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Senate Banking, Housing and Urban Affairs Committee Hearing
"Annual Oversight of Wall Street Firms"
December 6, 2023
Overview Provided by:

DeltaStrategy Group

OVERVIEW

The Senate Banking Committee held a hearing entitled "Annual Oversight of Wall Street Firms." The witnesses in the hearing were:

- Mr. Charles W. Scharf, CEO And President, Wells Fargo & Company
- Mr. Brian Thomas Moynihan, Chairman and CEO, Bank of America
- Mr. Jamie Dimon, Chairman And CEO, JPMorgan Chase & Co.
- Ms. Jane Fraser, CEO, Citigroup
- Mr. Ronald O'Hanley, CEO, State Street
- Mr. Robin Vince, CEO, BNY Mellon
- Mr. Davis Solomon, CEO, Goldman Sachs
- Mr. James P. Gorman, CEO, Morgan Stanley

Below is a summary of the hearing prepared by Delta Strategy Group. It contains several high-level takeaways from the hearing, followed by opening statements and witness testimony and a summary of the Q&A portion.

Key Takeaways

The following is a summary of some of the topics explored in today's hearing. Each is discussed in further detail in the Discussion section below.

- Today's hearing centered around the Basel III Endgame Proposal. Republican Members and witnesses alike generally stated that the proposal's capital requirement increases will create a burdensome regulatory environment for the American financial system. Republican Members raised concerns that the proposal will reduce banks' ability to lend to the public and small businesses, negatively impact farmers' ability to hedge their risks efficiently in derivatives markets, and potentially affect Treasury market liquidity.
- Witnesses highlighted the redundancy of the Basel III proposal, saying the banking system is in good health as demonstrated by the numerous stress tests their banks have passed. Witnesses generally clarified that increased capital requirements will

limit their ability to engage in public lending and discussed how the increased capital requirements will make hedging more expensive for American farmers. Witnesses said Basel III will put the U.S. financial system at a competitive disadvantage on a global scale.

- Democrat Members reasoned that recent bank failures indicate a need to reevaluate our capital requirements and that banks' negative reaction to increased capital requirements is an overreaction. Most Democrats did not question witnesses on the Basel III proposal specifically, and instead raised issues as to housing affordability for low-income and marginalized communities, AI, and cryptocurrency.

SUMMARY

Opening Statements and Testimony

Chairman Sherrod Brown (D-OH)

- We need strong capital requirements so big banks can fulfil their responsibility to ensure investors, not taxpayers, are on the hook when their risky decisions do not pay off. Basel III Endgame is a commonsense rule that will ensure banks are prepared to withstand losses from the riskiest financial decisions. Banks are heavily focused on maximizing quarterly profits at the expense of working families. Banks should be cutting prices for consumers, increasing opportunities for employees, and increasing diversity within their executive ranks.

Ranking Member Tim Scott (R-SC)

- Basel III Endgame will stop big banks from lending to small businesses or first-time home buyers as it requires more capital to be held on the sidelines and less available for lending. We need to be asking how this nightmare proposal will impact the everyday Americans. Basel III will limit the availability of credit for housing for those who need it most, severely restrict lending for small businesses, and cut into the retirement savings of Americans when they are dealing with higher prices and runaway inflation brought by the left. Two-thirds of all loans processed will be impacted by the Endgame Proposal. If regulation continues to increase the cost of providing a loan, I fear that banks will decrease lending across the country. Ultimately, decreased lending will reduce opportunity for Americans and create a concrete ceiling for low-income Americans.

Mr. Charles W. Scharf, CEO And President, Wells Fargo & Company

- Considering bank failures earlier this year like SVB, Wells Fargo, along with other banks here today, stood as a source of strength and stability. The strength of our institution allowed us to lend support to a smaller bank in a time of need and keep a challenge from becoming a much broader crisis. Our strength comes from strong financial profile, disciplined financial risk management and a commitment to run our business with high standards. We proudly serve one in three households and

10 percent of small businesses in the U.S. We remain committed to our employees and our customers.

Mr. Brian Thomas Moynihan, Chairman and CEO, Bank of America

- As Globally Systemically Important Bank (GSIB), we are subject to the highest capital liquidity requirements in all of our metrics exceed those requirements. While we have declared that we have the capital today to meet the proposed new capital rules, we remind you how important it is to have banks be able to position their balance sheets to help customers and clients in times of stress. We believe the capital accumulated by the industry should continue to serve the customers in America's economy and not be subject to regulatory capture.

Mr. Jamie Dimon, Chairman and CEO, JPMorgan Chase & Co.

- Despite zero evidence that banks are undercapitalized today, the Basel III Endgame would unjustifiably and unnecessarily increase capital requirements by 20-25 percent for the largest banks, which will create a harmful ripple effect on the economy, markets, businesses of all sizes, and American households. The Federal Reserve has not studied, contemplated, or shared how this proposal will impact our economy in a sufficient way. If the cost of hedging risk increases for producers and market participants, we will see this cost passed on to the consumer. This proposal will lead market activity to a shift to less regulated markets.

Ms. Jane Fraser, CEO, Citigroup

- Collectively, our banks serve as the engines for growth, supporting businesses and households. We are engaged in initiatives to increase access to credit and reduce the number of Americans who are unable to get credit. Every element of the Basel III Endgame proposal will make lending activities more expensive for small businesses and consumers. The most likely result of increasing the cost of banks to offer a variety of products is that it would move more activity into the less regulated nonbank sector, which carries its own risk for consumers and the stability of the financial system. It would also diminish our industry's ability to compete internationally, especially with our European counterparts.

Mr. Ronald O'Hanley, CEO, State Street

- Investors are at risk when there is not proper custody of assets. The collapse of FTX, which did not use bank custodians, demonstrates that more remains to be done to protect investor assets. In the emerging digital finance space, a comprehensive, effective regulatory framework is not yet in place, and the consequences are clear. I am concerned with the Basel III Endgame proposal which I fear could negatively impact the U.S. economy by limiting bank credit extension. I am concerned by the SEC's proposed Safekeeping Rule as it has no clear rationale, challenges the foundational elements of custody banking, and destroys the low-cost service we provide to investors.

Mr. Robin Vince, CEO, BNY Mellon

- It is critical that banks are prepared to prevent, respond, and recover from all different financial conditions. We need to have enough capital and liquidity to respond to market disruptions, which we have a strong track record with. U.S. leadership on distributed ledger technology (DLT), cyber security, and AI is important for our economy and regulators need to address these areas responsible way.

Mr. Davis Solomon, CEO, Goldman Sachs

- The Federal Reserve's stress tests have proven that all of us here have sufficient capital to withstand a severe global recession. The Basel III Endgame is significantly more stringent than any other jurisdiction. The proposal will nearly double the capital required for market making activity. As of the third quarter, the institutions most impacted by this proposal amount to two thirds of both lending and capital markets activity in the U.S. These punitive regulatory measures would quadruple our capital requirements for clean energy tax equity products, run the risk of harming U.S. competitiveness and capital market strength globally, and push activity overseas and outside of the regulated banking sector.

Mr. James P. Gorman, CEO, Morgan Stanley

- U.S. banks, who already undergo annual rigorous stress testing, are required to maintain specific capital buffers already. Additional increases are wholly unnecessary. Recent bank failures do not indicate a banking crisis. As it stands, the proposal would increase the cost of capital and borrowing across the economy, not just to large and small corporations, but to pensions, municipalities, and endowments. We hope the federal agencies will be open to changes and reviewing the industry's comments thoughtfully.

Discussion

Basel III Endgame Proposal

Brown (D-OH): Would your bank be able to meet Basel III Endgame capital requirements if implemented as proposed? *All witnesses:* Yes.

Scott (R-SC): Can you achieve increased capital requirements without negative consequences to the economy and lending? *Scharf:* We do have concerns that the proposal will lead us to increase prices or to reduce the amount we lend; *Moynihan:* This proposal will reduce our ability to serve clients. We need to be allocating our capital to serve the public; *Dimon:* This question should have been asked before it was proposed. A lot of our loans will not make sense anymore as they will become unprofitable.

Scott (R-SC): Will this have an impact on rural communities that need derivatives? *Fraser:* This will increase cost of borrowing for farmers and rural

communities. Hedging in derivatives markets will become much more expensive under the proposal.
Scott (R-SC): Will this proposal make our economy safer? *Soloman:* A wholesale increase of 25 percent capital on the largest banks is ultimately punitive to economic growth and does not strike the right cost benefit analysis. The system is already in good shape.

Rounds (R-SD): Will these proposals negatively impact farmers and small businesses? *All witnesses:* Yes.

Tillis (R-NC): Can you speak on operational risk of this proposal? *Gorman:* It makes no sense. You should not punish institutions for creating fee-based businesses.

Kennedy (R-LA): Have you ever failed a stress test or reached a point where your liabilities are greater than your assets? *Dimon*: No.

Kennedy (R-LA): In light of recent bank failures, do you think regulators have overstepped in giving the well-functioning banks? *Dimon*: This proposal is pushing business outside of the banking system, and it is adding risk about transparency.

Hagerty (R-TN): Do you think the impact of Basel III Endgame will be minimal? *All Witnesses:* No.
Hagerty (R-TN): How will this proposal impact not only your bank, but the markets and the economy more broadly? *Dimon:* It will diminish certain kind of mortgages, and particularly diminish mortgages for lower-income people. More broadly, it will have an extreme impact on market making. We do not even know the extent to which it will impact market liquidity.

Hagerty (R-TN): How will this proposal impact banking on an international basis? *Fraser:* This will impact U.S. banking competitiveness.

Hagerty (R-TN): How will this proposal impact capital markets? *Soloman:* The U.S. capital markets are the strongest capital markets in the world. I think it is one of our big competitive advantages. Raised capital requirements would push more activity into other jurisdictions, and it would make banks and other jurisdictions more competitive.

Britt (R-AL): Would this proposal have a minimal impact on Wells Fargo's lending? *Scharf:* No, it would impact the availability and pricing of credit. Additionally, when regulation like this has taken hold, you can see substantial migration out of the banking system.

Britt (R-AL): How will this proposal have a trickle-down effect? *Moynihan:* If you increase capital requirements increase by 25 percent, you will have to get a higher return which will trickle down to the consumer base.

Britt (R-AL): Will institutions below the $100 billion threshold feel the impact of Basel III? *All Witnesses:* Yes.

Britt (R-AL): Will this rule, as written, put the U.S. banking system at a disadvantage in the international playing field? *Fraser:* Yes.

Daines (R-MT): What are the consequences of this proposal on small businesses? *Dimon:* In terms of loans, we must charge more so we get our return across the capital. Secondly, the operational risk capital will increase the cost of simply holding the small business checking account or making a loan.

Daines (R-MT): How will this proposal impact how we finance the energy sector? *Dimon:* We must finance a transition to a greener energy system. We need secure, safe, and affordable oil and gas to do that.

Fetterman (D-PA): In light of SVB and other bank failures, can you explain why Basel III is not a good idea? *Moynihan:* It is our belief that these capital rules will not address that for smaller banks; *Dimon:* There were certain things that happened at SVB that should be addressed by regulation and the most important one is their taking on excessive interest rate risk. That has nothing to do with Basel III.

Lummis (R-WY): What does Basel III mean for smaller banks? *Dimon:* It will trickle down to higher cost for small businesses in one way or the other. It also changes the competitive landscape. It may in some ways make it harder for them to compete with us as opposed to easier.

Lummis (R-WY): What are the impacts of Basel III on hedging risks in derivatives markets? *Fraser:* Hedging plays an important role in risk mitigation. The increase in capital requirements will have an impact on the cost of hedging.

Lummis (R-WY): Why do we have to stay competitive on a global scale? *Fraser:* We account for over 50 percent of all of the capital activity and investment activity in the world. It is something we should be incredibly proud of, and it's something that we need to defend.

Treasury Market Liquidity

Rounds (R-SD): How could sustained high levels of debt have adverse effects on U.S. Treasuries market? *Soloman:* The growth in the U.S. Treasury debt has more than tripled over the past fifteen years. That debt will continue to grow as the cost of refinancing that debt also grows. This cost obviously hampers our ability to invest in other things, and it could also impact market liquidity as the cost of securities positions will rise.

Crypto

Warren (D-MA): Why is cryptocurrency an attractive tool for illicit activity? *Dimon:* I am deeply opposed to crypto. It has a special anonymity and speed of transactions that makes it attractive for illicit actors. If I was the government, I would shut it down.

Warren (D-MA): Do you think crypto companies should follow the same anti-money laundering rules that you do? *All Witnesses:* Yes.

AI

Warner (D-VA): What is your stance on AI? *Fraser:* It is both an opportunity and a threat. We all hope it will be an opportunity to improve the strength of the financial system. We have a lot of regulation that is in place right now that works very well to safeguard our financial system, but that regulation should continue to be used as a guide.

Smith (D-MN): How do you see AI being deployed internally? *Soloman:* We see it being a tool to increase efficiency for our clients, but it can also be used against us in terms of cyber security. We are thinking about how these tools can be used to attack our system, and we are trying to stay on the offense; *Fraser:* We want to use to defend against threats.