July 27, 2023

Eric Froman
Financial Stability Oversight Council
1500 Pennsylvania Avenue
NW, Room 2308, Washington, DC 20220

Re: Docket ID FSOC-2023-0002, Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies; and
Docket ID FSOC-2023-0001, Analytic Framework for Financial Stability Risk Identification, Assessment and Response

We, the (twenty-five) undersigned organizations, representing millions of U.S. residents, strongly support FSOC’s proposed revised interpretive guidance concerning FSOC’s procedures for designating nonbank financial companies for enhanced federal supervision (Proposed Guidance), and related Analytic Framework (Framework). We urge FSOC to finalize both proposals as quickly as possible and to begin making determinations about nonbanks’ systemic importance soon thereafter.

Background
In 2010, Congress determined that, to prevent another financial crisis, insurance companies and other non-bank financial institutions that could threaten financial stability—either through their own material distress or through their activities—need enhanced federal supervision. The Dodd-Frank Act authorized the Financial Stability Oversight Council (FSOC) to identify firms that are systemically important and to designate such firms for supervision and regulation by the Federal Reserve.

Guidance adopted by FSOC in 2019 to implement these provisions of the Dodd Frank Act established a series of barriers to designating entities that are, in fact, systemically important and ought to be supervised by the Federal Reserve. These barriers have made designations virtually impossible, frustrating Congress’ intent that FSOC use designations as a precautionary measure to avoid financial crashes and public bailouts of financial institutions. For example, the 2019 guidance called for FSOC to perform costly, time-consuming and unnecessary analyses prior to designation, which effectively prohibited FSOC from designating systemically important institutions.

While the 2019 Guidance has constrained FSOC’s ability to designate firms, threats by such entities to financial stability are growing, particularly in light of growing climate change-related financial risks. Nonbank financial institutions are, for example, already facing heightened stress from large and repeated climate-related shocks—as evidenced by several major insurers’ recent decisions to withdraw coverage from California and elsewhere. And large insurers, publicly listed asset managers, private equity firms and private debt entities are also creating significant risks to the financial system through their insured or financed emissions—risks that are often forced upon other financial institutions and consumers that lack the capacity to avoid and manage these risks. Black, Indigenous, People of Color (BIPOC) communities are disproportionately impacted by such risks and impacts, and many are already struggling to maintain insurance on their homes and to obtain adequate access to credit. The increased number and severity of
extreme weather events is creating unprecedented smaller shocks to these institutions and consumers that could precipitate a systemic crisis before long.

Large nonbank financial institutions are heavily connected to other financial entities throughout the United States and globally, and yet the current regulation of these entities does not clearly maintain their safety and soundness, is not always transparent, and in some cases is virtually nonexistent. Additionally, many nonbanks carry out activities in a non-transparent manner further contributing to financial stability risk.

By establishing a clear designation process, removing barriers to designation, and enhancing the public’s understanding of how FSOC will identify, assess, and address systemic risks more generally, the Proposed Guidance and Framework are critically important.

Support for the Framework
We particularly support several features of the Framework, including the following:

● explicit mention of climate-related financial risk as a potential risk to financial stability;
● the acknowledgment that threats to financial stability could derive from external sources and long-term vulnerabilities;
● the recognition that FSOC can make recommendations to regulatory agencies and Congress when financial institutions’ activities could create or increase the risk of significant liquidity, credit or other problems among low-income, minority, or underserved communities;
● attention to the fact that activities that are sizable and interconnected with the financial system can destabilize markets even when these activities are intentional and permitted by law; and,
● the description of vulnerabilities and risk transmission channels that can lead to systemic risks.

Suggested enhancements to the Framework to address climate risk
Nevertheless, we believe the Framework can be improved by greater attention to (1) the need for a precautionary approach to systemic risk—to proactively managing risks that are highly uncertain, including radically uncertain climate risks, and that could cause unacceptably high losses for the financial system or the economy; (2) the fact that some new or evolving risks, including those introduced by climate change, are often being forced on entities that have not created them or willingly acted to assume them, and that lack the financial capacity to manage them—these entities should not be disproportionately burdened by such risks and related costs; and (3) the potential for new or evolving risks to involve new risk transmission channels and require new risk management measures—including measures that prevent risk from spreading among low-income, minority, or under-served communities.

Thank you for the opportunity to comment on these critically important proposals.

Sincerely,

Americans for Financial Reform Education Fund
Climate Action California
Climate Reality Leader
Divest Washington
Earth Action, Inc.
E3G
Friends of the Earth U.S.
The Greenlining Institute
Green Party of Sacramento
Institute for Agriculture and Trade Policy
MARBE SA, Costa Rica
Micah Six Eight Mission
New York Communities for Change (NYCC)
Oil & Gas Action Network
Revolving Door Project
Rise Economy (formerly California Reinvestment Coalition)
The Phoenix Group
Positive Money US
Private Equity Stakeholder Project
Public Citizen
Sierra Club
Stand.earth
The Sunrise Project
Texas Campaign for the Environment
350NYC