paulson declared that the U.S. Government would step in and place Fannie Mae and Freddie Mac in conservatorship and provide enough taxpayer support for the GSEs to fulfill our financial obligations. We effectively nationalized the GSEs in 2008. As you know, shortly after, the Fed embarked on an asset purchase program that included well over 1 trillion of mortgage-backed securities from the now effectively nationalized GSEs. Today, there is talk that this Administration may seek to release the GSEs from conservatorship. A release of the GSEs out of conservatorship would reverse that structure that was put in place in 2008 and would raise some serious issues from a monetary policy standpoint I think for all of us. Instead of purchasing assets from two government-owned and controlled companies, you would be purchasing assets from companies owned and operated by private shareholders.

As a member of the FOMC, you have thought about what it would mean for the Fed's current portfolio and the future purchases should these institutions return to being privately owned and controlled companies. I know you have, and you might want to share your thoughts on some of this. And before we get to that, let me say that I regret that we were not able to resolve this issue during my time here in Congress, but I would like to caution against making a bad situation worse. If talks about releasing the

GSEs from conservatorship ever reach you at the Fed I sincerely hope that you will recognize the important role the Fed has played in this space dating back to the 1990's. I had many conversations with Alan Greenspan on the need for systemic risk regulation over the GSEs into the early 2000's. And, in fact, I had legislation here that we were not able to pass in order to try to control that systemic risk and in order to try to reduce the leverage in those portfolios.

I hope that you consider the potential impact on monetary policy and consider the massive moral hazard problem, which is the thing that worries me most about all of this, that would be created by releasing these companies back to shareholder control. We have seen politics and short-term profits went out over good policy when it comes to the GSEs in the past. I hope this Administration and this Congress have learned something from this failed duopoly and do the hard work necessary to reform our housing finance system, but in the interim, there is your role in this, and so, if I could ask you to respond, I would greatly appreciate it.

Mr. QUARLES. So thank you.

Certainly, with respect to the GSEs, in my earlier Treasury service, that was a topic that I gave a lot of thought to and very much share your concern that we need to ensure that the risk around those institutions is appropriately handled and the structure of them does not create systemic risk in our financial system.

Mr. ROYCE. Well, the reason it is so important is that the moral hazard that was created by that and—it was not the only factor. But certainly, at 100-to-1 leverage, it became a key factor. And the fact that so many other institutions held this as basically in their—under the law as equivalent of cash—

Mr. QUARLES. Right.

Mr. ROYCE. —meant that suddenly they were undercapitalized so that when housing finance went down, it meant that eventually the financial system nearly went down. And so now we find ourselves with this reality also that once these institutions that are neither—that really have an opaque structure where the investor doesn't know who really owns them but presumes that the government will bail out the consequences—and, of course, that has been proved—it creates an inability to price risk for these institutions. So, at this point, I was looking for some assurance in terms of your leadership in trying to do something to prevent that catastrophe from occurring again.

Mr. QUARLES. It is something that we give thought to as we consider the normalization of our balance sheet, definitely.

Mr. ROYCE. Thank you. Mr. Quarles, thank you.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Arkansas, Mr. Hill.

Mr. HILL. I thank the Chairman for the time. I appreciate Mr. Quarles being here. It is good to see you before the committee. I appreciate your service.

I want to echo something that Mr. Lucas discussed with you, which is mortgage servicing rights. I have been in Congress for 2 terms, 4 years, and this has been a topic that we have talked about for all those 4 years with no progress. And in your role in the pri-

vate sector and now as Vice Chairman of the Fed, do you acknowledge that mortgage servicing rights are an acceptable banking practice for a commercial bank or a bank holding company to be in that business?

Mr. QUARLES. Absolutely.

Mr. HILL. And don't you agree that Basel III and the resulting—results of that have driven that business out of the depository institution sector into shadow banking and other investors?

Mr. QUARLES. It has certainly been a material factor, yes.

Mr. HILL. Yes.

So we have—I know the default answer today from the Fed is soon.

Mr. QUARLES. Soon.

Mr. HILL. But I would invite you to commit that we will have our mortgage servicing rights regulatory proposal out before the end of the year. Is that possible?

Mr. QUARLES. I don't know that it will be possible before the end of the year, but we are not talking about before the end of next year. So it will be sooner than—it will be soon.

Mr. HILL. So now I have gotten you to say "sooner" rather than "soon." That is good. I like that. Thank you.

We also talked about—earlier today about Volcker. And you were asked, I think by the Chairman, an interesting proposal, which is on this idea of harmonization.

Could the interagency process though the SIFI act with leadership from the Fed really push regulatorily what I have tried to push legislatively, which is harmonization with the Fed as the leader among equals on that topic? Because we have serious record over the past—since the passage of Dodd-Frank of misinterpretation and conflicting interpretation of this rule. I don't think it is going to be resolved by Volcker 2.0. I really don't. I think these are hard issues. I think they are made difficult by the statute itself. I don't believe the agencies are going to be able to wordsmith their way around the statute.

So this harmonization piece that was left out of 2155 I think is really an important issue.

Do you believe that is realistic, that the agencies could work together? When I say "the agencies," I don't mean banking. I mean CFTC and SEC as well.

Mr. QUARLES. So it is certainly not impossible. The work right now on simplifying Volcker is, I think, proceeding very well. And that is—while it is being pushed by the Fed, all the agencies are participating equally, and I think exactly as one would want and as exactly as one would expect under the—if the proposed legislation were in effect.

And so I would think that one could move that at least in the initial circumstances. You could maybe see that happening. I am not sure how sustainable it would be over many different administrations, different people sitting in these seats. The current group of regulators works very well together for a whole variety of reasons. I don't know that that would be a sustainable solution, although it could be a near-term one.

Mr. HILL. Well, I certainly will work in the remainder of this Congress and early in the next Congress to push this harmoni-

zation idea. We had 300 votes for that in this House. And so I want to make sure that, on a bipartisan basis, that we can move that forward.

I also heard you address with Mr. Luetkemeyer CECL. And I was pleased to read in the last couple weeks that suddenly Jamie Dimon at JPMorgan Chase has learned about CECL. I was pleased to hear his comments on that.

In meetings with the district bank presidents around the country, they don't seem to have that issue brought to their table, and I would encourage you to reach out to the district bank presidents and proactively ask for comments about CECL. I think the Feds should take a leadership role in dealing with FASB (Financial Accounting Standards Board) pronouncements and not treat that as something over here because of the severe impact on compliance costs for your institutions you supervise and the unintended consequences of it as it relates to capital where, as you noted a few minutes ago, it could be essentially a redundant exercise to what we are already doing. So I would urge you to do that.

And I thank you for appearing today. And I yield back the balance of my time, Mr. Chairman. Thank you.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Georgia, Mr. Loudermilk.

Mr. LOUDERMILK. Thank you, Mr. Chairman.

And thank you for being here today. And I trust you received the letter I sent on September 28 with most of the Republicans regarding the SIFI regulations. And I am looking forward to your response soon. And my questioning is going to be around that area.

Do regional banks with less than $250 billion in assets currently pose a systemic risk to the economy?

Mr. QUARLES. I would say, with the current configuration of their activities, none of them individually does, no.

Mr. LOUDERMILK. OK. And that is my feeling, and especially working with a lot of the banks, especially regional banks back home. And I agree. I think with most of the data the Fed has, it shows they don't pose a systemic risk.

And so some of the concerns—and I appreciate my colleague bringing up CECL—is it appears that there may be a pro-cyclical effect that CECL may have in that incentivizing making loans in a strong economy but decentivizing those loans in a downward economy. I understand maybe you have the same feelings about that, that you mentioned in a speech. Can you elaborate?

Mr. QUARLES. So I think that we need to understand much better than we do what the effects of CECL would be, both the so-called day one effects and then the longer-term effects, including effects during a period of stress.

We have gotten a lot of input already with respect to what that would be, but a lot of it points in different directions, which is one of the reasons why we have said that—for how CECL reserving relates to our capital requirements, we are going to phase that in so that we can have more experience with how it actually operates in practice before it actually begins to affect, essentially add to the loss absorbency with our capital regime. So we will be studying

that and phasing it in over time so we can see how that works because I think there is a lot that we don't really know.

Mr. LOUDERMILK. OK. And I appreciate that.

Last question, and it actually looks like I may have a little time to reserve back for once.

Some of the banks that I talk to back home have concerns that, if the Federal Reserve banks will actually abide by the changes to the SIFI regulation when they are supervising banks, the concern that it may not flow; these changes may not flow all the way down. Can you commit that that will happen with these updated changes?

Mr. QUARLES. Yes. We are devoting a lot of resources to ensure that these supervisory messages flow throughout system. As you can appreciate, that is a lot of work. It is not a question of turning on a switch, but it is work that we are very much engaged in.

Mr. LOUDERMILK. OK.

Thank you, Mr. Chairman. I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from West Virginia, Mr. Mooney.

Mr. MOONEY. Thank you, Mr. Chairman.

And, Mr. Quarles, good see you again.

The Trump Administration has frozen implementation of Basel III's punitive treatment of mortgage servicing assets.

What are your long-term plans for MSAs? And will you be returning to the treatment of MSAs to pre-Basel III for community banks?

Mr. QUARLES. So we have a proposal out that would significantly increase from Basel III the proportion of mortgage servicing assets that can count for capital. It would not go all the way back to— the proposal would not go all the way back to pre-Basel III levels, but it is a material increase. And we are in the—we are gathering comments and in the process of evaluating those comments to determine whether there should be additional changes.

Mr. MOONEY. OK. Well, I have been working on my, with my staff, on legislation to support community banks, who are, frankly, suffering under these Basel III absurd treatment of these assets. And I would like to work with you, take a look at the draft legislation when I get it, and possibly recommend some improvements so we can get community banks lending again.

Mr. QUARLES. Very much I would be delighted with you on that.

Mr. MOONEY. And then one additional question, really from my friend from New York, Congressman John Faso. He successfully sponsored an amendment to the CHOICE Act, which would have restored the ability of directors of a bank organized as a mutual holding company by resolution to waive dividend returning to the status quo prior to Dodd-Frank. Unfortunately, this provision was not included in our Dodd-Frank reform passed earlier this year. So Representative Faso had sent you a letter in May 2018 whether the Fed can undertake a review of its regulation to remove this unnecessary impediment to MHC operations.

Can you advise on the status of his request or whether you believe this change can and should be made?

Mr. QUARLES. So we are looking into that. It is a complicated situation, but we are looking into what can be done.

Some of it isn't really even legal interpretation or changes that we can make as opposed to changes in practice, but I don't have a resolution for you today, but we are working on it.

Mr. MOONEY. OK. It is a long, three-page letter. I have a copy of it I can leave with you if you want to review it again.

Mr. QUARLES. It is on my desk.

Mr. MOONEY. You got it?

OK. Thank you.

Mr. QUARLES. Because it is extremely interesting. It is not easy.

Mr. MOONEY. Again, I appreciate your good work.

And, Mr. Chairman, that exhausts my time. I yield back the balance of my time.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Ohio, Mr. Davidson.

Mr. DAVIDSON. Thank you, Mr. Chairman.

Mr. Quarles, thank you for your testimony. Thanks for the service that you are doing for our country in your role as Vice Chairman of the Federal Reserve.

And it is an incredibly important role in the regulatory environment and, in fact, has taken a strong international component. We have talked a lot about Basel. We have talked about the importance of clarity on Volcker and, frankly, the implementation of the major reform that we were able to successfully pass through the House, the Senate, and get the signature on it. So I trust you guys are fairly busy.

One of the areas I have taken a strong interest in is crypto assets. While the U.S. is a global leader in the financial sector, my fear is that we are losing ground to other prominent nations, such as Singapore, Switzerland, and the U.K., due to lack of legislation and regulatory clarity with these assets.

I was pleased to hear you use the phrase "crypto assets," because it recognizes they are not generally currencies, and, in fact, there are all sorts of varieties: Crypto securities, crypto commodities, and certainly things that approach currencies.

One of the big challenges for them to be currencies, however, is ubiquity. And it is hard to have ubiquity without regulatory certainty.

I was quite alarmed, however, when you talked about something over a 10-year, 20-year horizon on something that could be used in a payment system. And the reality is, if you look at the way a ripple can settle in seconds versus the payment system we are using today, you are in the process of dealing with that. I believe that open blockchain technology offers solutions.

Could you talk about the intersection of that that is real time, something you are actively working on in payment systems, and open blockchain versus one that I think you guys are contemplating that would be quite closed and controlled?

Mr. QUARLES. So, with respect to—so I completely agree with you that the technology—not just the blockchain technology, although that is obviously very important, but then the specific application of the blockchain to some of these crypto assets is—I think there is a lot that is quite interesting about that.

My only point was that, currently, until society gets a handle on how they are going to value these, it makes it difficult for any of these assets, whatever their technological advantage is, to be the type of store of value or constant—to have—for users to have enough confidence in their continued value to really be a substitute for currency. Over time, I could see that happening.

On the payment system, what we are trying to do is to catalyze the private sector to come to solutions there because of limitations on our own authority, a view of what is the appropriate role of the Government/Federal Reserve versus private sector solutions. So we are trying to catalyze private sector solutions as much as possible.

And so it really will be up to them how they take advantage of some of these technological advances and which of them they think are most—

Mr. DAVIDSON. Thank you for that. Because I think a lot of people will be encouraged to hear that you are not looking at contemplating crowding out the private sector there.

Mr. QUARLES. Right.

Mr. DAVIDSON. And, to the factor of volatility, certainty, without regulatory certainty, we are likely to see more volatility.

And, last, on that, there are now stablecoins that are out there. They are essentially like pegged currencies, so it takes away the volatility that would be inherent.

As my time is rapidly winding down, I would just add to the dialog that has already occurred on CECL and the role of FASB. I do believe that FASB has had market distorting pronouncements. And to the extent that the Fed can join the SEC in being a buffer against irrational actions by FASB, we would greatly appreciate your efforts there.

I would like to yield the balance of my time, Chairman.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from North Carolina, Mr. Budd.

Mr. BUDD. Thank you, Mr. Chairman.

And, Mr. Quarles, good to see you again. Again, thank you for your hard work.

I want to start with CECL, or the current expected credit loss, and discuss that a little bit. I think my colleague Mr. Hill from Arkansas mentioned that just a few moments ago.

But you have said in the past that regulators seem to agree that, in times of stress, the CECL accounting standard will add pro-cyclicality to the banking system. So I know that regulators have proposed phasing in over 3 years the regulatory capital impact at the time of adoption.

However, due to the increased pro-cyclicality, in my view, the phase-in would have little effect if the economy goes into a slowdown shortly after it were to be adopted.

So can you tell us, is there any consideration being given to an ongoing add-back to regulatory capital for the impact of CECL until this new regime, one that is CECL responsive, can be agreed on? And if so, how long do you think it will take to finalize a capital plan like that?

Mr. QUARLES. So there is not a concrete plan to have an interim capital add-back to account for CECL. But obviously we are looking

at, during this phase-in period—and one reason for the long phase-in period is for us to consider what responses there ought to be for us to see how CECL operates in practice and then to consider whether there ought to be a response.

If we saw that there was a negative effect that we saw happening more quickly than during this phase-in period, perhaps because of changes in the macro economy, then we would accelerate what it is that we were doing.

Mr. BUDD. OK. Or slow it down, depending on what would be needed?

Mr. QUARLES. Right.

Mr. BUDD. I want to switch over now to a smaller part of your portfolio: Insurance oversight. And I know that you have extensive knowledge of the way that the international standard setting and regulatory cooperation is done. I know that you are familiar with the concept of mutual recognition.

One of the areas where a large bipartisan majority of this committee is trying to achieve mutual recognition is for our State-based insurance regulatory system with the IAIS (International Association of Insurance Supervisors) on their development of an international capital standard, ICS.

The IAIS, through both their actions and words, has repeatedly made it clear that their goal is to force changes to the entire U.S. State-based insurance regulatory system to make our insurance solvency regime look exactly like Europe's through Solvency II. I find this unacceptable for our U.S. insurance consumers, our markets, and our industries.

There has been a publicly released document from the IAIS detailing an agreement reached in Kuala Lumpur, and this was in November 2017, the IAIS proclaims that the base parameters of the ICS are going to be Eurocentric. The release also does leave the door open to having the U.S. system formally recognized by the IAIS. But numerous statements from them and their officials make it clear that is not their goal and that their end goal is to, in fact, force significant changes to the U.S. system.

So my question is this: Will you commit to us today to stand up to European members of the IAIS who are attempting to use that forum to force us to adopt their system? I will let you—that was a long question, so I will let you—give you a few moments.

Mr. QUARLES. So the Fed in its—which sits on the IAIS, as you know, has been working very closely with the State regulators' so-called Team USA approach in ensuring that the building-block approach to capital, which reflects the U.S. system, is accepted in the IAIS. And I think that that is—I actually think that that process is working reasonably well. The reports that I get from our delegation are that they—that—well, it is a process that the IAIS is—that they are reasonably happy with how that is proceeding. In any event, we are very committed to it, and we are working with the State regulators on it. And certainly that is not over.

Mr. BUDD. I want to add just another piece to that question. So would you commit today that you will not allow the Federal Reserve to be part of any final agreement on the ICS that does not formally recognize the U.S. system of insurance regulation, one that has worked well for us for the for last 150 years?

Mr. QUARLES. I mean, we certainly wouldn't have the ability to commit to anything that would change our domestic insurance system at all, so—

Mr. BUDD. OK. Chairman, my time is nearly expired. I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Indiana, Mr. Hollingsworth.

Mr. HOLLINGSWORTH. Happy Wednesday. I am glad that you were here and have reached what I think is the end of the line, like Little Round Top at Gettysburg, you have reached the end.

I wanted to work through two questions, two very separate questions. You had an earlier exchange with Representative Barr talking about some foreign banks that operate in the United States and how you had recently issued guidelines, I think on October 31, around regional banks, or what I consider regional banks, that are domestic and providing some updated guidance or views on what that updated guidance may look like, right? And I think you referenced that these foreign banks that are operating in the United States aren't identical to those domestic operating banks, and so there may need to be some deviations from that or some further reviews.

First, do you have a timeline of what that further review may look like? And then, second, do you know of any deviations that may exist or need to exist for these foreign bank—I think in previous testimony and a lot of speeches you have expounded the philosophy that banks should be competing on a level playing field and the importance of foreign banks operating in the United States for consumers, for borrowers, for depositors, and how we want to maintain that level playing field.

So I am curious about those two things.

Mr. QUARLES. So, on the timeline, I think we should have a proposal for you early next year.

Mr. HOLLINGSWORTH. Great.

Mr. QUARLES. With respect to the foreign banks, the tailoring for the foreign banks.

With respect to specific differences, again, as you stated, as I have stated and completely agree with, the foreign banks are an important part of our domestic financial system, and so we need to ensure that there is a level playing field for them. They are different than a domestic bank of the same size for a few reasons. So the foreign banks are organized. You have the intermediate holding company that contains the nonbank assets that are enhanced potential standards directly applied to. But they operate—there is always a branch of the larger parent that also operates in the United States, isn't directly covered by that regime. They can exchange assets. They operate in concert to some extent. That, again, changes a little bit the character of how they think about them. They are part of a larger global organization. That can be stability enhancing.

Mr. HOLLINGSWORTH. It can be positive; it can be negative.

Mr. QUARLES. It can be positive; it can be negative. And so you need to think about that.

So I don't view it as a one-for-one transposition if you have an intermediate holding company of X size, it ought to be treated exactly the same as a domestic holding company of X size in order for there to be a level playing field, because there are those differences.

Mr. HOLLINGSWORTH. So I just want to encourage that even if there are deviations in the mechanics by which you arrive, the goal is to arrive at the same place.

Mr. QUARLES. Precisely.

Mr. HOLLINGSWORTH. OK. And I just want to make sure that we continue to encourage that. I want them to be able to compete on a level playing field even if there are mechanical differences in how we arrive at that.

Second question, far afield from that. Much has been talked about large banks, large institutions, and some of the work that has been requested or has not been requested in how we might further fine-tune and make more efficient the regulatory environment. I think everybody here concurs that we want to watch our large institutions closely, but I am really, really concerned about how we are layering on surcharges and looks and reviews on top of reviews and how those begin to pile up and create really distortionary effects for our larger institutions. So, again, trying to create an environment where we can get to more efficient regulation at the super large institutions as well.

Do you see that there is any opportunity to be able to make that more efficient, more transparent and, thus, more effective both for those that are regulated and consumers that are a big part of the consumer base for those large institutions?

Mr. QUARLES. I do. I think that some of the changes that I have talked about recently, evolution of our stress-testing practices, which are very important for the largest institutions, and changes in those practices can happen that significantly reduce regulatory burden on those institutions without affecting their resiliency or the overall loss absorbency of the firms or of the system.

I do think we need to think about the international level playing field for our largest firms and not so much—I mean, certainly it is important whether the playing field is fair to them, to domestic U.S. firms, but for the systemic reason that, if you have an unlevel playing field, you will have risky activities moving to the weakest parts of that system, which it may not be our firms but that ultimately we in the U.S. may suffer from if you get these systemic imbalances that result from regulatory incentives we create. So we need to be thinking all of that through.

Mr. HOLLINGSWORTH. Right.

I just want to make sure and continue to encourage you, as we look at how we manage the regulatory framework for our super large institutions, that we don't layer in redundancy after redundancy without point—and we continue to try to make a framework that is clear, transparent, but also efficient, and to remember that millions of depositors, millions of consumers, millions of borrowers do business with these large banks every single day. And it is important to those to make sure that we continue to get to a more efficient framework, not just a larger, more redundant one.

So thank you so much.

Chairman HENSARLING. The time of the gentleman has expired.

There are no other Members remaining in the queue. Thus, I would like to thank the witness for his testimony today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

Governor Quarles, we would ask that you respond as promptly as you are able.

This hearing stands adjourned.

[Whereupon, at 12:34 p.m., the committee was adjourned.]

A P P E N D I X

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Statement by

Randal K. Quarles

Vice Chairman for Supervision

Board of Governors of the Federal Reserve System

before the

Committee on Financial Services

U.S. House of Representatives

November 14, 2018

Chairman Hensarling, Ranking Member Waters, other members of the committee, thank you for the opportunity to testify on the Federal Reserve's regulation and supervision of the financial system. My testimony today covers two main topics: our efforts to improve regulatory transparency, including the report accompanying my submission to the committee, and our progress in making the post-crisis regulatory framework simpler and more efficient.

The Role of Transparency in Regulation and Supervision

I am mindful that this semiannual testimony--like my position as Vice Chairman for Supervision--is grounded in Congress's efforts to strengthen and improve the nation's regulatory framework following the financial crisis. This testimony reflects a critical element of those efforts: the desire, and the need, for greater transparency.

Transparency is part of the foundation of public accountability and a cornerstone of due process. It is also key to a well-functioning regulatory system and an essential aspect of safety and soundness, as well as financial stability. Transparency provides financial firms clarity on the letter and spirit of their obligations; it provides supervisors with the benefit of exposure to a diversity of perspectives; and it provides markets with insight into the condition of regulated firms, fostering market discipline. Transparency increases public confidence in the role of the financial system to support credit, investment, and economic growth.

The Federal Reserve has taken a number of steps since my last testimony to further increase transparency, and to provide more information about our supervisory activities to both regulated institutions and the public.

For example, the Board recently improved its supervisory ratings system for large financial institutions.[1] Ratings are an essential vehicle for supervisory feedback--a clear, concise way to convey whether a firm meets expectations, with tangible, predictable consequences for those that fall short. Our ratings system for large institutions had remained unchanged since 2004, even as our supervision of those institutions evolved significantly after the crisis. The new rating system will better align ratings for these firms with the supervisory feedback they receive, and will focus firms on the capital, liquidity, and governance issues most likely to affect safety and soundness.

The banking agencies also recently clarified that supervisory guidance is a tool to enhance the transparency of supervisory expectations, and should never be the basis of an enforcement action.[2] Guidance--a valuable tool for examiners to help evaluate firms and explain supervisory findings--should always be based on concerns for safety and soundness or compliance at a particular firm. However, guidance is not legally enforceable, and Federal Reserve examiners will not treat it that way.

Finally, we expect shortly to make final a set of measures to increase visibility into the Board's supervisory stress testing program. The enhanced disclosures will include more granular descriptions of our models; more information about the design of our scenarios; and more detail about the outcomes we project, including a range of loss rates for loans held by firms subject to the Comprehensive Capital Analysis and Review. The disclosures will provide a more complete picture of the stress testing process, and facilitate thoughtful comments from academics

[1] Board of Governors of the Federal Reserve System, "Federal Reserve Board finalizes new supervisory rating system for large financial institutions," news release, November 2, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20181102a.htm.

[2] Board of Governors of the Federal Reserve System, Bureau of Consumer Financial Protection, Federal Deposit Insurance Corporation, National Credit Union Administration, and Office of the Comptroller of the Currency, "Agencies issue statement reaffirming the role of supervisory guidance," news release, September 11, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180911a.htm.

and other members of the public, while mitigating the risk of convergence on a single model. As a result, we believe the disclosures will improve our work, making the tests more reliable, visible, and credible. We will continue our efforts toward greater transparency in stress testing over the next several years, including by disclosing descriptions of additional material models and modeled loss rate disclosures for loan and non-loan portfolios.

Semiannual Review of the Safety and Soundness of the U.S. Banking System

The report that accompanies my testimony today is another tool to keep Congress, and the public, informed about our work, the banking system, and the role of both in supporting the broader economy.[3] The report focuses on the Federal Reserve's prudential supervisory activities.[4] As the report shows, the banking sector remains in strong condition, in line with strong U.S. economic performance, with lending growth, fewer nonperforming loans, and strong overall profitability.

Large institutions are well capitalized and liquid, and their capital planning and liquidity-risk-management processes are improving. Ninety-nine percent of regional and community banks are currently well capitalized, and supervisory recommendations made to smaller firms during the financial crisis have largely been closed. We are, however, very much aware of the dangers of complacency, and our report lists several priority areas of risk we will continue to monitor closely in the coming year, including cyber and information technology risks at supervised firms of all sizes.

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[3] Board of Governors of the Federal Reserve System, "Supervision and Regulation Report," November 9, 2018, www.federalreserve.gov/publications/supervision-and-regulation-report.htm.

[4] The Federal Reserve is also responsible for timely and effective supervision of consumer protection and community reinvestment laws and regulations. More information about the Federal Reserve's consumer-focused supervisory program can be found in the Federal Reserve's Annual Report to Congress. See section 5, "Consumer and Community Affairs," at https://www.federalreserve.gov/publications/annual-report.htm. The Federal Reserve also publishes the Consumer Compliance Supervision Bulletin, which shares information about examiners' supervisory observations and other noteworthy developments related to consumer protections. See https://www.federalreserve.gov/publications/consumer-compliance-supervision-bulletin.htm.

Improvements in Regulatory Efficiency

Improving regulatory efficiency is another core element of our current regulatory efforts. Tailoring regulation and supervision to risk has been a programmatic goal of Federal Reserve policy for more than two decades. The motivations are clear: supervisory resources are not limitless, and supervision is not costless, either to the public or to supervised institutions. Activities and firms that pose the greatest risk should receive the most scrutiny, and where the risk is lower, the regulatory burden should be lower as well.

This principle guided Congress and the federal banking agencies in designing the post-crisis regulatory framework, which imposed greater restrictions on larger, more systemically important firms and less intrusive requirements on smaller ones. It has also guided our implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA, or the Act).[5] On this front, we have made substantial progress:

- expanding eligibility of community banking firms for the Small Bank Holding Company Policy Statement, and for longer, 18-month examination cycles;[6]
- giving bank holding companies below $100 billion in assets immediate relief from supervisory assessments, stress testing requirements, and some additional Dodd-Frank Act prudential measures;[7] and

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[5] EGRRCPA, Pub. L. No. 115-174, 132 Stat. 1296 (2018).

[6] Board of Governors of the Federal Reserve System, "Federal Reserve Board issues interim final rule expanding the applicability of the Board's small bank holding company policy statement," news release, August 28, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180828a.htm.

[7] Board of Governors of the Federal Reserve System, "Statement regarding the impact of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA)," July 6, 2018, https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20180706b1.pdf.

- implementing changes to liquidity regulation of municipal securities and capital regulation of high-volatility commercial real estate exposures.[8]

The Board, Federal Deposit Insurance Corporation (FDIC), and Office of the Comptroller of the Currency (OCC) have also continued the work to significantly reduce the reporting burden on community banking organizations, altering reporting frequencies, items, and thresholds, while preserving the data necessary for effective oversight.[9] The agencies recently issued a proposal to reduce further reporting requirements for small depository institutions in the first and third quarters of the year. Under the proposal, around 37 percent of data items would not be required in those quarters.

Our most significant step to implement the Act came two weeks ago, when the Board issued two proposals to better align prudential standards with the risk profile of regulated institutions.[10] These proposals implement changes that Congress enacted this spring in the EGRRCPA. One of the proposals addresses the Board's enhanced prudential standards for large banking firms, and the other is an interagency proposal amending the regulatory capital and liquidity regulations that apply to large banking organizations. Both proposals separate large banking firms into four categories, using size as a relevant but not sufficient factor for increased regulatory requirements. Among the other factors that will now enter into this assessment are nonbank assets, short-term wholesale funding, and off-balance-sheet exposure. The changes

[8] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies propose rule regarding the treatment of high volatility commercial real estate," news release, September 18, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180918a.htm.

[9] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies issue proposal to streamline regulatory reporting for qualifying small institutions," news release, November 7, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20181107a.htm.

[10] Board of Governors of the Federal Reserve System, "Federal Reserve Board invites public comment on framework that would more closely match regulations for large banking organizations with their risk profiles," news release, October 31, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20181031a.htm.

would significantly reduce regulatory compliance requirements for firms in the lowest risk category, including most institutions with between $100 billion and $250 billion in assets. Firms with $250 billion or more in assets, or firms with assets between $100 billion and $250 billion that meet a risk threshold, will face reduced liquidity requirements. The proposals would largely maintain existing requirements for the largest and most complex firms.

These new categories represent a step forward in regulatory efficiency. They draw on our experience administering enhanced prudential requirements and other post-crisis measures. They recognize that other indicators of risk beyond size are appropriate to consider when determining if more stringent standards should apply to certain firms. They move toward a more risk-sensitive, nuanced framework, where riskier activities and a larger systemic footprint correspond to higher supervisory and regulatory requirements.

Apart from the requirements of the Act, we also recently proposed a new approach to calculating credit risk, known as the standardized approach to counterparty credit risk, or SA-CCR. The new approach would better account for the risks associated with derivatives exposures, including market practices that reduce risk, such as netting and initial margin.[11] We issued a proposal simplifying and tailoring requirements under the Volcker rule, to ensure that the most stringent requirements apply to the firms with the most trading activity, and that compliance is as simple and objective as possible. We also issued a rule limiting the exposure of large firms to a single counterparty, addressing a key source of contagion during the financial crisis. We have received thoughtful input from the public that will help inform our implementation of all of these measures.

[11] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies propose rule to update calculation of derivative contract exposure amounts under regulatory capital rules," news release, October 30, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20181030a.htm.

Finally, we have continued to engage with supervisors and central banks overseas. The ultimate goal of having an efficient and transparent regulatory system is to help the American economy--to enable banking organizations to offer safe, stable financial services to households and businesses around the country. But American businesses compete in a global marketplace, and as the financial crisis showed, when regulatory standards fall in other countries, Americans can pay the price. Engaging overseas, through forums like the Financial Stability Board and the Basel Committee on Banking Supervision, helps level the playing field--and it helps ensure that all countries, not just the United States, do their part to maintain and protect the global economy.

Our work to improve regulatory efficiency is not done, and we expect to make additional progress in the months ahead on a number of issues. In particular, we are working with our counterparts at the OCC and FDIC on a community bank leverage ratio proposal. We expect that this proposal would meaningfully reduce the compliance burden for community banking organizations, while preserving overall levels of capital at small banks and our ability to take prompt action when problems arise.

I look forward to continuing our efforts to make our regulatory framework simpler, more transparent, and more efficient--and I look forward to participating in the committee's oversight of those efforts. As Chairman Powell said at his swearing-in: "As a public institution, we must be transparent about our actions so that the public, through its elected representatives, can hold us accountable."[12] We will continue to do so to the best of our ability.

Thank you, and I look forward to answering your questions.

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[12] Jerome H. Powell, "Remarks at the Ceremonial Swearing-in" (speech at the Federal Reserve Board, Washington, DC, February 13, 2018), https://www.federalreserve.gov/newsevents/speech/powell20180213a.htm.

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August 28, 2018

The Honorable Jerome Powell
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, DC 20551

Dear Chairman Powell:

I am writing to express my concerns regarding the continued delay in implementing a real-time payments system.

The United States' outdated payment system imposes significant and unnecessary costs on Americans, leading consumers to incur billions of dollars a year in fees associated with the delayed movement of funds.[1] These costs are primarily borne by the millions of American families who live paycheck-to-paycheck, while they are rarely, if ever, applicable to wealthier families who never approach the lower bounds of their bank account. According to the Federal Reserve's own data, almost half of Americans report not being able to "cover an emergency expense costing $400, or would cover it by selling something or borrowing money."[2] For these Americans, settlement delays translate into real money.

Recent work from the Brookings Institute illustrates the impact of our slow payment system on lower-income Americans: "Unlike the Federal Reserve's zero lower bound of monetary policy, the lower bound faced by American households is easily breached. One cup of coffee on your debit card can break it. When you go negative, the penalties are severe: $35 or more on average in overdraft fees. These fees add up, to the tune of over $15 billion a year."[3]

Working families appreciate recent technological advances that allow for digital check capture and processing. Since the enactment of the *Check 21 Act*, the Federal Reserve has radically reduced its check processing footprint, from 45 different check processing centers to just one.[4] Yet the American public still does not receive its funds in real time.

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[1] Lane, Charles. *Why Slow Electronic Payments Can Cause Cash Flow Problems*, NPR, February 18, 2015. https://www.npr.org/2015/02/18/386769503/why-slow-electronic-payments-can-cause-cash-flow-problems
[2] Board of Governors of the Federal Reserve System. 2016. *Report on the Economic Well-Being of U.S. Households in 2015.* https://www.federalreserve.gov/2015-report-economic-well-being-us-households-201605.pdf
[3] Klein, Aaron. *How the Fed can help families living paycheck to paycheck*. The Brookings Institute, November 22, 2017. https://www.brookings.edu/research/how-the-fed-can-help-families-living-paycheck-to-paycheck/
[4] Board of Governors of the Federal Reserve System. *Regulation CC (Availability of Funds and Collection of Checks)*. February 28, 2017 https://www.federalreserve.gov/paymentsystems/regcc-about.htm

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In 2007, when the Federal Reserve reported to Congress on the wisdom of lowering check holding periods, as required under the *Check 21 Act*, the Fed found that electronic adoption "has not been sufficient to warrant changes in the maximum permissible hold periods mandated by the EFAA and Regulation CC."[5] However, today the Federal Reserve on its website states that, "the nation's interbank check-collection processes have become almost entirely electronic."[6] The Fed's website goes on to tell consumers that they must still wait for faster funds availability, "over the longer term, if Check 21 sufficiently increases the speed of check processing, the Board will reduce maximum hold times."[7]

The Federal Reserve's own electronic processing system, the automated clearing house (ACH) does not offer real-time payments, in stark contrast to central bank systems in the UK, Poland, Mexico, South Africa, Denmark, Singapore and more. Accenture Consulting's report on faster payments found that the United States has been slow to embrace real time payments in part because of the lack of central payments regulation.[8]

As you know, the Federal Reserve has been considering this issue for many years. The Fed convened the Faster Payments Task Force to engage a diverse array of stakeholders in advancing the work outlined in *Strategies for Improving the U.S. Payment System*. The Task Force concluded its work with a call for real-time payments by 2020, but no mandate for adoption. Recently the Treasury Department released a report in which it stated that: "Treasury recommends that the Federal Reserve set public goals and corresponding deadlines consistent with the overall conclusions of the Faster Payments Task Force's final report."[9]

The Bank of England adopted real-time payments in 2007. The Federal Reserve was once ahead of the curve in promoting the adoption of payment technology. It is unacceptable that the United States continues to lag behind its peers in modernizing our payment system. Each year, this failure imposes billions of dollars of unnecessary costs on millions of working families. I trust that you share this view and ask for your commitment to complete payment system modernization within a year. This reform is way overdue.

Please respond to the following by September 11, 2018:

1. What regulatory actions are needed in order to implement real-time payments?
2. What industry actions are needed in order to implement real-time payments?
3. What, if any, legislative actions are needed in order to implement real-time payments?

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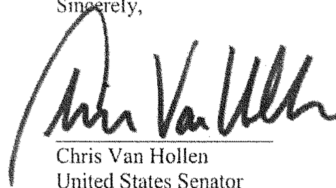
[5] Board of Governors of the Federal Reserve System. Report to the Congress on the Check Clearing for the 21st Century Act of 2003, April, 2007. https://www.federalreserve.gov/boarddocs/RptCongress/check21/check21.pdf
[6] Board of Governors of the Federal Reserve System. *Regulation CC (Availability of Funds and Collection of Checks)*. February 28, 2017 https://www.federalreserve.gov/paymentsystems/regcc-about.htm
[7] Board of Governors of the Federal Reserve System. *Regulation CC (Availability of Funds and Collection of Checks)*. February 28, 2017. https://www.federalreserve.gov/paymentsystems/regcc-faq-check21.htm
[8] Accenture Payments. *A Real-Time Revolution: Faster Payments in the US*, p. 2. October 6, 2016. https://www.accenture.com/t20161006T004905Z__w__/us-en/_acnmedia/PDF-34/Accenture-US-Faster-Payments.pdf#zoom=50
[9] U.S. Department of the Treasury, *A Financial System That Creates Economic Opportunities: Nonbank Financials, Fintech, and Innovation*, August 2018, https://home.treasury.gov/sites/default/files/2018-08/A-Financial-System-that-Creates-Economic-Opportunities---Nonbank-Financials-Fintech-and-Innovation.pdf,

4. Will you commit to taking action to mandate the recommendations made in the Final Report of the Faster Payments Task Force? Will you follow the Treasury's recommendation to set public goals and corresponding deadlines consistent with those recommendations? If so, what are those goals and dates?
5. Given the rapid acceleration in the use of electronic checking, why has the Federal Reserve not used its existing authority to lower check clearing wait times further? What public benchmarks for adoption will you provide for such acceleration?
6. Has the Federal Reserve conducted research on how real time payments could benefit the half of all American families who have difficulty coming up with $400 in an emergency?

Sincerely,



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October 29, 2018

The Jerome H. Powell
Chair
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

VIA ELECTRONIC SUBMISSION: regs.comments@federalreserve.gov

Re: Potential Federal Reserve Actions to Support Interbank Settlement of Faster Payments; Docket No. OP – 1625

Dear Chair Powell:

We are writing to urge the Federal Reserve to use its existing authority under the Expedited Funds Availability Act to mandate real time payments. Additionally, we urge the Fed to modernize its own infrastructure to be able to accomplish this goal with the Automated Clearing House system. Delay is costing Americans billions of dollars they do not have and contributing to the growing income inequality that the Fed rightfully agrees is harming our nation.

We appreciate the Fed's request for comments on improving its settlements infrastructure to support faster payments because of this initiative's impact on low and moderate income ("LMI") communities, especially those individuals that may live paycheck to paycheck. Of particular interest is Question 7 of the request for comments where the Board inquires whether updating its settlements infrastructure would help achieve ubiquitous, nationwide access to safe and efficient faster payments in the long run. The Board raises this question after noting that "the net effect on the efficiency of [a] faster payment environment would depend on the extent to which it generates societal benefits by improving…public access to safe and secure faster payment services."

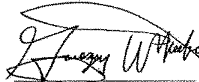
The impetus behind the Fed posing this question suggests the net benefit of a faster payments system is unclear. However, we believe a preponderance of evidence already exists that highlights the overwhelming public benefit of a faster payments system. Specifically, research conducted by the Brookings Institution, Pew Charitable Trust, Center for Financial Services Innovation and others has illustrated the prohibitively high costs of our nation's slow payment system and the sizable benefits for communities of color that would begin to

accrue savings from adoption of real time payments. The increased prevalence of overdraft fees, high cost small dollar credit, and check cashing has cost our constituencies tens of billions of dollars that a real time payments system would help ameliorate.

With the public benefits so clear and the costs of delay so dire, we reiterate our strong desire for the Board to move expeditiously toward implementing a faster payments system. Not only should the Fed's ultimate decision reflect the circumstances endured by our communities, it should also reflect the forward-thinking evolution of payment systems demonstrated abroad.

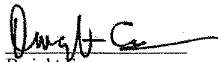
Sincerely,

Cedric Richmond
Chair, Congressional Black Caucus



Gregory W. Meeks
Co-Chair, CBC Economic Development and Wealth Creation Task Force

Joyce Beatty
Co-Chair, CBC Economic Development and Wealth Creation Task Force



Dwight Evans
Co-Chair, CBC Economic Development and Wealth Creation Task Force