HFSC PANEL EXAMINES GLOBAL GOVERNANCE STANDARDS

EXECUTIVE SUMMARY

On September 11, the House Financial Services Subcommittee on Financial Institutions and Monetary Policy held a hearing on Transparency in Global Governance. During the hearing, lawmakers took anticipated party-line positions on the value of U.S. participation in international standards-setting bodies, as well as on more granular proposals such as Basel III Endgame Proposal and the Securities and Exchange Commission's (SEC) Climate Disclosure Rule.

Republicans on the panel sharply critiqued U.S. participation in multilateral financial institutions, criticizing them as avenues for foreign influence over the U.S. financial sector, and raising particular concern with climate-related regulations and the impact they may have on small and community banks. They relayed a desire for greater transparency in the interactions between U.S. regulators and these institutions, noting their concern with a lack of congressional oversight. In contrast, Democrats defended U.S. participation in the organizations, arguing that they are partially responsible for the success of U.S. capital markets. Subcommittee Democrats further argued for the importance of climate-related financial regulation, expressing concern at the potential for climate-induced economic malaise, and defending the SEC's Climate Disclosure Rule.

OPENING STATEMENTS

Ranking Member Maxine Waters (D-CA) (statement) accused the hearing's topic of being based on "conspiracy theories." She used the balance of her time to offer support for international standard-setting organizations.

Subcommittee Chair Andy Barr (R-KY) (statement) critiqued what he termed a "lack of transparency" in the interactions between U.S. financial regulators and global governance bodies, including the Bank of International Settlements (BIS), the Basel Committee for Banking Supervision (BCBS), and the Network for the Greening of the Financial System (NGFS). He called for these international bodies to make representatives available to Congress, and for Congress to be granted oversight authority over global governance bodies — which he views as neglecting public consultations. He attacked the Basel III regulations as an example of "foreign interference" with U.S. capital regulations. Chair Barr reiterated his desire for greater transparency, and called for colleagues to support his Congressional Banking Regulation Priorities and Accountability Act, which would improve transparency regarding financial regulators' dealings with international financial institutions.

Subcommittee Ranking Member Bill Foster (D-IL) noted the importance of multilateral financial organizations in maintaining U.S. economic leadership and global economic stability, recognizing that U.S. regulators enjoy outsized influence in the development of standards at these institutions. He took care to emphasize the latter point, noting that both the 2008 Recession and the covid-related economic shock saw cross-border economic contagion as a result of global economic interconnectedness. He emphasized the U.S. regulators are under no statutory obligation to adopt the policies recommended by these bodies, noting that the proposed Basel III endgame rules were based on public comments received by U.S. regulators rather than the plans of the BCBS. Ranking Member Foster acknowledged that Federal Reserve (Fed) Vice Chair Michael Barr has already announced the intention of financial regulators to make changes to the proposed regulations, and called for the U.S. to maintain its global leadership in financial regulations.

WITNESS TESTIMONY

Ms. Christina Parajon Skinner (testimony) of the Wharton School of Business, accused the governing bodies of international financial institutions of being "deeply antithetical" to U.S. laws governing transparency and agency decision-making, pointing out that international bodies are not accountable to Congress or judicial review for standards or rules until transferred into U.S. law. She declared the "impossibility" of disentangling aspects of rules shaped by foreign interests from the justifications offered by U.S. regulators seeking to promulgate the rule. She called for new procedures to improve transparency regarding any regulations originating from multinational institutions, and questioned the statutory authority that agencies must adopt rules and regulations agreed to at international forums.

Mr. Paul Kupiec (testimony) of the American Enterprise Institute (AEI), reiterated Ranking Member Foster's point that the agreements reached by members of global governance institutions are non-binding, and hold no legal standing, but are encouraged by multilateral financial organizations including the World Bank (WB) and the International Monetary Fund (IMF). He noted that the U.S. Congress has no role in this process, and these agreements are not required to serve the national interest of the U.S. Mr. Kupiec accepted that these agreements are not inherently harmful to economic growth, but also established that these agreements are narrowly targeted to address certain issues, often without a cost-benefit analysis on the implications of their adoption — critiquing rules regarding climate change in particular as being "politically-driven." Finally, Mr. Kupiec called for Congress to revisit the authorizing statutes of independent financial regulatory agencies to limit their ability to impose regulations on future risks that do not pose imminent threats to financial soundness, such as climate change.

Ms. Elizabeth Jacobs (testimony), of Third Generation Environmentalism (E3G), emphasized three points: (1) that U.S. participation in international financial institutions benefits its financial markets, allowing U.S. regulators to pursue U.S. interests internationally without surrendering domestic regulatory authority; (2) mitigating risks of climate change should be a top priority for the U.S. financial sector; and (3) there is transparency in international standards-setting which is supported by U.S. regulators. She applauded the strength of U.S. capital markets and noted the importance of

diversification in the global economy, recognizing the importance of U.S. participation in multilateral economic organizations for securing U.S. investors' access to information and competitive markets to reinforce that U.S. participation improves investor protections and secures economic growth. She emphasized that internationally negotiated regulations, as with any policymaking, are adopted only based on domestic statutory mandates and responsibilities. In conclusion, Ms. Jacobs emphasized that international standard setters are consistent with domestic principles and norms regarding transparency.

Discussion and Questions

Basel III Endgame

- **Rep. Scott Fitzgerald (R-WI)** expressed doubt regarding the statutory authority of U.S. regulators to participate in Basel III negotiations. Ms. Skinner agreed, arguing that the Basel III endgame proposal issued last year is inconsistent with Supreme Court precedent on the discretion of executive agencies.
- **Rep. William Timmons (R-SC)** called for the Fed to issue a complete re-proposal of the Basel III Endgame rule.

U.S. Participation in Global Governance Bodies

- Chair Barr questioned if including the NGFS in the U.S. policymaking ecosystem would add value to U.S. banking regulation and supervision Ms. Skinner answered that it is "unclear" why the Fed participates in the NGFS.
- Chair Barr asked if U.S. regulators consider any potential risks from adopting policies from global organizations. Ms. Skinner declared her belief that they do not and claimed that participation in these organizations poses risks to Fed independence and credibility, as well as U.S. economic sovereignty.
- Ranking Member Foster recognized that international coordinating bodies have no governing authority over U.S. financial services. Ms. Jacobs noted that U.S. participants in these bodies take a position of leadership, and as a result, the bodies represent the interests of the U.S. She elaborated that in the oversight of global markets and derivatives, as well as accounting and reporting, the Dodd-Frank Act and the Sarbanes-Oxley Act served as templates adopted by jurisdictions around the world — thus advancing U.S. economic interests.
- Ranking Member Foster asked if U.S. regulators should require explicit statutory authority to participate in international bodies, noting that none exists for crucial issues such as international supply chain fragility. Ms. Jacobs observed the importance of preserving the broad authority and discretion of financial regulators, as they must be able to anticipate financial stability risks in advance. To provide an example, she acknowledged the interconnection of insurance markets and banks as a possible source of risk important for regulatory consideration.
- **Rep. Bill Posey (R-FL)** asked if Congress should be concerned about the influence of global governance bodies over U.S. regulators, contemplating the possibility that they have been "captured" by foreign interests. Mr. Kupiec downplayed the potential for regulatory capture,

but emphasized the need for congressional oversight of regulatory participation in international organizations.

- Rep. Posey questioned if there are any confidentiality agreements between U.S. regulators, global bodies, or foreign governments. While Ms. Skinner relayed that she is unaware of any such agreements, she relayed that these institutions often observe practices such as Chatham House Rules, which create institutional cultures of confidentiality.
- **Rep. Roger Williams (R-TX)** questioned what risks are posed by financial regulators' participation in global governance bodies, as well as how to increase oversight over these bodies to protect U.S. interests. Ms. Skinner claimed that there is no check on the jurisdiction of these organizations, or even a universal definition of financial stability. She expressed worry that regulators could interpret themselves as having a "limitless" ability to engage in financial stability work.
- Rep. Williams questioned how smaller and community banks are affected by the standards set by international bodies. Ms. Skinner noted that small financial institutions are not meant to be covered by rules intended for internationally active banks, and that it is difficult for small banks to abide by regulations such as the SEC's Climate Disclosure Rule.
- **Rep. Barry Loudermilk (R-GA)** and Ms. Skinner expressed their belief that global economic institutions exercise influence over U.S. economic policy, to the detriment of the U.S. economy, banking system, and financial system.
- **Rep. Sean Casten (D-IL)** questioned the economic consequences of a U.S. withdrawal from multilateral organizations. Ms. Jacobs emphasized that the success of U.S. capital markets is, in part, based on U.S. regulations and the ability of regulators to "export" these to other markets.
- **Rep. Young Kim (R-CA)** acknowledged the importance of U.S. participation in global bodies, but echoed concerns raised by her Republican colleagues regarding foreign influence and transparency.
- Rep. Kim asked about the negotiation process at the BCBS to reach an agreement on rulemakings. Ms. Skinner relayed that the inner workings of these organizations are opaque, and it is difficult to ascertain how agendas are set or working groups constituted.
- Rep. Kim critiqued the BCBS' harmonization efforts, noting differences in the regulations adopted by individual member-states. Ms. Skinner noted that the BCBS is essentially a forum for political negotiations, and individual countries implement rules as their regulators see fit.
- Rep. Kim expressed concern at the lack of a universal definition for terms such as "financial stability" or "safety and soundness." Ms. Skinner agreed, arguing that the lack of definition allows regulators to expand their jurisdiction.
- Discussing how these international bodies impact access to capital with Rep. Kim, Ms. Skinner argued that small and community banks are forced to comply with additional regulations, thus increasing the costs of doing business and reducing the availability of financing.
- Rep. Timmons criticized the participation of U.S. regulators in international bodies, and joined calls for the passage of the Congressional Banking Regulation Priorities and Accountability Act.

Climate Change

- Chair Barr accused international bodies of seeking to force the Fed to engage in efforts to favor or disfavor certain assets on the basis of purported risk from climate change, and questioned if it has the statutory authority for such acts. Ms. Skinner asserted her belief that the Fed does not have the authority to "proactively green" the financial system, and that agencies broadly do not have the discretion to break with "political consensus" in the U.S.
- Chair Barr pondered what risks could arise from incorporating "speculative" models regarding climate change into the issuance of principles, guidance, or regulations aimed at directing credit towards green activities. Mr. Kupiec argued that "politically-driven" regulations are destabilizing, as they may change from administration to administration. He claimed that these regulations could raise the costs of borrowing and slow economic growth.
- Chair Barr claimed the SEC's Climate Disclosure Rule is one possibly adopted under foreign pressure or influence.
- Rep. Williams accused U.S. financial regulators of increasing partisanship, especially regarding climate and the environment. Mr. Kupiec agreed, reiterating his belief that "partisan" regulations are a threat to the U.S. economy as a result of their inherent instability between administrations, noting that the Financial Stability Oversight Council (FSOC) did not consider climate change to be a systemic risk until directed by executive order. He declared that their attention to climate risks has distracted FSOC from other threats to economic stability.
- **Rep. Juan Vargas (D-CA)** asked the witnesses to assess systemic risks posed by climate change. Ms. Skinner argued that it is not a risk to the U.S. financial system, saying that it fails to present a verifiable credit risk that could cause the insolvency of a large bank. She asserted that climate risks would need to be paired with a wide range of the private sector becoming unable to repay loans due to large-scale climate-related physical damage or destruction across the world, which she termed "very unlikely." Ms. Jacobs disagreed, saying that providing information to market participants will help to manage these risks and that the climate disclosure rule was driven by investor demand.
- Rep. Loudermilk asked if the Fed's statutory authorization provides a mandate to engage in climate policy. Ms. Skinner expressed her belief that the Fed does not have the authority to preemptively try to "green" the economy, and attempts to do so undermine its authority and independence.
- Rep. Fitzgerald asked what role Congress can play in "resisting" European Union (EU) climate policies, which he claimed are being imposed on the U.S. Ms. Skinner reiterated Chair Barr's call to enact the Congressional Banking Regulation Priorities and Accountability Act.
- **Rep. Ayanna Pressley (D-MA)** highlighted that the Fed's recent stress test found that the six largest U.S. banks are unprepared to manage the consequences of climate change, and questioned if this analysis should be expanded. Ms. Jacobs agreed that the Fed should expand its climate risk scenario analysis to include all large banks that are stress-tested annually.
- Rep. Pressley questioned what regulatory steps adopted internationally should be explored by U.S. regulators. Ms. Jacobs highlighted the importance of enhancing climate scenario analyses, as well as cross-sector stress tests. She also noted her hope for greater disclosures

in the banking and insurance sectors, with proposals available for public comment at this time.