[Journal of Financial Crises](https://elischolar.library.yale.edu/journal-of-financial-crises)

Volume 3 | Issue 2

2021

Lessons Learned: Arthur Murton

Sandra Ward

Yale Program on Financial Stability
Lessons Learned

Arthur Murton

By Sandra Ward

Arthur Murton joined the Federal Deposit Insurance Corp. in 1986 as a financial economist and rose through the ranks to become Director of the Division of Insurance and Research, a post he held from 1995 to 2013 and which he steered through the financial crisis of 2007-09. Murton participated in the important interagency discussions held on Columbus Day weekend in 2008 that led to the establishment of breakthrough programs that proved critical in stabilizing financial markets. This "Lessons Learned" summary is based on an interview with Mr. Murton about his crisis experience.

Broaden the View: Regulators should assume more watchful and nuanced monitoring.

Despite concerns about and analyses of subprime lending activities and the potential risks posed to the economy in the years leading up to the crisis, there was a lack of understanding among regulators of how intertwined financial institutions had become and how severe a problem was developing, notes Murton. He says,

> We didn't appreciate the magnitude of the problems that we were going to have, and we didn't really have a good window into some of the interconnectedness in the banking system and financial system. Things such as SIFIs [systemically important financial institutions] we weren't really aware of and didn't see how the risk was building up, not in the banks themselves, but in their affiliates and other holdings.

Understanding current risks to the financial system requires vigilance by the regulatory community, says Murton. He stresses that it is important for regulators, like the FDIC, to keep abreast of developments like the linkages between banks and nonbanks in order to be prepared to address problems that may arise outside of the traditional banking system. He says,

> We need to do a better job before the problems arise. We need to be ready to exercise the authority we've been given. In the last crisis, we thought a lot of risk was outside the banking system and banks' balance sheets, but it all came back to the banks' balance sheets. So, we can't be lulled into a false sense of security when problems arise outside the banking system."

Collaboration: The key to successful programs.

Working in concert with other federal agencies, including Treasury and the Federal Reserve, to establish the debt guarantee programs aimed at stabilizing the financial system, says Murton, sped up the design of the programs and allowed for a structure that was financially sound. The collaboration among agencies was valuable in coping with issues that were new to all and necessary to implementing the programs and their ultimate success.

It was also important, he notes, to work together with those that would be issuing the guaranteed debt, in order to manage operational issues and smooth out snags in the early stages of the programs. He observes,

> What we learned was that the partners of this debt expected regular payments at regular times and wanted those payments to come at precisely the times they were supposed to, and there's a specific term for it called "time and payment." We had to be prepared to make the payments that the debtor expected at precisely the time they were due. That was different from what we did in normal bank failures.
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> We had to work out operational issues as to how we would do this and come up with ways that we could be sure that we could make the payment if one of these banks that had issued this guaranteed debt defaulted. For example, with commercial paper, which is based on short-term debt, it could be an issue if, in the case of a default, the relevant parties would learn of it in the morning and we would need to be able to pay it by the end of the afternoon. We had to work with the Treasury and the Federal Reserve and others to come up with a way that we could do that. Once we did that, the banks and the public got much more confident with the different programs.

Global engagement: Building a stronger global financial system is necessary.

Historically, the FDIC didn't interact much with its overseas financial regulatory counterparts, and so while the Europeans were first movers in rolling out guarantee programs and coordinated their efforts, U.S. efforts lagged, unable to draw on the European models, Murton recounts. That dynamic changed as a result of the crisis. He notes,

> It was a time, before the financial crisis, that the FDIC didn't have a lot of engagement with other financial regulatory authorities in the other jurisdictions, which is completely different today. We now have very strong relationships with other jurisdictions, particularly the UK and the Bank of England, and the European Union through the Single Resolution Board, and so forth.
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> We have a lot of engagement with them so it would be a very different situation today if something like this were to happen. We have a lot more dialogue about these things. We're in a better position to deal with future problems because we have this kind of engagement.

Date: June 2021
YPFS Lessons Learned No: 2019-49