

**HEARING BEFORE THE UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES**

April 10, 2019

Testimony of Ronald P. O'Hanley
President and Chief Executive Officer, State Street Corporation

Chairwoman Waters, Ranking Member McHenry, and members of the Committee, thank you for inviting me to testify today.

Who We Are and What We Do

I was honored to become State Street's CEO on January 1, 2019. Headquartered in Boston, Massachusetts, and founded in 1792 (the same year as the New York Stock Exchange and the Post Office Department), State Street has two core lines of business - investment servicing and investment management. Our purpose is to create better outcomes for the world's investors and the people they serve. Unlike many other major banks, we do not serve retail consumers directly. Our clients are large global institutions such as pension funds, mutual funds, central banks, sovereign wealth funds, and insurance companies. As of year-end 2018, our total consolidated assets were \$245 billion, our assets under custody and administration on behalf of our clients were \$31.62 trillion and our clients' assets under management were \$2.51 trillion. We operate in 29 countries with more than 40,000 employees, about 16,000 of whom are based in the United States. We serve approximately 4,500 institutional clients globally.

State Street is organized as a U.S. bank holding company, with operations conducted through several entities, primarily our wholly-owned insured depository institution subsidiary, State Street Bank and Trust Company. State Street Bank and Trust Company is a Massachusetts state-chartered bank and member of the Federal Reserve System, and operates through three U.S. branches, including our main office in Boston and 11 non-U.S. branches around the world. State Street Global Advisors, our investment management arm, is a global leader in institutional asset management, managing assets for investors including pension funds, endowments, and foundations. State Street is also registered as a limited purpose (i.e., for foreign exchange trading only) swap dealer with the Commodity Futures Trading Commission (CFTC).

Because we are not a commercial, retail, or investment bank, we do not provide typical commercial or retail banking services such as traditional mortgages, consumer credit, commercial lending, savings or checking accounts, or underwriting securities. As a result, State Street does not encounter consumer-focused issues, such as forced arbitration clauses. Our capital markets trading business is focused on foreign exchange trading, largely to facilitate international investments by our institutional client base. We do not make markets in asset classes other than foreign exchange.

We serve institutions that are making investments on behalf of others. Our services, which can be broadly characterized as the safekeeping, servicing, and management of assets, allow the investment process to operate smoothly and as intended, ultimately allowing our clients' customers - individual citizens with savings - confidence that their investments will be available when they need them.

Our investment servicing line of business provides custody, accounting, daily pricing and administration, master trust and custody, record-keeping, cash management, foreign exchange, securities lending, deposit and short-term investment facilities, performance risk and compliance analytics, and financial data management.

Our investment management business provides a full range of investment options. Most of our assets under management are in low-cost, index-based funds. We are also a leading provider of exchange-traded funds (ETFs), including the SPDR ETF.

The nature of our core businesses results in a different risk profile compared with retail, commercial, or investment banks. Like all banks, State Street faces credit risk, market risk, liquidity risk, and operational risk. The extent to which we face each of these risks, however, is significantly different from that of other banking models. In general, our potential risk to the financial system is more related to operational risk than credit or market risk, compared with more traditional banking models.

State Street's Commitment to Diversity

I strongly believe that diversity contributes to better performance, decision-making, and outcomes, and I agree with the Chairwoman that our industry needs to do better in this area.

State Street's commitment to improving workforce diversity includes educational efforts (such as unconscious bias training), broad inclusion programs (such as

more than 30 employee resource groups around the world), and a diverse slate requirement for more senior hires. Further, progress on achieving our diversity goals and support for diversity programs are considered (along with other factors) in making executive compensation decisions.

Today, close to 40 percent of our Management Committee and 25 percent of our Board are women. Over the past five years, we have seen improvement in the numbers of employees of color at our senior management levels. However, we have some distance to go with African-American, Latino and Hispanic representatives on our Board and Management Committee, where we currently have none. I am personally committed to ensuring that diversity is a key priority at all levels of our organization.

I am also proud of our ongoing efforts to promote the use of diverse contractors, such as our more than 15-year record of using diverse brokerage firms. In 2017, we spent more than \$97 million with women-, minority-, and veteran-owned businesses and have recently initiated a formalized and more aggressive program to promote the use of minority contractors.

We are very proud of our 100% score on both the Human Rights Campaign Index for our inclusion of LGBTQ professionals in the workplace, and the Disability Equality Index for our disability inclusion policies and practices. We have also appeared six times on the Working Mother 100 Best Companies list.

State Street's Approach to Compensation

State Street unequivocally supports equal pay for equal work. Given the competitive, talent-driven industry that we operate in, we are focused on incentivizing, rewarding, retaining, and motivating superior employees through performance-driven compensation in a manner aligned with sound risk management and our corporate values.

Since the financial crisis, State Street has taken numerous steps to enhance our compensation practices to further support both long-term shareholder value and financial stability. This includes more closely aligning incentive compensation with the risks and performance results experienced by our shareholders, most notably through the use of significant levels of deferred equity-based compensation that vests over time. All incentive compensation awards are subject to multiple recourse mechanisms, including ex ante adjustment (downward adjustments to awards before they are made), and forfeiture (reduction or cancellation of awards after they are made but before vesting). In addition, all awards made to our Executive Vice President and Management Committee leaders are additionally subject to claw-back (repayment of historic

awards already vested and delivered). In instances of violations of State Street's policies, we have and will continue to use all appropriate recourse mechanisms with respect to an executive's compensation.

State Street's Commitment to the Community

State Street is committed to supporting the communities in which we live and operate. For example, last year, our Foundation invested \$21.5 million in grants to support local communities.

Our Boston Workforce Investment Network (Boston WINs) is our signature venture philanthropy initiative where we have brought together five non-profit organizations to pursue a common goal of helping prepare disadvantaged youth for the workforce. Boston WINs' goals are: 1) help increase college enrollment rates for Boston public high school students, 2) ensure that once Boston public high school students get to college, they stay there, and 3) enhance career pathways for Boston youth, resulting in more stable employment and economic mobility.

State Street's Investment in the Community

Despite the fact that we do not provide consumer or commercial banking services, we have achieved "outstanding" ratings from the Federal Reserve for eight consecutive Community Reinvestment Act (CRA) examinations, dating back to 2003. State Street, as a wholesale bank, meets the needs of low- and moderate-income populations in four main ways:

1. Our State Street Foundation and corporate sponsorships of education and workforce development nonprofits, as well as employee-driven matching grants to non-profits worldwide;
2. Affordable housing investing;
3. Mortgage-backed securities investing (low- to moderate-income borrowers) and small business (SBICs) investing; and
4. Community development services, including State Street executives serving on non-profit boards. Approximately three quarters of our Executive Vice Presidents serve on non-profit boards.

State Street since the Financial Crisis

More than ten years after the global financial crisis, I believe the banking system in the U.S. is safer and more resilient, thanks to post-crisis regulatory reforms

including higher capital and liquidity requirements, rigorous stress testing, and extensive resolution and recovery planning requirements.

State Street was one of the nine banks asked by Secretary Paulson in 2008 to participate in the Troubled Asset Relief Program (TARP), and received \$2 billion in TARP funds. Although State Street's business model was not the driver of the crisis, we are grateful to the Congress and to the American people for the role they played in supporting the stability of markets and the financial system. After passing the U.S. Federal Reserve's May 2009 stress test by a wide margin, we were the first of the original "TARP 9" banks to fully exit the program by both repaying the invested funds and repurchasing the associated warrant. In addition, we supported other U.S. government efforts to address the financial crisis, most notably in our collaboration in 2008 with the Federal Reserve Bank of Boston in connection with the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF), which successfully supported money market fund liquidity during the crisis. While I appreciate the importance of these government efforts to address the financial crisis, I am committed to learning lessons from those years, and avoiding the need for such actions in the future.

State Street was designated as one of the eight U.S. Global Systemically Important Banks (G-SIBs) by the Financial Stability Board in 2011. While most of the G-SIB criteria relate to financial intermediation and interconnectedness, State Street was designated as a G-SIB due to the importance of our global custody business to the ongoing operation of the financial system in times of stress. We are also designated as a U.S. Systemically Important Financial Institution (SIFI) under the Dodd-Frank Act, and, due to our G-SIB status, will remain a U.S. SIFI despite changes in SIFI designation recently enacted by Congress for other banks with under \$250 billion in assets.

As a G-SIB and U.S. SIFI, we take our compliance responsibilities very seriously and we are subject to the highest levels of increased post-crisis supervision and regulation, which includes:

- Substantial increases in both risk-weighted and leverage capital --- State Street's Tier 1 capital has more than doubled since 2007, and all of our capital ratios are well over regulatory minimums;
- Increased and formalized requirements for liquidity, through the new Liquidity Coverage Ratio (LCR) and a new "Liquidity Program" (a horizontal assessment across large banks covering liquidity under both normal and stressed conditions). For State Street, the percentage of our balance sheet that qualifies as high-quality liquid assets (HQLA) has doubled since 2012;

- Extensive requirements to prove resolvability upon failure, through the new “living wills” process;
- Demanding stress testing of capital adequacy, through both the Dodd-Frank Act Stress Test (DFAST) and the Comprehensive Capital Analysis and Review (CCAR) process; and
- New loss absorbency requirements developed solely for large banks, through the new total loss-absorbing capacity rule (TLAC), under which we hold more than \$26 billion of loss-absorbing capacity in the form of Tier 1 capital and long-term debt to provide, if necessary, the resources for an orderly recapitalization of State Street.

Like every major financial institution, State Street works hard to remain vigilant about potential cybersecurity threats. We take our role as a trusted provider extremely seriously and we continue to devote significant time and resources to improving the governance and controls of our information security processes through monitoring, surveillance, and testing.

State Street is currently executing a technology transformation program focused on retiring legacy applications and modernizing our systems. As a result, our total spending on information technology is approximately 25 percent of our total expenses, enabling us to extend cyber and information security protections throughout our global organization and aligned operations, including subsidiaries, affiliates, and joint ventures, around a common security framework overseen by dedicated personnel under the leadership of our Chief Information Security Officer (CISO). The CISO is responsible for information security and coordinates the global activities of Information Security Officers (ISOs) assigned to each organizational unit. We are active participants in numerous industry and government cyber-related forums, including the Financial Systemic Analysis and Resilience Center (FSARC) and the Financial Services Information Sharing and Analysis Center (FS-ISAC).

State Street’s Commitment to Risk Excellence

In the years since the financial crisis, State Street has launched numerous initiatives intended to strengthen our corporate culture, most recently through our Risk Excellence initiative aimed at elevating the importance of risk and compliance excellence across our organization. This includes a programmatic education of our workforce, “Speak Up” training to encourage and facilitate all employees’ reporting of issues, and risk excellence criteria for all employees’ performance evaluations, compensation decisions, and executive promotions.

I strongly believe that trust is our greatest asset. We have, unfortunately, over the years since the crisis, had instances that led to enforcement actions and financial settlements with the government and clients. Since 2009, we have reimbursed clients and made payments to government agencies in settlements totaling approximately \$1 billion. This amount is primarily attributable to seven matters involving enforcement.

We deeply regret these situations and have reimbursed clients and strengthened related risk and compliance controls. I am committed to continuing to ensure that we have learned from their causes and to advancing a culture of trust and accountability at State Street. We enforce strict policies against employee misconduct.

Lessons Learned from the Financial Crisis

I believe there are a number of important lessons we learned from the financial crisis, including:

- It is critical for supervision and regulation to keep pace with industry developments, and to be tailored according to the risk profile of the individual institution. While ongoing adjustments, such as legislation recently passed by Congress, are appropriate, the general approach adopted by the Dodd-Frank Act of applying heightened prudential requirements related to capital, liquidity, and resiliency for larger banks has made our financial system stronger.
- The crisis revealed weakness in the risk management functions of many banks, which were often siloed and uncoordinated. We have strengthened our top-down risk management systems at State Street so that we have better transparency around enterprise-wide risks. We now have stronger, independent control functions and higher-quality risk analytics.
- The crisis cast a bright light on the dangers of groupthink in corporate leadership. That is one of the reasons why we have stepped up our focus on board diversity, including gender diversity, to promote better business and investment outcomes. Our asset manager, State Street Global Advisors, launched a major initiative to focus on the value of board diversity across all industries, most visibly through the placement of the Fearless Girl statue, which now stands outside the New York and London stock exchanges as a reminder of the power of female leadership.
- The crisis also exemplified the risks of short-term decision-making at the expense of long-term value creation. Misplaced incentives rewarding short-

term gains were clearly one of the root causes of the crisis. I believe we all will benefit from a focus on long-term goals, which includes asking ourselves and the boards of the companies in which we invest whether environmental, social and governance risks that might impact a company's ability to generate sustainable performance have been considered.

- We acknowledge that we must answer to stakeholders beyond our shareholders alone, including our employees, our clients, and our communities. With this in mind, we announced last year that some of the savings that we received from the recently enacted U.S. tax reform would be invested in retirement benefits for our employees, and used for increased support for charitable giving in our communities as well as increased investment in employee learning and development.

The legacy of the financial crisis, in addition to financial harm, includes an enduring lack of trust in our industry by the public. I know that State Street can only be as successful as the larger society in which it operates, and we are committed to engaging on those issues that will generate shared value for all of our stakeholders.

Conclusion

Ten years after the crisis, State Street is stronger and more resilient and, I believe, more nimble and responsive to emerging and new risks. I continue to believe that our financial system is the strongest, most innovative, and most productive in the world. I look forward to doing my part in ensuring that State Street is a source of stability to our financial markets, and providing services that support and protect the financial future of all Americans.

Thank you again for providing me the opportunity to testify today, and I am pleased to answer any questions from the Committee.