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Subcommittee on Health Care and Financial Services

Topic: A Failure of Supervision: Bank Failures and
The San Francisco Federal Reserve

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Chairwoman McClain, Ranking Member Porter, and Members of the Subcommittee:

Thank you for the opportunity to be here today.

Bank supervisors are charged with promoting the safety and soundness of the banks they oversee. How likely they are to succeed in this task depends on the rigor of the supervision, but it depends even more on the magnitude of the challenge set before the supervisory team. Adequate regulation and appropriate compensation schemes for bank executives—including possible claw backs when banks fail—are key to making this task manageable.

The recent failures of three different large regional banks, with three different business models, and three overlapping but distinct sets of supervisors, are a clear sign that the building blocks for success were lacking. Yes, the supervisors failed. Yes, further examination of the reasons for those failures is warranted. And yes, there is room for improvement in promoting healthy accountability and oversight of bank supervision generally, and of supervision within the Federal Reserve System in particular. But the question of why so many supervisors, employed by different state and federal bodies, fell short can only be answered by also examining the common factors that made these failures so likely.

I will begin by addressing why context matters and how it fell short. I will then explore some tools that could enhance oversight of bank supervision and while also helping supervisors to do their jobs well. I will close with some reflections on structural issues that can impede efficacy and oversight and ways to potentially mitigate those challenges.

I. Regulation and Compensation: The Stage for Supervisory Success (or Failure)

Banks provide credit and other financial services that are key to the economic well-being of individuals and families and to the economic vibrancy of the country. Up to a point, a robust financial system promotes healthy economic growth.[1] Yet, just as there are broad benefits to a well-functioning banking system, bank failures can impose significant and widespread harms. People depend on banks as a safe place to store their money. The failure of one bank can ignite fear among depositors at other banks, causing dysfunction to spread. A dangerous cycle of bank

[1] Jean-Louis Arcand, Enrico Berkes & Ugo Panizza, Too Much Finance? (IMF Working Paper No 12/161, June 2012); Stephen G. Cecchetti & Enisse Kharroubi, Reassessing the Impact of Finance on Growth (Bank of International Settlements Working Paper No 381, July 2012).

runs, bank closures, loss of faith in the banking system, and a contraction in credit was a core factor contributing to the economic devastation wreaked by the Great Depression.[2]

Today, the United States is fortunate to have devised a set of tools and safeguards that make it far less likely that a banking crisis will again cause such widespread suffering. Deposit insurance is the cornerstone of this system, helping to assure people that money in their bank is safe. Similarly, the "systemic risk exception" to the requirement that the Federal Deposit Insurance Corporation (FDIC) resolve a bank in the manner that imposes the least cost on the Deposit Insurance Fund gives financial regulators flexibility to provide broader assurances when needed to prevent panic and protect the health of the financial system.

These types of government support are key to preventing bank failures from inflicting lasting harm on the real economy. Yet they also accentuate the core underlying challenge: Bank executives and bank shareholders bear only a portion of the downsides that result when their banks fail. Sometimes, bank leadership appreciates the important public role they are playing, and manages their bank accordingly. But this cannot be assumed. Too often, absent regulation and oversight, bank leadership will want to assume too much risk and may systematically under-invest in domains such as compliance, where only a portion of the benefits accrue to the bank itself. This is why bank regulation and supervision are so important, and often so hard to do well.

A. Regulation

Appropriate regulation is the most important mechanism for helping to close the gap that can otherwise exist between what is privately and publicly optimal. Capital requirements make it less likely that a bank will fail and increase bank shareholders' skin in the game. Liquidity requirements mitigate the risk that most often falls on a financial institution, and the opportunity cost of holding high-quality liquid assets may motivate banks to otherwise hold too few. Stress tests ensure banks are engaging in forward-looking assessments of how they would fare should circumstances sour and can provide banks and their supervisors with important insights into the adequacy of a bank's risk management capabilities. Regulation is inherently coarse and incomplete, but it is also the most reliable, transparent, and widely used tool for helping to better align the interests of banks and bankers with the broader public.

The Dodd-Frank Wall Street Reform and Consumer Protection Act updated the regulatory scheme governing banks in light of the lessons learned during the 2007-2009 financial crisis, but adequate regulation requires ongoing diligence.[3] Accentuating the challenge, in 2018, Congress allowed banks to grow well past the previous cap of $50 billion without becoming subject to a suite of enhanced prudential requirements that had been designed to address the distinct challenges that arise as banks grow increasingly large, and increasingly hard to resolve in an orderly fashion.[4] And, in 2019, the Federal Reserve used the discretion it was given under the Economic Growth, Regulatory Relief, and Consumer Protection Act to go even further in reducing the regulatory burdens on large regional banks.[5]

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[2] Ben S. Bernanke, Nonmonetary Effects of the Financial Crisis in Propagation of the Great Depression (American Economic Review, Vol. 73, 1983).
[3] Dodd-Frank Wall Street Reform and Consumer Protection Act (Pubic Law 111–203, 2010).
[4] Economic Growth, Regulatory Relief, and Consumer Protection Act (Public Law 115–174, 2018), https://www.congress.gov/bill/115th-congress/senate-bill/2155/text.
[5] Changes to Applicability Thresholds for Regulatory Capital and Liquidity Requirements (84 FR 59230, 2019), https://www.govinfo.gov/content/pkg/FR-2019-11-01/pdf/2019-23800.pdf; Prudential Standards for Large Bank

The events since March of this year make it plain that irrespective of whether those decisions may have seemed reasonable at the time, they allowed large regional banks to grow too large and too quickly relative to their ability to manage the risks they were assuming, and the risks that they posed to others. That a unanimous board of the FDIC, all of the governors of the Federal Reserve System, and the Treasury Secretary, in consultation with the President, deemed it necessary to invoke the systemic risk exception to protect all of the uninsured depositors of two large regional banks shows that the failure of such banks can threaten the health of the broader financial system.[6] That a third such bank also failed in a way that imposed significant losses on the Deposit Insurance Fund further highlights the massive mismatch between the costs the failure of these banks can impose on others and the robustness of the regulations in place to constrain and direct their risk taking. The most important step that Congress and regulators can take to prevent a repeat of such costly failures is to update the regulatory scheme so that it better reflects the costs that large regional banks can impose on others.

B. Bank Management

Since 2018, Silicon Valley Bank's chief executive, Greg Becker, enjoyed a 30% increase in his annual compensation.[7] As a result, Becker's total compensation for 2022 exceeded $9.9 million.[8] Alongside his regular pay, Becker reaped an additional $3.3 million in 2023 from exercising stock options and immediately selling the stock. In March, the failure of SVB ripped a $20 billion hole in the Deposit Insurance Fund. Nonetheless, Becker may end up being able to retain all the money he earned in compensation, the cash bonus he got paid even as risks grew unaddressed, and the additional profits he reaped selling stock that would soon be worthless.

The ability of a bank executive to personally profit so much, even as he runs his bank into the ground, makes it far harder for supervisors to do their job well. Supervisors do have tools to deter egregious behavior by bank executives, including the ability to ban executives from the industry entirely should they act too irresponsibly. Yet, such tools are used only rarely, and have not been updated to reflect the realities of banking today.[9] More expansive claw backs could further help address the unfairness and incentive challenges that arise when decisions by bank executives, whether reckless or ill-advised, cause a bank to fail and inflict costs on others.

By design, bank executives have far more control, and more information, than even the best team of supervisors. Providing appropriate outside checks on the capacity of bank leadership to use their superior information and control to serve their own interests at the expense of others is key to reducing the risk that bank executives will find creative ways to game the rules for their own gain. Like regulation, checks on compensation are a critical component of what needs to be

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Holding Companies, Savings and Loan Holding Companies, and Foreign Banking Organizations (84 FR 59032, 2019), https://www.govinfo.gov/content/pkg/FR-2019-11-01/pdf/2019-23662.pdf. Then Federal Reserve Governor Lael Brainard dissented from this rule change.

[6] Joint Statement by the Department of the Treasury, Federal Reserve, and FDIC (2023), https://www.fdic.gov/news/press-releases/2023/pr23017.html.

[7] Ciara Linnane, Silicon Valley Bank Execs Enjoyed Generous Compensation in Recent Years, with CEO and CFO Packages up 30% from 2018 (2023), https://www.marketwatch.com/story/silicon-valley-bank-execs-enjoyed-generous-compensation-in-recent-years-with-ceo-and-cfo-packages-up-30-from-2018-a18c245a.

[8] Id.

[9] Da Lin and Lev Menand, The Banker Removal Power (Virginia Law Review, Vol. 108, No. 1, 2022), https://virginialawreview.org/articles/the-banker-removal-power/.

a multi-prong strategy for limiting and directing bank risk taking. Inadequate checks, like inadequate regulation, can set supervisors up to fail.

II. Oversight of Bank Supervision

Healthy regulation and appropriate checks on compensation are key to reducing the structural mismatch that too often arises between what is optimal for bankers and what is socially optimal. Yet, neither of these checks is a complete solution. Regulation is inherently coarse and often backward-looking. Banking, by contrast, is dynamic.[10] Some of this dynamism arises from efforts by bankers to game the rules, finding ways to comply with the letter but not spirit of a restraint. Some of it arises from innovations, technological and otherwise. Innovation can change the nature of banking, and introduce new forms of competition, in ways that can weaken the impact of regulations even in the absence of affirmative deregulation.[11] These are among the reasons that Congress and bank regulators must constantly update the rules governing both banks and nonbanks to accommodate changing structures and new insights. Yet it also explains why supervision remains so vital even as the rules governing banks have proliferated, and why supervisors must do far more than ensure banks are complying with applicable rules.

To be effective, bank supervisors must be willing to ask hard questions. They must understand a bank's business model, probe the assumptions underlying that model and think creatively about tail risks to which a bank may not be paying adequate heed. If the bank is rapidly growing in one domain, supervisors should seek to understand why and the risks associated with that growth. Supervisors should also assess just how well a bank is positioned to fare in the face of possible adverse developments, from inflation to a recession to shifting geopolitical tensions.

The burden on supervisors is particularly great today. Digitization and technological innovation are changing banking and finance in ways that reduce the utility of historical models and can render longstanding assumptions irrelevant. To keep apace as banks and nonbanks co-evolve, sometimes in competition and sometimes cooperating, supervisors must have the capacity and willingness to think creatively about what might be and what might go wrong.

A. Healthy Oversight

Understanding the important, challenging task set before bank supervisors lays the groundwork for understanding how best to hold supervisors accountable. The best accountability mechanisms promote both better bank supervision and better oversight of the way bank supervisors carry out their roles.

Voluntary reports. First, I want to express my deep appreciation of the reports recently issued by Board of Governors of the Federal Reserve System, the FDIC, the California Department of Financial Protection and Innovation and the New York State Department of Financial Services, alongside the independent review provided by the U.S. Government

[10] For a discussion of how the dynamism and complexity of modern finance, including banking, creates regulatory challenges, see Dan Awrey and Kathryn Judge, Why Financial Regulation Keeps Falling Short (Boston College Law Review, Vol. 61, No. 1, 2020).
[11] Kathryn Judge, Regulation and Deregulation: The Baseline Challenge, Vanderbilt Law Review Online (Vol. 104, 2018).

Accountability Office.[12] Each of these reports, voluntarily undertaken and produced with remarkable speed, provides useful insights into the recent bank failures and the ways that supervisors fell short. I admire leadership's willingness, in each instance, to look honestly at where their agency fell short and the incredible work the staff must have invested to provide such thorough accounts so quickly. The Federal Reserve went even further and also released supervision materials that typically remain confidential even when a bank fails.

These types of voluntary disclosures, self-scrutiny and public reporting promote healthy oversight by providing the information and insights that Congress and the public need in order to understand what happened—what worked well, and where did the current structures fall short. They simultaneously can enhance supervision going forward, as each supervisory body can learn from their own mistakes and from the shortcomings exhibited by others. This type of voluntary reflection and reporting should be applauded and encouraged.

Escalation frameworks. Escalation frameworks are another a great example of a tool that can enhance both bank supervision and accountability. The idea underlying escalation frameworks is that repeat offenses should be treated differently than isolated failures. All banks make mistakes. When a bank that generally has a good track record makes an error, the bank should be given a chance to course correct.

Other banks, however, are repeat offenders. They have had a deficiency brought to their attention through formal channels, and yet they still make little or no progress in addressing and correcting those deficiencies. Or they may instead have a pattern of deficiencies and abuses that repeatedly occur across the organization, suggesting more fundamental shortcomings in their commitment to robust risk management and compliance. Escalation frameworks help to address recidivism by putting banks on notice that even if they incur only a mild slap for an isolated violation, the consequences will be increasingly severe should they fail to course correct or fail to address the underlying dynamics giving rise to that deficiency.

Under a well-designed escalation framework, after a bank has been given notice of a deficiency and fails to take the steps needed to address it, the consequence is known and severe. And should the bank continue to fall short despite heightened supervisory action, the consequences again escalate. The Acting Comptroller of the Currency Michael Hsu recently highlighted the value of such frameworks, and provided concrete examples of the types of escalating ramifications that should result when a bank either cannot or will not take the actions necessary to course correct.[13]

When clearly articulated in advance, these types of frameworks can also help Congress and the public hold supervisors accountable, and they can help the supervisory leaders to hold field teams to account. For example, escalation frameworks may enable Congress to ask hard questions about whether a supervisor has complied with its own framework when it comes to light that a bank has a longstanding pattern of bad behavior. The articulated framework serves as a baseline for what effective supervision should look like—and what the consequences ought to

[12] Board of Governors of the Federal Reserve System, "Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank," (April 28, 2023); California Department of Financial Protection and Innovation, "Review of DFPI's Oversight and Regulation of Silicon Valley Bank," (May 8, 2023); Federal Deposit Insurance Corporation, "FDIC's Supervision of Signature Bank," (April 28, 2023); New York State Department of Financial Services, "Internal Review of the Supervision and Closure of Signature Bank," (April 28, 2023).
[13] Acting Comptroller of the Currency Michael J. Hsu, Remarks at Brookings: "Detecting, Preventing, and Addressing Too Big To Manage" (January 17, 2023).

be for deficiencies—making it easier for supervisors to hold banks to account and for Congress and the public to hold supervisors to account. There is always some need for judgment in execution, and dialogue is key to understanding the inevitable judgment calls that must be made, but the framework can make that dialogue possible and productive.

External indicia of possible distress. Another way to promote better supervision and better oversight would be for bank supervisors to explain when and how they make use of external indicia that a bank may be on a downward path. Few bank failures are completely unique. Instead, they follow patterns. In the periods before a bank fails, for example, it is not uncommon for a bank to grow rapidly, increase its reliance on "advances" from the Federal Home Loan Bank system, pay higher rates of interest on deposits and other liabilities, increase reliance on brokered deposits, hoard liquidity, and, if publicly traded, see the price of its stock and bonds decline.[14] None of these is a red flag indicating that a bank is necessarily in trouble. But they are yellow flags—indicia that a bank may be en route to distress. At times, market indicia may also provide insights into how well bank regulation, generally speaking, is accomplishing desired aims.[15]

Identifying leading indicators of bank distress is a difficult enterprise, but supervision is well suited to address the noise inherent in such indicators. Supervisors can use yellow flags as prompts to look more closely at a bank's health, and potentially increase oversight to ensure that deficiencies are known and are being addressed in a timely way. Articulating a set of yellow flags and creating structures for ensuring they are monitored and utilized can also enhance oversight—increasing the capacity of supervisory leadership to monitor supervisors on the ground and increasing the ability of Congress and the public to understand when supervisors are, and are not, making full use of available information.

As with the other tools here, context matters. There are unlikely to be "smoking guns" indicating clear success or failure. Nonetheless, articulating what indicia bank supervisors see as significant and how they use that information again helps to create a baseline that could enhance both supervisory processes and accountability.

B. Oversight and Procedural Checks Can Backfire

At the other end of the spectrum, some efforts that may seem aimed at promoting accountability and consistency can have the effect of throwing so much sand in the wheels that they impede the ability of supervisors to do their jobs well. For example, procedural checks internal to a bank supervisory organization can help to promote uniformity in how bank supervision is carried out in ways that promote fairness. Too many procedural checks or checks that are too onerous, however, can delay needed action. Evidentiary standards are another two-edged sword. On the one hand, supervisors should not force a bank to change its course of conduct because of a vague hunch that something is amiss. On the other hand, requiring supervisors to amass too much evidence of a deficiency and its probable consequences before

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[14] E.g., Kathryn Judge, Three Discount Windows, 99 Cornell Law Review 795 (2014); Viral V. Acharya & Ouarda Merrouche, Precautionary Hoarding of Liquidity and Interbank Markets: Evidence from the Subprime Crisis, 17 Review of Finance 107 (2013)Isabelle Distinguin, Philippe Rous & Amine Tarazi, Market Discipline and the Use of Stock Market Data to Predict Bank Financial Distress, 30 Journal of Financial Services Research volume 151 (2006); Viral V. Acharya & Ouarda Merrouche, Precautionary Hoarding of Liquidity and Interbank Markets: Evidence from the Subprime Crisis, 17 Review of Finance 107 (2013).
[15] E.g., Natasha Sarin and Lawrence H. Summers, Have big banks gotten safer?, Brookings Papers on Economic Activity (Fall 2016).

taking action has the effect of systematically slowing and weakening supervisory responses despite a recognized deficiency.

More generally, the environment in which supervisors are operating also affects their capacity to do their jobs well. High-quality bank supervision is not a check-the-box undertaking. It requires judgment. A climate of fear is not conducive to the type of creative, forward-looking thinking that this country needs from its supervisors, today more than ever.

Recall, regulation is most likely to fall short when lawmakers do not yet have the wealth of information and experience needed to design appropriate, standardized rules. An array of factors suggest that the coming months and years could be a period of industry transformation, in which supervisors will need to use discretion and judgment in order to succeed. The digitalization of finance that allowed depositors to flee so quickly from Silicon Valley Bank is also changing the banking landscape in other ways that banks and their supervisors are only starting to understand. Banks are investing heavily in technology; many are using an array of third-party partnerships to remain competitive and navigate the transition to a more digital environment; and, banks are facing an evolving set of nonbank competitors with respect to both the lending and payment services that traditionally have been core to banking. The recent rapid rise in interest rates and recent bank turmoil have the potential to accelerate shifts that may have been possible for some time, but which were less likely in a more stable environment.

Banks and their supervisors are on the frontline of these changes. A healthy dialogue among supervisors, regulators and lawmakers could be fruitful in helping to facilitate the transitions that may lie ahead. Oversight that promotes respect and mutual learning can go a long way in helping the regulation and supervision, of banks and nonbanks, keep pace in a rapidly changing environment. Introducing rigidities, requiring too many checks or fostering an environment that encourages more defense than offense, by contrast, could undermine the type of supervision and learning this moment requires.

III. Structure of Bank Supervision in the United States

Looking more broadly at ways to promote effective bank supervision and to foster accountability of bank supervisors reveals structural issues that merit attention. The fragmented nature of financial regulation in the United States often does more harm than good, and there are also particular features of how supervision is carried out within the Federal Reserve System that may warrant reconsideration.

A. Structure of Bank Supervision

The United States has an unusual system for chartering, regulating and supervising banks. There are three different federal bank supervisors, the Federal Reserve, the Comptroller of the Currency and the FDIC. Focusing just on U.S. banking organizations: the Federal Reserve oversees state banks that are Federal Reserve members and banking holding companies; the OCC supervises national banks; and the FDIC supervises state banks that are not members of the Fed. State banks receive their charter from a state authority that also regulates and supervises their activities (The amount of gamesmanship this enables is limited today by the requirement of FDIC insurance and the regulatory floors and federal oversight that accompany that insurance. Credit unions have their own regulator, supervisor and federal insurance fund in the National Credit Union Administration, and can also be chartered, regulated and supervised by states.

This regime is simpler and better functioning than it was fifteen years ago. The Dodd-Frank Act helpfully eliminated the Office of Thrift Supervision—yet another federal regulator of bank-like organizations and one that seemingly used laxity to attract banks to its domain.[16] There are also structures in place to mitigate the disparities that can arise from this supervisory patchwork. In particular, the Federal Financial Institutions Examination Council, an interagency body, works to promote common principles for the federal examination of financial institutions across these bodies, and it also coordinates with the state supervisors of banks, thrifts and credit unions. Nonetheless, the overall scheme is still far from simple. This patchwork is a byproduct of history more than an embodiment of any coherent strategy for how best to institute a system for chartering, regulating and supervising banks.

A more streamlined regulatory architecture for bank regulation and supervision could facilitate more effective oversight by providing simpler, cleaner lines of authority. Particularly if addressed as part of a broader effort to examine the structure of the financial regulation in the United States, such changes could well promote more effective supervision, enhanced oversight, and a more resilient financial system.[17]

B. Structure of the Federal Reserve System

The United States also has a very unusual central bank. When it was first founded in 1913, much of the power of the Federal Reserve System resided with the twelve regional banks scattered across the country. These banks were structured as cooperatives "owned" by member banks, and subject to oversight by a board of directors that consisted, in equal thirds, of directors representing member banks, directors chosen by member banks to represent the public and industry in the district, and public directors selected by what is now the Federal Reserve Board of Governors. Over time, much of the power that once lay in the hands of the regional banks has migrated, through amendments to the Federal Reserve Act, legal opinions and evolving internal norms and practices, to the Board of Governors. All Federal Reserve Governors are appointed by the President, by and with the advice and consent of the Senate.

The Dodd-Frank Act revised this structure in two ways that are relevant here. First, without changing the composition of the boards of directors of the Reserve Banks, it eliminated the ability of the directors who represent member banks to participate in the appointment of the Reserve Bank President. This was a helpful step in mitigating, though far from eliminating, the conflicts that can arise from having member banks who are overseen by the Fed also choosing its leadership. Around supervision, this conflict is further addressed—at least in theory—by not having the board of directors play any role overseeing supervisory activities carried out by regional Reserve Banks.[18]

Separately, the Dodd-Frank Act created a new role, Vice Chair for Supervision of the Board of Governors of the Federal Reserve System.[19] By statute, the Vice Chair for Supervision is obliged to make recommendations with respect to how the Board should use its regulatory

[16] Patricia McCoy & Kathleen C. Engel, Federal Preemption and Consumer Financial Protection: Past and Future (Banking & Financial Services Policy Report, vol. 31, no. 3: 25–36, 2012)
[17] E.g., The Volcker Alliance, Reshaping The Financial Regulatory System (2015); Richard Neiman & Mark Olson, Dodd-Frank's Missed Opportunity: A Road Map for a More effective Regulatory Architecture (Bipartisan Policy Center, April 2014).
[18] Roles and Responsibilities of Federal Reserve Directors, Federal Reserve System Publication, available at https://www.federalreserve.gov/aboutthefed/directors/about.htm.
[19] Pub. L. 111–203, title XI, § 1108(a)(1), July 21, 2010, 124 Stat. 2126.) as codified at 12 U.S. Code § 242.

authority over financial institutions. The Vice Chair for Supervision is further charged with overseeing the Fed's supervision of banks, banking organizations and certain nonbanks. The central role that Michael Barr, the current Vice Chair for Supervision, has played in the oversight conversations following the recent bank failures is a testament to how helpful it is to have this new position. At the same time, in practice, the Board continues to delegate much of its supervisory authority to the regional Reserve Banks. This is why we are gathered here today for a hearing focused on the role of the Federal Reserve Bank of San Francisco in the recent bank failures.

Stepping back, there is much to like about this overall structure. For example, the Reserve Bank Presidents bring helpful insights into how the economy in their region is faring into the process of setting monetary policy.[20] The Reserve Banks also play important roles in helping to explain what the Fed is doing and why to businesses and people in their regions. Having separate research bodies across the Federal Reserve System can also help guard against groupthink, and can surface important issues and insights that may not have been generated by a more centralized system.

At the same time, there are drawbacks to this structure, as recent events have revealed. It makes sense to preclude Reserve Bank boards from playing a role overseeing supervision, and that should not be changed, but it also creates a modest governance gap around the supervisory activities carried out at the Reserve Banks. Some recent research also casts indirect doubt on whether this insulation is quite as complete in practice as it is in theory.[21] More importantly, although Vice Chair Barr has done a commendable job in taking responsibility for recent missteps and in taking the lead in efforts to improve supervision at the Fed, the current structure could slow and otherwise impede those reforms. The OCC and FDIC also have regional offices, and this type of structure is needed given the geographic dispersion of banks. But it may be prudent to reconsider how supervision is carried out within the Federal Reserve System and the nature of the role that Reserve Banks in that process.

Conclusion

The biggest lesson from the recent bank failures is the importance of appropriate regulation. That four regional banks failed in a short period of time, three failed in ways that imposed significant costs on the Deposit Insurance Fund, and two failed in ways that required use of the Systemic Risk Exception makes it plain that the rules governing their activities were not sufficiently robust relative to the risks that they posed. Appropriate regulation is key to supervisory success, and one reason bank regulators are so often also bank supervisors—the two tasks go hand-in-hand.

Yet recent events also provide useful insights into shortcomings in how supervision was carried out at each of the banks that failed. The reports exploring these failures provide a useful starting point for exploring how to simultaneously improve both the quality of bank supervision and the capacity to oversee supervisory activities. For supervision to succeed, this oversight should encourage creative, forward-looking assessments of possible risks alongside promoting

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[20] E.g., Beige Book: Summary of Commentary on Current Economic Conditions by Federal Reserve District, https://www.federalreserve.gov/monetarypolicy/publications/beige-book-default.htm.

[21] Peter Conti-Brown, Kaleb Nygaard & Brian D. Feinstein, Board Diversity Matters: An Empirical Assessment of Community Reinvestment at Federal Reserve-Regulated Banks (Yale Program on Financial Stability Working Paper Forthcoming, April 2023), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4000110.

diligence and follow-through on what may seem like more mundane matters. Longer term, it may be useful to explore some of the unusual regulatory structures that can complicate regulation, supervision and other efforts to promote a healthy and vibrant financial system.