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The resolution of large regional banks and lessons learned with Martin Gruenberg

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INTRODUCTION

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HARRIS: Good afternoon, everyone. Thank you for coming. My name is Ben Harris, and as of this very morning, I'm the vice president and director for Economic Studies at the Brookings Institution. Today marks my fifth stint at the Brookings at Brookings over the course of my career and is a true privilege and honor to have the opportunity to again rejoin this esteemed institution.

There are many reasons why I found a return to Brookings appealing, but a major motivation was to be part of events like the one we're hosting today. FDIC chairman Marty Greenberg, who will be formally introduced by Senior Fellow Aaron Klein in a few moments, has been at the forefront of financial regulation for decades and was one of the key officials who helped mitigate the fallout from the Silicon Valley Bank and Signature Bank failures earlier this year. We are very, very lucky to have him with us today.

I suspect that this afternoon's event must feel like a bit of a victory lap for the FDIC chair, given that in 2019 he sat in this very room and warned in great detail about the risk of failure by a large regional bank. In his remarks, which are required reading for anyone hoping to better understand this issue, Gruenberg warned about the financial and economic risks posed by the failure of these banks and highlighted the destabilization risk of outsized uninsured deposits, while he also cautioned that specific regulatory actions taken in 2019 would weaken regulators ability to respond to a crisis if and when they would occur. It's as prophetic a speech as you'll see in public policy. Of course, of course, Chair Greenberg's track record shows he is more than just a financial crisis clairvoyant, but that he has also played a massive role in helping resolve this spring's banking crisis.

In March of this year, when the SVB concerns materialized at lightning speed, I was serving as the chief economist and assistant secretary for economic policy at the Treasury Department. My role at Treasury meant that I was afforded a front row view to the crisis and had a deep appreciation of the economic risks associated with widespread regional bank failures. That experience left me with two broad takeaways. The first is that that precarious weekend in March 2023 was the most concerned I had been about the state of the U.S. economy from January 2021 through today. The statement is saying a lot, as this period included the omicron and delta waves, Russia's invasion of Ukraine and the subsequent three-month 30% increase in global oil prices, year over year CPI inflation topping 9% in June 2022, and widespread supply chain disruptions that threaten to leave store shelves bare around the holidays. Our financial sector and macro economy were on a razor's edge for several weeks and was certainly not implausible that last spring would have been the start of a painful recession ignited by a global run on U.S. banks. The second takeaway was that policy leaders deserve noble praise for threading the needle in March 2023 and preventing widespread bank failures. From my personal perspective, the experienced guidance of regulators and banking officials was crucial to preventing a broader crisis, and that less adept leadership could have led to a loss in confidence in the banking system and a severe financial disruption. Policymakers often don't get credit for crisis averted. But here, the decisions by frontline regulators, namely namely Yellen, Greenberg, Brainard, and Powell and their staffs, collectively stabilize the financial system and prolonged this ongoing economic expansion.

To close, let me note that events like today highlight the value of the Brookings Institution in particular, and the broader think tank community in general. Brookings scholars identify and tackle our most pressing economic and social challenges, ranging from health care to tax policy to financial regulation, and propose solutions founded in rigor and credibility in the policy arena. Being an effective policymaker means a commitment to continue learning and a drive to seek wisdom from policymakers like Marty Greenberg, which is why today's event is so relevant. Thank you to both Aaron Klein and Marty for making this event happen. I very much look forward to this important discussion. I'll now turn it over to Brookings Senior Fellow Aaron Klein. Thank you.

KLEIN: Thank you very much, Ben. Thank you all for joining us in person online and through however you find this. I am a senior fellow and the Miriam K. Carliner chair in Economic Studies here at the Center on Regulation and Markets. And in financial regulation, there's a cycle. There's a crisis, there's new regulation, then there's deregulation. Then there's a crisis. That cycle has played on for a long time. We can debate what contributes to what, why these cycle or phenomenon happen, but they do. We here at the Center on Regulation and Markets are focused on this throughout that cycle. It becomes very trendy to lean in when there's a crisis. And as the crisis is forgotten, the attention goes away. The issues remain. As we try to get a better and more stable and secure and stronger economy, it requires a better financial system and higher quality regulation. The fact that the chief economist at the Treasury Department was more concerned in March during this financial crisis than all the other litany of economic threats ought to underscore why financial regulation is so critically important and why we keep returning to this.

It is my honor and privilege to return to the Brookings stage, FDIC Chair Martin Gruenberg. To give you a little background and history on on Marty, Marty has been a board member of the FDIC since 2005 for 18 years, which is the FDIC turns 90 this year. So roughly about 20% of the FDIC's history, Marty has been there. He has seen it. 2005 was the year when he was first confirmed. It was also the first year in American history without a single bank failure. 2006 was the second year. People mistakenly took the impression that the absence of any bank failures meant that we were well-regulated. I think nobody here would dispute the idea that the financial system started 2007 in a place of safety, soundness, strength and quality regulation. So, by the way, the next year in American history without a single bank failure? 2020. 2021. And here we are are, 2023, having gone through this crisis in the spring, and the question is not, we'll talk a bit about what caused it, what happened, but what are we going to do going forward. And I can think of nobody more well-situated, more experienced, more credible and who's thought through and experienced these issues throughout the entire cycle than Chairman Gruenberg. And I'm very eager and intrigued to hear how he's going to approach this, given the experience of the spring, given the experience he's had before, and given the very issues he's raised on this stage, as Vice President Harris recalled, in 2019, when he warned that our system had become overconfident, that we had, that we were in a good place to deal with the failure. Because whatever you think about how the failure was dealt, it, it was very clear that we were not in a structurally strong place to handle what started out as one failure and very quickly ensconced other massive financial institutions. So, Mr. Chairman, I think the floor is yours and we're all eager to learn what you think we ought to do to make the system better, stronger and more resilient in the future.

GRUENBERG: Good afternoon, everybody. Let me congratulate you on being here in Washington in the middle of August. I honestly didn't expect this larg a crowd this this time of the year. So I appreciate your coming. And let me also thank Ben and and Aaron for their very kind comments. As a bank regulator, candidly, I'm not used to that. So I'll take it. I'll take it where I can get it. And let me begin by thanking the Brookings Institution Center on Regulation and Markets and my friend Aaron Klein for inviting me to speak here today.

As both Ben and Aaron mentioned, four years ago, I did have the opportunity to speak at Brookings about an underappreciated risk, the resolution of large regional banks in the United States. For better or worse, it's probably fair to say that risk is perhaps better appreciated today than it was a few years ago. The key point made in that speech was that while regional banks may not be as large and complex and internationally active as the so-called global, systemically important banks that - the GSIBs - they would pose distinct and significant challenges in resolution that could raise serious financial stability risks. That was the key message of that speech. In particular, the speech pointed out that the heavy reliance of regional banks on uninsured deposits for funding was a core vulnerability. That reliance has the potential to create a destabilizing contagion effect on other banks, if one regional bank were to fail and uninsured depositors took losses. That was the key point. And we had evidence. I didn't make it up. There was evidence to support this. In order to illustrate the point, the speech contrasted the failures of Washington Mutual Bank and IndyMac Bank during the global financial crisis of 2008. As both Aaron and Ben mentioned, I've been around long enough to remember to remember those experiences. Washington Mutual. A $300 billion thrift institution was the largest bank failure in U.S. history, yet it was resolved at no cost to the deposit insurance fund, and uninsured depositors suffered no losses. IndyMac, which was a $30 billion thrift, a 10th of the size of Washington Mutual, yet it proved to be the costliest failure in FDIC, FDIC history up to that point, at over $12 billion, and uninsured depositors suffered losses. Now, a number of reasons led to the differing outcomes in those two cases. But a particularly important one that I'm going to talk about today was that Washington Mutual had sufficient unsecured debt to absorb all of the losses of the bank. And IndyMac had none.

If we had any doubts about the challenges in resolving regional banks and the potential for significant adverse impact on the financial system, those doubts were dispelled by the failure this spring of three large regional banks: Silicon Valley Bank, Signature Bank, and First Republic Bank. While the FDIC resolved all three of those institutions in a manner that mitigated systemic risk, that outcome was by no means certain. In particular, the resolution of Silicon Valley Bank and Signature required the use of extraordinary authority by the FDIC, the Federal Reserve, and the secretary of the Treasury, the so-called systemic risk exception under the Federal Deposit Insurance Act to protect uninsured depositors at those institutions, setting aside the least-cost requirement to the deposit insurance fund. That experience should focus our attention on the need for meaningful action to improve the likelihood of an orderly resolution of large regional banks under the Federal Deposit Insurance Act without the expectation of invoking the systemic risk exception. So today, I would like to revisit this issue of the resolution of large regional banks in the United States in light of our recent experience. And in particular, I believe there are important changes to capital regulation, resolution planning requirements, including long term debt, bank supervision, and deposit insurance pricing that would make a repetition of what occurred much less likely.

So just to provide context - people's memories are remarkably short, even two or three months - just to provide context, it may be worth recounting the events of earlier this year, just as a reminder. When Silicon Valley Bank failed overnight on Friday, March 10th. I do remember it well. The FDIC initially established what we call a deposit insurance national bank under FDIC control so that depositors would have access to their insured funds o the Monday after failure. Uninsured depositors would have access to a substantial portion of their funds through the payment of what we call an advance dividend. But a portion of those uninsured deposits would be held back in the receivership and would experience losses depending on the losses to the deposit insurance fund. That's the way it normally works. Now, as it turned out, the prospect that uninsured depositors at Silicon Valley Bank would possibly experience losses alarmed uninsured depositors at other similarly situated banks, and they began to withdraw funds. Signature Bank and First Republic Bank experienced heavy withdrawals. A contagion effect became apparent at these and other banks. There was clear evidence that the failure of a regional bank in which uninsured depositors faced losses could cause genuine systemic disruption. So in response on Sunday, the U.S. authorities invoked the systemic risk exception to the FDIC's least-cost test. This allowed the FDIC to fully protect all depositors at Silicon Valley Bank and its signature bank. They were placed into separate bridge banks under FDIC control. Signature Bank was sold a week later to Flagstar Bank, a subsidiary of New York Community Bank. And Silicon Valley was sold two weeks later to First Citizens Bank of North Carolina. And as you all know, First Republic Bank in California also experienced large deposit outflows that weekend but managed to survive at least the weekend. The bank spent the next few weeks trying to raise capital but was unsuccessful. On May 1st, the state of California closed the bank. The FDIC had time before the bank was closed to conduct a competitive bidding process, which resulted in JPMorgan Chase submitting the least cost bid and purchasing all of the assets and assuming all of the deposits to First Republic. The winning bid covered all uninsured depositors under the least cost test and did not require a systemic risk exception. So, in brief, that was the story in March and April.

So, what should we learn from this episode? What should we take away from this experience? The three banks that failed this spring shared common characteristics that made them more vulnerable to a run. Reports from the Federal Reserve and the FDIC on the failures of Silicon Valley Bank and Signature Bank, respectively, found that they were poorly managed and not responsive to supervisory feedback, and their supervisors were not forceful enough in requiring them to take corrective measures. In addition, the three banks grew rapidly and relied heavily on uninsured deposits for funding. Two of them had uninsured deposits approximating 90%, about 90% of their funding, and the third approached 70%. Further, two of them had unrealized losses on securities or low-yield loan portfolios that were large relative to their capital base. All three had little or no long-term debt outstanding. These characteristics proved to be a toxic combination when each bank faced stress. In addition, the resolution plans that had been received from two of the three banks were limited in content. So there are some obvious lessons here that we now have an opportunity to address. And that's that's what I want to talk about.

Let me begin by capital requirements and the capital treatment of these unrealized losses on the balance sheets of the banks. In late July, the three federal banking agencies issued a notice of proposed rulemaking to implement the Basel III capital rule. There's a lot in that proposal, as you probably know, but one in particular is a step toward addressing one of the key vulnerabilities of the recent failures. Under the proposal, unrealized losses and available for sale securities would flow through regulatory capital for all banks with over $100 billion in assets. That means, just to be clear, that those banks, in order to maintain their capital levels, would have to retain or raise more capital as these unrealized losses occur. It's worth noting in regard to Silicon Valley Bank that although its failure was caused by a liquidity run, the loss of market confidence that precipitated the run was prompted by the sale of available for sale securities at a substantial loss that raised questions about the capital adequacy of the bank. This loss of confidence followed the announced self-liquidation of another local institution, Silvergate, a day earlier, in case you all had forgotten about that institution. That bank had announced its sale of available for sale securities at a substantial loss and planned capital raise just a week earlier. Had Silicon Valley Bank been required to hold capital against the unrealized losses on its available for sale securities as the proposed Basel III framework would require, the bank might have averted the loss of market confidence and the liquidity run. That's simply because it would have held more capital against those assets. Not complicated, but relevant. In addition to capital, the banking agencies will, in the near future propose a long-term debt requirement for banks with $100 billion or more in assets. Let me talk about this a bit. In October of last year, the FDIC and the Federal Reserve jointly issued what's called an advance notice of proposed rulemaking on resolution-related resource requirements for large banking organizations. Based on the feedback from that ANPR, advance notice of proposed rulemaking, the agencies, and we'll be joined by the Office of the Comptroller of the Currency. So, the three agencies together have worked to develop a proposed rulemaking and the proposed -- then the three agencies look forward to acting on that proposal soon. The agencies expect to propose that each covered bank be required to issue long term debt sufficient to recapitalize the bank in resolution. While many regional banks have some outstanding long-term debt, the new proposal will likely require issuance of new debt. We expect the proposal to provide for a reasonable timeline to meet the debt requirement and to take into account existing debt outstanding. As indicated, the proposal is likely to apply to all banks over $100 billion in assets, an outcome certainly influenced by the events of earlier this year. Such a long-term debt requirement bolsters financial stability in several ways. First, it absorb losses, it absorbs losses before the depositor class, the FDIC and uninsured depositors take losses. That lowers the incentive for uninsured depositors to run. Second, even if the institution fails, the buffer of long-term debt reduces cost to the deposit insurance fund and makes it more likely that a closing weekend sale could comply with the statutory least-cost test and avoid the need for a systemic risk exception. Further, it creates additional options in resolution, such as recapitalizing the failed bank under new ownership, or breaking up the bank and selling portions of it to different acquirers as an alternative to a merger with another large banking institution. Further, since this debt is long term, it will not be a source of liquidity pressure when problems become apparent. Unlike uninsured depositors, investors in this debt, no, they won't be able to run when problems arise. This gives them a greater incentive to monitor risk in these banks and exert pressure on management to better manage risk. And finally, because these instruments are publicly traded, their prices serve as a signal of the market's view of risk in these banks. So that's long-term debt.

Now, let me turn to resolution plans, which I think are a critical complement here. An important complement to a long-term debt requirement is meaningful resolution plans for these large regional banks. There is currently a requirement for these banks to file plans that address the resolution of the insured depository institution under the Federal Deposit Insurance Act. Just to be clear, that's separate from the Dodd-Frank Act Title I resolution plans that apply to the largest bank holding companies. The FDIC will soon proposed changes to the IDI plan requirements that would make them significantly more effective. And really want to walk through this because to me, this is an important part of addressing this issue. The IDI plan or insured depository institution plan rule was first adopted in 2011. It requires banks with over $50 billion in total assets to periodically submit resolution plans to provide the FDIC with information about the bank that is essential to effective resolution planning and to support the execution of a resolution if necessary. The rule requires covered banks, and I quote, to develop and submit detailed plans demonstrating how they could be resolved in an orderly and timely manner in the event of receivership. Over the years, the FDIC has given banks feedback and guidance with respect to their plans and has considered different approaches to the planning requirements. The FDIC has continued to consider ways to improve the effectiveness, effectiveness of these plans and to set clear expectations for banks with respect to their content. We have determined that a rulemaking is the best approach to meet those goals in a way that is both transparent and effective. And to that end, the FDIC plans to issue a notice of proposed rulemaking in the near future that will be a comprehensive restatement of the rule for notice and comment. In developing the proposal, we have incorporated the most useful elements of past feedback and guidance, as well as lessons learned from past plans and resolutions. Institutions, I should note, under $100 billion can also present resolution challenges, and we do not propose requiring full plans for these banks under this strengthened rule. We will propose requiring certain information from banks over $50 billion to inform our resolution planning. The importance of this work was underscored this spring. While Silicon Valley Bank and First Republic had been required to file resolution plans which provided basic information that was useful, far more robust plans would have been helpful in dealing with the failure of these institutions. Signature Bank failed just before it would have been required to file its first resolution plan in June. Let me give some examples. Some of the elements that would have been helpful this spring to include in these plans would be the bank's capability to promptly establish a virtual due diligence data room and populate it with enough information for interested parties to bid on the bank or certain of its assets or operations. It's a threshold capability to allow an effective bidding process. Maintenance of information necessary for operational continuity of the bank, including a more thorough description of key personnel and retention plans. Critical third-party and shared services and payments and trading activities. And third, the ability to describe communications systems and strategies for reaching internal and external key stakeholders in the event of a resolution. These were all things we had to deal with, frankly, in March and April. While each of the three bank failures this spring ultimately concluded in a sale to a single acquirer, it is also clear that a sale to a single acquirer, given the size of these institutions, may not always be possible. Therefore, the proposed rule will seek to expand the options available to the FDIC. The proposed rule would require a bank to provide a strategy that is not dependent on an over-the-weekend sale. It would require a bank to explain how it could be placed into a bridge, how operations could continue while separating itself itself from the parent and its affiliates, and the actions that would be needed to stabilize a bridge. The rule would also require banks to identify franchise components such as asset portfolios or lines of business that could be separated and sold in order to provide additional options for exiting from resolution by disposing of parts of the bank to reduce the size of the remaining institution and expand the universe of possible acquirers. A stronger resolution planning requirement for large regional banks, combined with a long-term debt requirement, would provide a much stronger foundation for the orderly resolution of these institutions. It's really as straightforward as that.

So finally, the bank failures earlier this year highlighted the vulnerabilities that can result when banks have a heavy reliance on uninsured deposits for funding. The significant proportion of uninsured deposit balances exacerbated deposit run vulnerabilities and made all three banks susceptible to contagion effects from the quickly evolving financial developments. Heavy reliance on uninsured deposits for funding carries a number of liquidity risks, just to be clear. First, large uninsured depositors such as businesses, nonprofit organizations and wealthy depositors are likely to be more sophisticated and more attuned to market developments than retail depositors, and thus may be more likely to withdraw funds quickly. Second, such deposit accounts are often concentrated in a relatively small number of depositors, also making them more susceptible to runs. Third, electronic banking services allow for the instantaneous withdrawal of large uninsured deposits. And finally, liquidity runs on uninsured deposits can be amplified and exacerbated through social media. For the banking industry as a whole, reliance on uninsured deposit funding has been increasing significantly. The FDIC report, "Options for Deposit Insurance Reform" that will be released in May notes that in the aggregate, uninsured deposits rose from about 18% of domestic deposits in 1991 to nearly 47% at their peak in 2021, higher than at any time since 1949. The aggregate concentration of uninsured deposit funding has come down slightly from 2021, but still remains high. Concentrations of uninsured deposit funding are more common among large banks. At year end 2022, banks with more than $50 billion in assets were approximately 1% of all banks in the United States, but held nearly 80% of all uninsured deposits, and the majority of domestic deposits were uninsured. The majority were uninsured for more than 40% of those institutions. Although reliance on uninsured deposits is a more common issue for large and for larger banks, it is not exclusively a large bank issue. Uninsured deposits comprise the majority of domestic deposits for about 15% of banks, between $1 billion and $50 billion in assets. As noted previously, uninsured deposit funding tends to come from a relatively small number of deposits. You get the drift here. At the end of 2022, less than 1%, less than 1% of all deposit accounts had balances above the deposit insurance limit of $250,000, but accounted for over 40% of banking industry deposits. At the time of its failure, Silicon Valley Banks' ten largest deposit accounts collectively held $13.3 billion in deposits. So needless to say, more forward-leaning supervision of large regional banks is certainly a key lesson from the events earlier this year. In particular, the FDIC is reviewing whether its supervisory instructions on funding concentrations should be bolstered to better capture risks related to high levels of uninsured deposits generally, or types of deposits more specifically, such as business operating account deposits. For example, FDIC examiners instructions could establish a specific threshold for concentrations of uninsured deposits, which would require examiners to devote supervisory attention to the concentration. Regulators and other stakeholders may also benefit from more granular and more frequent reporting of deposits. And needless to say, these are matters of priority attention for the FDIC. In addition, I might add, risk-based deposit insurance pricing can deter banks from relying too heavily on less stable sources of funding, such as uninsured deposits, and can maintain fairness by charging banks with unstable funding sources for the risk they pose to the deposit insurance fund. For this reason, it is worth reexamining the ways in which deposit insurance pricing captures the risks of uninsured deposits. Calibrating precisely the risk of uninsured deposits is a challenge. Therefore, while deposit insurance pricing may be a useful tool, it is probably best seen as a complement to other tools that mitigate the risk of overreliance on uninsured deposits.

So, in conclusion - there is an end here - if I may, in conclusion, the failure of three large regional banks this spring and the need to exercise a systemic risk exemption to protect uninsured depositors at two of them demonstrated clearly the risk to financial stability that large regional banks can pose. It makes a compelling case for action by the federal bank regulatory agencies to address the underlying vulnerabilities that made the failure of these institutions possible. The federal banking agencies have the statutory authorities to address these vulnerabilities. As I have outlined, the agencies' actions include requiring long term debt, capital recognition of unrealized losses for available for sale securities, strengthened bank resolution plans, as well as enhancing supervisory attention to uninsured deposit concentrations and considering adjustments to risk-based pricing for deposit insurance. Once implemented, these measures will mitigate these risks and enhance the stability and resilience of the U.S. banking system. These are perhaps lessons we should have learned from the 2008 financial crisis. However, the events of this year provide us with another opportunity, this time, if I may say, I don't think we're going to miss. Thank you all very much.

KLEIN: Here, come on down, Mr. Chairman. You've made a lot of news and gave us a lot of room to think for a Monday in the middle of August. Let's start with with where you lined up, which is you juxtaposed IndyMac and WAMU's failures in the beginning and the value of having that subordinated debt kind of making a huge difference. So imagine that your speech in Brookings 2019, that requirement had been put in place, the requirement that's coming from the three regulators for the unsecured debt. Would that have been enough for SVB to avoid needing the systemic risk resolution to you?

GRUENBERG: If I may say, you're raising a hypothetical, but I think without a doubt it would have helped. And I sort of tried to outline that. You can't say with certainty it would have avoided the failure. I think, had they had a substantial amount of unsecured debt, that would have been reassuring to uninsured depositors and might have influenced their behavior. And even if it had not been sufficient to avoid the run, and the bank still failed, having that unsecured debt as a buffer would have mitigated the loss to the deposit insurance fund and might have put us in a position to avoid exercising a systemic risk exception. So whether it could have avoided the failure altogether, we can't say. I think there's a chance of that. And even if it wouldn't have, it could have been quite beneficial in mitigating the the impact of the failure. So the, you know, the common sense of extending such a requirement to the regional banks to me is is is pretty persuasive.

KLEIN: So, yeah, to be clear, I think the failure was a good thing in the sense that that bank deserved to fail. It was a poorly managed institution with an unstable funding base and a bad business model. Stopping bank failure is not - speaking just for myself - is not my goal. Stopping the use of systemic risk exception is a, is very different. And I take it that the it is your belief that the imposition of this loss absorbing capital will have impacts on both, but particularly on stopping the need for systemic risk exemption authority and creating enough buffer above where the taxpayer and the FDIC fund lay.

GRUENBERG: Yeah, I think I think that's true. But if I may say, sitting where I sat, the possibility of avoiding the failure and the disruption to the system, if that were, you know, an alternative scenario, that that would have been of great value to the system, to the financial system and to the economy. So if I may say Aaron, I, I don't discount that potential benefit as well.

KLEIN: I speaking of benefits you there's going to be a lot of focus on TLAC. It's the first question. It's been kicking around for a long time. It's had a lot of area in its use. You said you already had an ANPR out about it. Now you're moving - advanced notice of public rulemaking - now you're moving to a notice of public rulemaking, and in essence, the rule. The second part has to do with the resolution plans and the upcoming rule on that. And it's easy to think of those separate and apart and not together. What do you think the combinatory value is of having both of these together as opposed to just thinking, okay, now we have loss-absorbing debt, now we have resolution plans. This adds, this adds that; in economics we sometimes look for interactive variables in our analysis. What are the combinatory effects?

GRUENBERG: Look, from from the standpoint of the agency actually responsible for executing the resolution in an orderly way, having the loss-absorbing resource in a sense is a threshold which you can't overstate the value of having the information and the strategic thought and the optionality prepared ahead of time that can be used as a, in deploying the additional loss-absorbing capability, which is why we place a lot of importance on the two going together, acting on the long-term debt requirement and significantly strengthening the resolution plan requirement for these regional regional banks as really going hand in glove and particularly giving us as the agency the information and the strategic thinking well ahead of time. That would just put us in a much stronger position. I think taken together, it's just common sense, a much, much stronger foundation for dealing with the possible failure of one of these institutions. And look, if we in addition and we are, have already proposed it, requiring capital against these unrealized losses, let me put it this way - hypothetically, just to be clear - but if we had had an offer of unsecured debt for Silicon Valley Bank, if we had had a robust resolution plan and if Silicon Valley Bank had been required to hold capital ahead of those unrealized losses, you know, it's hypothetical, but we could have had a different scenario. I mean, I think that's plausible. I think that's plausible. And given the costs and risks associated with the failure, potential failure of institutions of this size, you know, the policy case for having these requirements, to me, as I say, is is really pretty compelling.

KLEIN: You make the point about speed and time. And I struggle with this because every day has had 24 hours, whether it was Monday, March 8th or Friday, March 11th, they both had 24 hours, but it sure felt like one of them was a longer day than the other. And the speed at which your agency has to react. Monday, markets open. Nobody was talking about SVB that much. The stock price was $275 a share. Shows you what the equity markets saw coming. And then Friday, poof, we haven't made it through. And yet you have the same number of hours. Is that why these having these plans ahead of time is so valuable?

GRUENBERG: I think that's that's part of the story. And it it raises the liquidity risks of uninsured deposits, which are the other other part of the story, which I think these measures actually help with. But, you know, I think we learned we did learn a lot of lessons about liquidity risk in the episodes earlier this year. Meaningful difference even from the 2008 episode, the speed of the run within a 24 hour period, bringing about the failure of a substantial $200 billion bank almost overnight was was eye-opening. And it to me it adds to the need to take meaningful actions. I think the things we've outlined in addition to the supervisory attention on uninsured deposits, why any bank, you know, should have 90% reliance is a serious question to ask and a super serious supervisory matter, you know, for examiners to pay attention to. And and deposit insurance pricing obviously would would be relevant there as well. And an important point to keep in mind here is the agent, these are all things that the agencies currently have- under our authority. We don't have to look anywhere else. We have the authority now to take these steps that would be, I think, meaningful and effective and could really make a difference the next time around. And we, we need to take advantage of the opportunity now so we'll be in a stronger position in the future.

KLEIN: So let me ask you, picking up on that authority, these are all legal authorities you have now after as 2155, which was passed, that rolled back certain provisions of Dodd-Frank, was enacted. There's been a lot of debate pointing left and right about what impact that law had as it related to the failures this spring. How do you weigh in on that?

GRUENBERG: Well, you know, I'm not frankly looking to point fingers, but the conclusion as I take away from this episode is that banks down to $100 billion in assets can, in the right circumstance, result in significant financial stability risk. And I made this point before, and I made it again today, in thinking about our prudential requirements for capital, for long-term debt, for resolution plans, for liquidity, I think we need to keep that in mind. And it ought to be part of our thinking as we establish these standards.

KLEIN: So I'm going to turn to a question from that we received from the internet, and then I'm going to turn to questions for for the audience. You guys are on deck, but we take questions online. And Jim McGann from Great Point Financial - the name may ring a bell to some folk - asked a question about the speed of payments, including the speed of FedNow, and you mentioned a couple of times, payments and real time payments. Folks know I've been a strong advocate for and the Federal Reserve just this last month in July released their very long awaited, long developed real-time payment platform FedNow. Some people have speculated that may play a role in bank failures. You talked about the speed of things, point out FedNow didn't exist in March, even though some people online seem to think if there's a that it did. Is the speed of the retail payment system a relevant factor for these types of bank runs?

GRUENBERG: I think as a practical matter, it's not clear to me how a run can get much faster, candidly than what we experienced, you know, in March. And the certainly for these large uninsured depositors, they have the capability now of instantaneous electronic withdrawals of deposits that can cause an immediate liquidity crisis for an institution. And I you know, I don't, FedNow on the retail payment end, you know, I don't think is going to change change that fact. I mean, I think we're already there in terms of the liquidity, speed and risk. And this goes back a long way. So it's not even that new the the ability, particularly of large, sophisticated depositors to make electronic withdrawals has been around for a while. But it has really demonstrated itself in these recent events.

KLEIN: The speed of light and the ability of a large corporate treasurer with a $500 million account to move their money isn't materially changed by a retail payment system at 10,000 bucks. That's that's. All right, so that was a question from online from the audience. I'm going to turn to questions in the room. Everybody came here in the back, came on a Monday in August. Sorry, and please ask a question.

AUDIENCE MEMBER: Thank you for the very informative introduction, how, you address both of these in your presentation, but in criticism from the left and the right, at the most philosophical level. We'd like to hear your response to them from the left, is the criticism that this was all about bailing out billionaires, not the average American. As you pointed out, the vast majority of the uninsured are very wealthy depositors. So why are we not letting them take care of themselves. And from the right, the criticism is if you teach the market that the government, in whatever form, is always going to come in and bail out everybody, no matter how reckless management or depositors are, they'll always be bailed out, then you don't give an incentive for. So their criticisms from the left and the right, at the philosophical level, it would be helpful to hear your response to both. Thank you.

GRUENBERG: You know, look, I think those are fair points, candidly, and it's why, frankly, I feel such an urgency to address the vulnerabilities that make, that made what I think was a necessary action to take in regard to the systemic risk exception. It was a very consequential decision that I think we would have preferred to avoid for the obvious reasons. I think the evidence was pretty clear, particularly following the failure of Signature Bank and the pressures that were evident to the regulators of stress and other institutions, that we had a genuine financial stability risk here, and that if we didn't act, the repercussions for the system could have been very significant. I think that was the judgment. You can second guess it. You can always you know, but based on the facts at the time, I really don't second guess it. And based on the experience, since, frankly, I don't second guess it. But that being said, we should not underestimate the consequence of the decision. As you, I think, appropriately point and others appropriately point out, which which is why we really need to take meaningful actions to address to address these issues.

KLEIN: Dennis?

AUDIENCE MEMBER: Thanks for your remarks. All pretty interesting on regional banks, but I wonder if you gave any thought to, in the old days used to be a bank run, you'd run to the bank and you'd line up and get George Bailey's money and you'd get your money. Now you don't run to get your money. You run to move your money. And in this case, the money's all being moved to the GSIBs, because the belief is that the GSIBs are too big to fail. And so uninsured deposits were still uninsured deposits, they just happened to be in a different place where there's a belief that the government will never let them fail. So aren't we really dealing with some of the symptoms, albeit important to do at regional levels? But to me it kind of highlights the bigger problem, the Damocles sword still hanging over the country from the GSIBs. Have you given any thought to that?

GRUENBERG: It might surprise you, but the answer is is yeah. And look, there was some of that. But actually according to the data that we have, perhaps less than was commonly thought. Most of the liquidity that left the regional banks was actually going to non-bank financial institutions by depositors seeking higher yield, rather than to the to the GSIBs. But it raises a fair point. And so, you know, for a long time we had been preoccupied with thinking about the resolution of GSIBs, and we woke up and realized these regional banks can cause a lot of trouble. And we've now had an episode where that has been demonstrated. I think the attention on the GSIBs is still critical. It's an enormous challenge, I would argue, and this is just another speech or another discussion, you know, about the framework we've put in place in regard to the GSIBs in terms of a TLAC or long-term debt requirement for them, resolution planning requirements for them. An array of authorities under Title II of the Dodd-Frank Act, particularly relating to financial derivatives and the ability to place a consolidated company, meaning the holding company and affiliates in addition to the bank. It gives us a framework potentially to manage the orderly failure of one of these institutions, but we haven't executed it yet. So, you know, one should be, to say the least, modest in regard to the assertions made. I do think we have a framework in place that that holds that potential, but maybe that's another conversation for another day.

KLEIN: So we would be delighted to have you come back for another conversation. In fact, I'd be remiss if I didn't point out that you were here talking about digital assets, speaking about being prophetic and warning about the concerns of digital assets entering into the banking system in last summer, when there was a big hotshot company called FTX going around, when there were banks leaning into crypto, of which we focused a lot on SVB, we focused much less on Signature Bank, which had much more of a digital asset. And you did a good job in your speech, I think about pointing out the Silvergate the first of the four, which was even the most heavily crypto on that. Subject also for for for a different time, that interaction. We're going to bring you back to talk about about that. One final, since since it's a subject important, you raised in your response to Dennis that money flowing out of the banking system to non-banks seeking higher yield. Some people might interpret that to be a reference to money market mutual funds who are often, who are non federally insured investment vehicles, who, per our first questioner, have received government bailouts from the Treasury and the Federal Reserve both in the 2008 financial crisis and again in COVID. It would be odd to think about money leaving the banking system that's highly regulated with regulators, with the authority to provide systemic risk exemption to money market mutual funds where no such authority exists from their market regulator, the SEC. But we seem to have observed this, this gets the bailouts beget bailouts phenomenon. I've been a little critical in that space, and I thought your speech in an excellent job of reminding that on Friday you did not invoke the systemic risk exemption on the Friday of Silicon Valley Bank. You invoked a depository resolution system that would have set up a system in which these ten large uninsured folks would have received some losses. And it wasn't until Sunday that you made that choice. Why was, as somebody who's been a bit of critical of that choice, why was it, why am I wrong? Why was that the right choice to make?

GRUENBERG: Oh, I think by Sunday it was it was quite clear from where we were sitting, that that the system was at risk. That the contagion effect through uninsured deposits that had brought about the failure of both Silicon Valley Bank and Signature and, you know, First Republic was hanging by a thread that weekend. It also could have failed and of course ultimately did a few weeks later, and there were other institutions under stress. So if we had not acted, it was really not clear how far this could go. And it had the potential, frankly, to go up the chain of the system and down the chain of the system. And the responsible officials at the three agencies involved, you know, under the law, a, the board of the FDIC and the board of the Federal Reserve have to vote to recommend the exercise of this systemic risk exception. And then the Treasury secretary, in consultation with the president, has to make a determination to exercise the authority. And frankly, by the Sunday, all the responsible members of the FDIC board and the board of governors of the Fed unanimously voted to make that recommendation. And then the secretary, in consultation with the president, made the determination. So, you know, I think I think the risk was was real. And I think if we had not acted, we'd be in a in a worse spot today. So I don't second guess it. It was not something we wanted to do. And as I indicated, it was consequential and it quite critical that we learn from this episode and take actions to avoid a recurrence. But I, do I have second thoughts? And believe me, I'm a professional in that category. I don't have second thoughts on this and certainly on the, our actions at the time and based on ensuing events.

KLEIN: One thing you learn working in the Senate is the chairman always gets the last word. Thank you very much, Chairman Gruenberg.

GRUENBERG: Thank you. All right, great.