

# SUPERVISION, REGULATION, & CREDIT

**S**upervision and regulation are among the most critical components of the banking system. The Supervision, Regulation, and Credit Department (SRC) supervises and regulates domestic and foreign operations for financial institutions in eastern Pennsylvania, southern New Jersey, and Delaware, under the jurisdiction of the Federal Reserve Bank of Philadelphia and the Board of Governors.

It is imperative for SRC to maintain public confidence and normal operations at the Bank regardless of existing circumstances. While this objective has been challenged in past crisis situations, it had never been put to the test as on the days following the September 11 terrorist attacks on America.

In the following, Senior Vice President Michael E. Collins recounts SRC's response to the crisis.

## A PLAN OF ACTION

"Historically, our supervisory and regulatory framework has played an important role in identifying and anticipating problems before they become crises. An essential ingredient in managing problem institutions is our ability to know what traits of an emerging situation could cause problems. When we are success-

ful, this allows us to help banking organizations maintain safe and sound operations without undertaking undue risk.

"The need for crisis management skills comes into play when we as supervisors do not have advanced warning about potential problems and are instead faced with an urgent crisis situation. This was the case on September 11.

"On that morning, when we realized that these were terrorist attacks on America, SRC immediately began gauging the impact on the financial services industry. Some members of our SRC staff were attending a Subcommittee on Credit, Reserves, and Risk Management meeting at the New York Fed, not far from ground zero. Immediate telephone contact was made to determine if any employees had been affected. After ensuring the safety of our staff, we organized a conference call among key players in SRC to determine a plan of action. Our primary objectives were 1) to manage the technical aspects of the attacks on the banking system and 2) to keep people informed regarding the human aspects of the crisis."



**SRC'S PRIMARY FUNCTION IS TO ENSURE SAFETY AND SOUNDNESS IN THE FINANCIAL INDUSTRY INCLUDING PROTECTING CONSUMERS, ENSURING THE ACCESSIBILITY OF FINANCIAL SERVICES, AND PROVIDING LIQUIDITY TO THE FINANCIAL SYSTEM.**

**MICHAEL E. COLLINS**

SENIOR VICE PRESIDENT AND  
LENDING OFFICER

## COMMUNICATION IN A CRISIS

“To gauge the impact of the crisis on the Third District, we contacted select institutions around the region to assess and evaluate their financial condition. This way we were able to identify any high-risk areas in the District and locate potential clearing or settlement bottlenecks. In addition, we immediately took action to analyze the sufficiency of back-up systems. Our preparation for the century date change proved helpful in our analysis.

“Immediate and continuous dialogue with financial institutions communicated our willingness to accommodate special requests in this time of crisis. Issues related to section 23A of the Federal Reserve Act, which covers transactions with affiliates including collateral requirements, quickly began to emerge. The discount window staff was instructed to take an accommodative posture to ensure adequate liquidity and assure institutions that we were open to lend. Also, lending and supervisory inquiries were coming in from financial institutions around the District as banks became apprehensive about whether their normal channels for funding would be available. We acted promptly on these inquiries and gathered intelligence, which allowed us to preempt potential financial difficulties.

“The crisis also warranted extensive communications among banking agencies, including all Federal Reserve Banks, and federal and state regulators. In fact,

the Office of the Comptroller of the Currency sent messages to New York via the Philadelphia Fed, as they were unable to get through to New York.

“Acting as process facilitator proved a crucial aspect of SRC’s role on September 11. We called the New York Fed on behalf of institutions in our District

that expected to receive funds from New York banks. The New York Fed then contacted its institutions to ascertain their ability to conduct business. With offices evacuated and systems down, there was uncertainty about the effective clearing

and settlement of transactions. We were able to provide a source of information to our institutions regarding account activity. Meanwhile, our Credit Risk Management staff worked late into the night addressing settlement issues and completing transactions.”

## LENDER OF LAST RESORT

“In the days and weeks following the attacks as intelligence was gathered, we were in constant communication with our institutions to impart real-time policy decisions. As lender of last resort, especially in times of crisis, it is our responsibility to lend to those with no access to credit. We communicated policy directives encouraging institutions to work with customers and not allow the temporary breach of the stringent supervisory framework to impede service. Banks were assured that temporarily inflated balance sheets or temporary declines

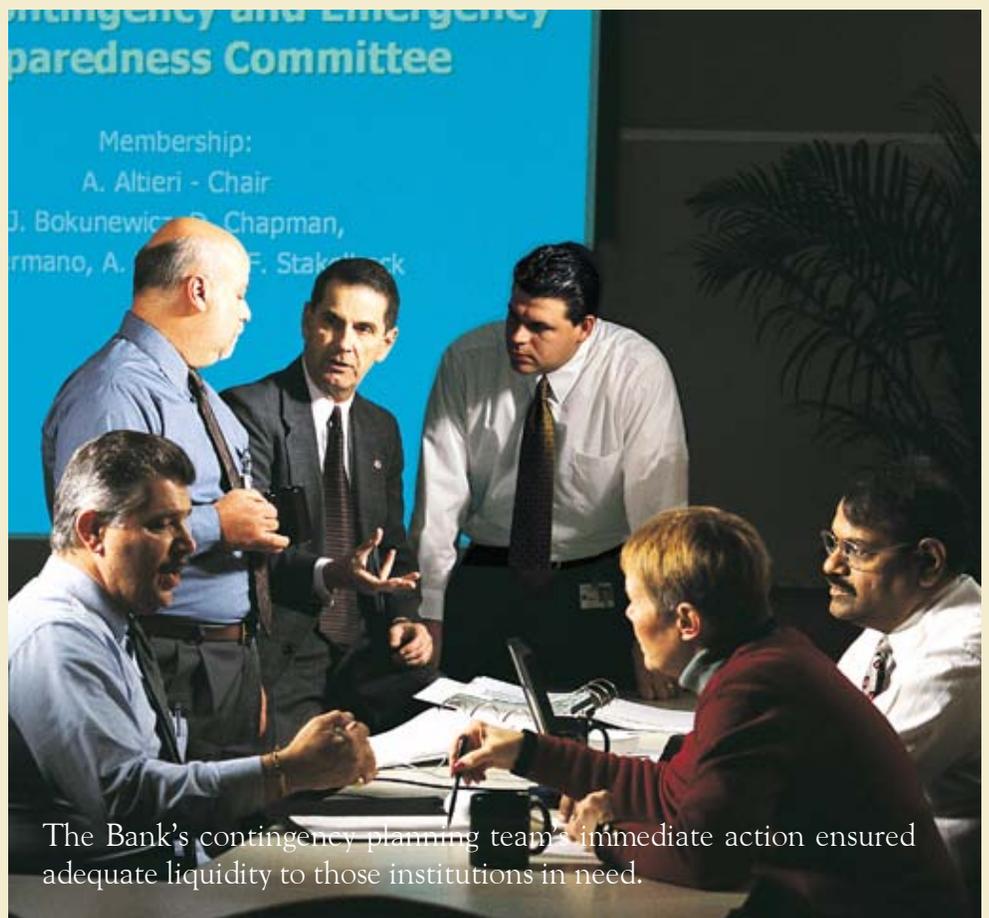
## IMMEDIATE AND CONTINUOUS DIALOGUE WITH FINANCIAL INSTITUTIONS COMMUNICATED OUR WILLINGNESS TO ACCOMMODATE SPECIAL REQUESTS IN THIS TIME OF CRISIS.

in capital ratios would not trigger corrective action on our part as regulators. The temporary easing of credit terms and waiving of certain obligations provided the flexibility to ensure adequate liquidity to those institutions in need.”

**BANKING SYSTEM INVESTIGATION**

“Once liquidity concerns were addressed, we turned our attention to how the banking system might have been used in the attack. Who was behind the attacks? How were they funded? These were the questions at the forefront of the investigation. We received lists of names from law enforcement officials which we circulated to financial institutions, along with instructions on how to notify the proper authorities if a name from this list was discovered on their accounts.

“This brings us into the realm of money laundering, an area where I am certain we will see immediate and far-reaching policy changes. Proposed legislation would give the Treasury new powers to target foreign countries or banks deemed to present a major money-laundering threat.”



The Bank’s contingency planning team’s immediate action ensured adequate liquidity to those institutions in need.

**OUR UTMOST OBJECTIVE**

“Engaging in proactive crisis management presents us with a unique challenge. We are essentially preparing for an event we hope never comes to fruition. But crises do occur, sometimes insignificant like Y2K, sometimes devastating like September 11. Regardless of the issue, we must never lose

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sight of the public nature of our work. Operating efficiently, protecting the safety net, and keeping the confidence of our customers is achieved through maintaining the safety and soundness of our financial system. That is, and always has been, our utmost objective.”