OVERSIGHT OF PRUDENTIAL REGULATORS: ENSURING THE SAFETY, SOUNDNESS, DIVERSITY, AND ACCOUNTABILITY OF DEPOSITORY INSTITUTIONS

HEARING

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OVERSIGHT OF PRUDENTIAL REGULATORS: ENSURING THE SAFETY, SOUNDNESS, DIVERSITY, AND ACCOUNTABILITY OF DEPOSITORY INSTITUTIONS

Wednesday, December 4, 2019

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:08 a.m., in room 2141, Rayburn Office Building, Hon. Maxine Waters [chairwoman of the committee] presiding.

Members present: Representatives Waters, Maloney, Sherman, Meeks, Clay, Scott, Green, Cleaver, Perlmutter, Himes, Foster, Beatty, Heck, Vargas, Gottheimer, Gonzalez of Texas, Lawson, Tlaib, Porter, Axne, Casten, Pressley, McAdams, Ocasio-Cortez, Wexton, Adams, Garcia of Illinois, Phillips; McHenry, Wagner, Lucas, Posey, Luetkemeyer, Huizenga, Stivers, Barr, Tipton, Williams, Hill, Emmer, Zeldin, Loudermilk, Mooney, Davidson, Budd, Kustoff, Hollingsworth, Gonzalez of Ohio, Rose, Steil, Gooden, Riggleman, and Timmons.

Chairwoman WATERS. The Financial Services Committee will come to order.

Without objection, the Chair is authorized to declare a recess of the committee at any time.

Today's hearing is entitled, "Oversight of Prudential Regulators: Ensuring the Safety, Soundness, Diversity, and Accountability of Depository Institutions." I want to inform all concerned that this hearing will end either at 1:30 p.m., or at the first series of votes on the House Floor.

I now recognize myself for 4 minutes to give an opening statement.

Today, we are here to conduct oversight of the regulators at the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve (Fed), and the National Credit Union Association (NCUA), as well as to receive written testimony from the Office of the Comptroller of the Currency (OCC). So, I would like to welcome back Chair McWilliams, Vice Chairman Quarles, and Chairman Hood.

I am very concerned that our banking regulators are following the dangerous deregulatory blueprint that the Trump Administration laid out in a series of Treasury reports, and checking off deregulatory items one by one. For example, they have moved to weaken capital stress testing and other requirements for the larg-

est financial institutions; taken action to weaken the Volcker Rule, which prevents banks from gambling with taxpayer dollars; and proposed weakening the swap margin rule, which would threaten our economic stability for a $40 billion giveaway to Wall Street megabanks. In rolling back important reforms put in place in the Dodd-Frank Wall Street Reform and Consumer Protection Act to protect consumers, investors, and the economy, regulators are opening the door to the bad practices that contributed to the devastating financial crisis of 2008.

I am also very concerned that regulators are making a brazen attempt to weaken the implementation of the Community Reinvestment Act (CRA) under the guise of modernization. CRA is an important law that was passed in 1977 to prevent redlining and to ensure that banks are meeting the credit needs of the communities where they are chartered. While the implementation of the law needs updates to reflect the modern banking landscape, those changes should make the law more effective, not less. Ninety-eight percent of banks already receive a passing grade on their CRA exam, which shows that the law needs more teeth to get positive results for underserved communities.

In the wake of the regulators' approval of the SunTrust-BB&T merger, which creates the 6th largest bank in the nation, I would like to make it clear that this committee will continue to closely scrutinize large bank merger proposals. Regulators have a responsibility to ensure that bank mergers serve the public interest and do not create megabanks that threaten our economy and financial system. And it is not acceptable for bank mergers with implications for communities across the country to receive a cursory review or a rubber stamp from bank regulators.

This committee has been very focused on diversity and inclusion in the financial services sector, including through the committee's historic new Subcommittee on Diversity and Inclusion. Earlier this year, I, together with Congresswoman Beatty, who Chairs the Subcommittee on Diversity and Inclusion, wrote to the megabanks and requested their diversity and inclusion data and policies. The information we received reinforces what we already know, that these banks badly need to improve their diversity and inclusion.

For example, less than 1 percent of megabank spending is devoted to diverse asset managers and suppliers. Since each of the agencies represented by our witnesses today has a dedicated Office of Minority and Women Inclusion (OMWI), I expect to hear today about their diversity and inclusion efforts. I look forward to discussing these matters with our witnesses.

I now recognize the ranking member of the committee, the gentleman from North Carolina, Mr. McHenry, for 4 minutes.

Mr. MCHENRY. Thank you, Madam Chairwoman, for holding this hearing today. It is a very important and necessary hearing. It's good for our members to get this interaction with the regulators, and I appreciate all of them being here. And so, I want to thank Chairs Hood and McWilliams and Vice Chair Quarles for appearing before the committee today.

And I want to thank each of you for taking the time not just to testify, but for prioritizing the common-sense reforms that are necessitated by the bipartisan law that we commonly refer to as

S.2155. The last time you testified before the committee in May, we called on you to take swift action on implementing this bill, and you have largely answered the call. Clarifying the Volcker Rule, and tailoring requirements for foreign banks, are just a few examples of regulatory rightsizing that you have implemented to ensure that our economy, small businesses, and consumers remain vibrant and strong. However, there is more work to be done. There is certainly more work to be done. And what we would like to see from you is for the pace to go up and continue to go up so that we are staying ahead of market conditions and economic conditions. We need to make sure that the tools are there to help serve consumers and communities.

I also want to take this opportunity to raise a number of concerns that I continue to have. I am concerned with the trend in the Federal Reserve's open market operations and the wholesale funding markets. I appreciate Chairman Powell's prompt response to my recent questions about the Federal Reserve's repo market operations, and I understand there may be further interventions necessary at the end of the year. The Fed's intervention in the repo market raises the important question of how regulatory changes to our financial system are impacting its structure and function and impacting monetary policy.

I think it is very important for the Federal Reserve to have its independent monetary policy standards. I also think it is very important for the global economy, the American economy, and American consumers. But it is necessary for Congress to have oversight of those regulatory changes. And in this circumstance, if bad regulation is driving monetary policy, I think that raises greater concerns about financial stability in the market, and also economic growth. So in addition, the combined impact of proposed capital requirements, including Basel III revisions, and the stress capital buffer could have a significant impact on required capital if not thoughtfully implemented. This may further exacerbate the underlying issues that we are seeing. So, it is important to consider the system of capital requirements as a whole to ensure regulations are appropriately calibrated to allow institutions to continue to support economic growth.

In addition, in May, I voiced my concerns with the transition from the London Interbank Offered Rate (LIBOR) to the Secured Overnight Financing Rate (SOFR). Six months later, I am still concerned that consumers will be impacted by this transition. The repo market intervention is just one example of why that is of concern and should be of concern to average, everyday investors. As you know, LIBOR is the underlying bank reference rate for approximately $200 trillion in financial contracts worldwide and is to be phased out as a bank reference rate by 2021, and replaced with SOFR. Given the volatility in the repo markets, I am concerned about the consequences that that volatility will have on mortgages, auto loans, business loans, and other consumer loans as a new reference rate if that is driving overnight financing. Transferring LIBOR-based legacy contracts to SOFR will also require financial institutions to renegotiate with consumers, customers, and expose banks to litigation risk.

I hear clearly the tap, tap, tap of the gavel, and with that, I will reserve the rest of my comments for my questions. But thank you for being here, and I appreciate your attendance.

Chairwoman WATERS. I now recognize the gentleman from New York, Mr. Meeks, who is also the Chair of our Subcommittee on Consumer Protection and Financial Institutions, for 1 minute.

Mr. MEEKS. Thank you, Chairwoman Waters. I am glad we have three of the prudential regulators before us today, but I am very disappointed that Mr. Otting, the Comptroller of the Currency, did not make himself available to testify today. One of the issues I have spent the most time on this year, including chairing subcommittee hearings, sending letters, and leading a tour of my district in Queens this past summer, is the modernization of the Community Reinvestment Act. It appears that the Office of the Comptroller of the Currency (OCC) has abandoned the joint agency process and will plow forward with its approach to CRA modernization with a simple metric to evaluate bank lending to formerly-redlined communities. This approach is likely to decouple the link between CRA and the very communities it was created to service, and discriminate against whom it was meant to bring redress.

I look forward to engaging with the witnesses here today on this and other issues, particularly dealing with non-bank lenders, small-dollar loans, and broker deposits, and I look forward to engaging with the witnesses shortly. I yield back the balance of my time.

Chairwoman WATERS. Thank you. I now recognize the subcommittee's ranking member, Mr. Luetkemeyer from Missouri, for 1 minute.

Mr. LUETKEMEYER. Thank you, Madam Chairwoman. I would also like to thank the panel for testifying today. I look forward to discussing multiple issues with you regarding our financial system.

I would like to begin by reiterating my concern over the Financial Accounting Standards Board's (FASB's) Current Expected Credit Losses (CECL) accounting standard. Time and time again in hearings before this committee, it has been stated that CECL will have a detrimental effect on small financial institutions and, specifically, low- to moderate-income and minority consumers. Despite the numerous testimonies, hearings, statements, and letters highlighting these issues, this committee has remained silent. Not one hearing examining CECL, and no congressional oversight on any accounting standard that will prevent Americans from achieving the American Dream of homeownership.

While I will discuss issues with the panel besides CECL, I am hopeful that some of our witnesses who will be charged with enforcing the standard will outline how they plan to protect consumers in the absence of committee action. With that, I yield back the balance of my time.

Chairwoman WATERS. Thank you. I want to welcome today's distinguished panel: the Honorable Rodney Hood, Chairman of the National Credit Union Administration; the Honorable Jelena McWilliams, Chair of the Federal Deposit Insurance Corporation; and the Honorable Randal Quarles, Vice Chairman of Supervision for the Board of Governors of the Federal Reserve System. I note that the Comptroller of the Currency, Joseph M. Otting, was in-

vited to testify at today's hearing, but was unable to appear. I intend to have him appear as soon as possible before this committee, and he may be a single panel, but it is important, Mr. Meeks, that we hear from him. I understand he has submitted some written testimony, but that does not really substitute for his appearance here today.

Each of you will have 5 minutes to summarize your testimony. And without objection, all of your written statements will be made a part of the record.

When you have 1 minute remaining, the yellow light will appear. At that time, I would ask you to wrap up your testimony so we can be respectful of both the witnesses' and the committee members' time.

Chairman Hood, you are now recognized for 5 minutes to present your oral testimony.

STATEMENT OF THE HONORABLE RODNEY E. HOOD, CHAIRMAN, NATIONAL CREDIT UNION ADMINISTRATION (NCUA)

Mr. HOOD. Chairwoman Waters, Ranking Member McHenry, and members of the committee, good morning. As the 11th Chairman of the National Credit Union Administration Board, I am honored to testify before you this morning. In my brief opening statement, I will be discussing 3 topics: first and foremost, the state of America's credit union system; second, NCUA's efforts to foster diversity and inclusion; and third, cybersecurity.

First and foremost, I'd like to note that strong growth trends in federally-insured credit unions are continuing in 2019. Roughly 119 members are a part of the credit union system. That represents roughly one-third of the American public. Credit union assets through the third quarter are approximately $1.54 trillion. Credit unions also have a really strong net worth at the moment, an 11.39 percent aggregate net worth, well above the 7 percent statutory requirement. The National Credit Union Insurance Share Fund also remains well-funded at $16.7 billion, and it should be noted that that is a sizable increase from where it was at approximately at $10 billion, 10 years ago. Year-to-date operating results evidence that the credit union system is solid and healthy.

I'd now like to focus my attention on discussing NCUA's efforts to foster diversity and inclusion. I firmly believe that financial inclusion is the civil rights issue of our time. However, inclusion means not only broader access to financial services, but also employment and business opportunities. NCUA takes its responsibility seriously in implementing Dodd-Frank Section 342. When I travel around the country, I mention the importance of filling out the diversity survey. I also work with the head of our Office of Minority and Women Inclusion (OMWI), Monica Davy, to ensure that we are reaching out to diverse minority businesses.

To that end, I'm pleased to report that NCUA supplier diversity spend is 44.5 percent, to date. In addition, NCUA just hosted its first-ever Diversity, Equity and Inclusion (DEI) Summit. This summit took place just a few weeks ago, and it really demonstrated the importance of diversity and inclusion being more than a check-the-box exercise. Rather, our diversity, Equity and Inclusion Summit demonstrated that this should be viewed as a business and stra-

tegic imperative if credit unions are going to respond nimbly to shifting demands and demographics and to respond to today's dynamic marketplace. Given the well-attended DEI event, I'm intending now to host the DEI summit across the United States, so we're going to make this a yearly event. And I, to the degree possible, would like to invite you all on the House Financial Services Committee to join us when we host these summits in your areas.

Minority depository institutions (MDIs) are the lifeline in providing affordable financial services in communities of color. NCUA provides capacity-building activities to help these institutions reach and serve their mission. Capacity-building activities at NCUA include ongoing education, technical assistance, and our newly-launched mentoring program. I will in turn be hosting an MDI summit in early 2020 so that these institutions can continue to get the necessary support they need to bring affordable financial services to communities of color.

I'm very pleased to report that the NCUA board is also supporting diversity and inclusion. We just recently, as a board, developed a short-term ODAR product to provide opportunities for people needing emergency loans. We're calling it the PALs II Program, and it is a responsible alternative loan product for people so that they will no longer need to go to pernicious payday lenders to get their needs met. We also, as an NCUA board, have approved the Second Chance Initiative. The Second Chance Initiative works with individuals who have had nonviolent criminal offenses in the past, and who have paid their debt to society, so now these individuals can work with federally-insured credit unions so they can have greater opportunities for career success, and also have opportunities for upward mobility and access to shared prosperity.

The third area I'd like to talk about is cybersecurity. Cybersecurity is a high priority for me as chairman. Cyber attacks are acute, and we are making sure that we leverage our resources to provide credit unions with the support they need to combat these challenges.

In closing, I would like to go back to my statement again of financial inclusion being the civil rights issue of our time. Ladies and gentlemen of the committee, I would like to work in partnership with the House Financial Services Committee to look for legislative solutions to help credit unions adopt underserved areas. Thank you.

[The prepared statement of Chairman Hood can be found on page 66 of the appendix.]

Chairwoman WATERS. Chair McWilliams, you are now recognized for 5 minutes to present your oral testimony.

STATEMENT OF THE HONORABLE JELENA MCWILLIAMS, CHAIRWOMAN, FEDERAL DEPOSIT INSURANCE CORPORATION

Ms. MCWILLIAMS. Thank you. Chairwoman Waters, Ranking Member McHenry, and members of the committee and staff, thank you for the opportunity to testify today. Exactly 18 months ago, I began serving as the 21st Chairman of the FDIC, and I'm happy to celebrate my half-birthday with all of you here today.

During this period, the FDIC has undertaken a great amount of work with a particular emphasis on three overarching goals: one,

strengthening the banking system as it continues to evolve; two, ensuring that FDIC-insured and supervised institutions can meet the needs of consumers and businesses; and three, fostering technology solutions and encouraging innovation at community banks and the FDIC. The FDIC has made significant progress in each of these areas, and I appreciate the opportunity to share our progress with this committee.

Before discussing the FDIC's work to strengthen the banking system, I would like to begin by providing context regarding the current state of the industry. The U.S. banking industry has enjoyed an extended period of positive economic growth. In July, this expansion became the longest on record in the United States. By nearly every metric, the banking industry is strong and well-positioned to continue supporting the U.S. economy. While the state of the banking industry remains strong, the FDIC is continuing to monitor changes in the industry and to work to further strengthen the banking system by modernizing our approach to supervision, including outdated regulations and increasing transparency, enhancing resolution preparedness, assessing new and emerging risks, and creating the workforce of the future. My written statement details the many actions the FDIC has taken in each of these areas.

While these efforts are steps towards a stronger banking system, there are certain areas in which the needs of consumers and businesses must be addressed by more comprehensive reforms. We have been working diligently to update our regulations governing broker deposits, which were put in place over 30 years ago. In addition, we're working with our fellow regulators to modernize the Community Reinvestment Act and provide clarity for banks seeking to offer loans that meet consumer small-dollar credit needs.

Finally, perhaps no issue is more important or more central to the future of banking than innovation. Technology is transforming the business of banking both in the way consumers interact with their banks and the way banks do business. Regulators cannot play catch-up, but must be proactive in engaging with stakeholders, including banks, consumer groups, trade associations, and technology companies to understand and help foster the safe adoption of technology across the banking system, especially at community banks.

Since 1933, the FDIC has played a vital role in maintaining stability and public confidence in the nation's financial system. This mission remains as critical today as it was 86 years ago. But if we are to achieve our mission in a modern financial environment, the agencies cannot be stagnant. Last year, I began a 50-State listening tour to engage with State regulators, FDIC-regulated institutions, consumers, and other stakeholders. At the outset of that effort, I emphasized the need to reverse the trend of having those affected by our regulations come to Washington to have their voices heard, but instead to meet them on their home turf. With 26 State visits, I'm now more than halfway through the listening tour, which has been incredibly informative and has underscored the importance of seeking perspectives outside of the Washington beltway.

I look forward to visiting the remaining States and learning more about the issues that matter most to consumers and communities

across the nation, including your constituents. Thank you again for the opportunity to testify, and I look forward to your questions.

[The prepared statement of Chairwoman McWilliams can be found on page 89 of the appendix.]

Chairwoman WATERS. Thank you. Vice Chairman Quarles, you are now recognized for 5 minutes to present your oral testimony.

STATEMENT OF THE HONORABLE RANDAL K. QUARLES, VICE CHAIRMAN OF SUPERVISION, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM (FED)

Mr. QUARLES. Thank you. Chairwoman Waters, Ranking Member McHenry, and members of the committee, thank you for the opportunity to appear today. My colleagues and I join you on the cusp of a significant and shared milestone: the full and faithful implementation of Congress' effort to improve financial regulation in the form of the Economic Growth, Regulatory Relief, and Consumer Protection Act. Today, I'll briefly review the steps we've taken toward this milestone, share information on the state of the banking system, and discuss the continuing need to ensure our regulatory framework is both coherent and effective.

The Act was an effort to consolidate a decade of work on financial reform and a targeted response to the conditions facing today's banking organizations and their customers. It was also rooted, however, in a longstanding constitutional practice of reviewing the work done in the immediate aftermath of a crisis, of addressing any gaps, and of ensuring that public and private resources go toward their best and most efficient use.

The Board's latest supervision and regulation report, delivered in connection with my testimony today, confirms that we have a stable, healthy, and resilient banking sector with robust capital and liquidity positions, stable loan performance and strong loan growth, steady improvements in safety and soundness, and several areas of continued supervisory focus, including operational resiliency and cyber-related risk. The banking system is substantially better prepared to manage unexpected shocks today than it was before the financial crisis. And now, when the waters are relatively calm, is the right time to examine the efficiency and effectiveness of our protection against future storms.

With last year's reform legislation, Congress made a significant down payment on that task, and in less than 18 months after the Act's passage, we have implemented all of its major provisions. Earlier this year, we completed the cornerstone of the legislation, tailoring our rules for regional banks and building on our existing work that firms with greater risks should meet higher standards and receive more scrutiny. We previously relied heavily on a firm's total assets as a proxy for these risks and for the cost that the financial system would incur if a firm failed, and that simple asset proxy was clear and critical. It was rough and ready, but it was neither risk-sensitive nor complete. Our new rules employ a broader set of indicators to assess the need for greater supervisory scrutiny and maintain the most stringent requirements and strictest oversight for the largest and most complex firms.

We and our interagency colleagues have also worked on a range of measures addressed to smaller banks, with particular attention

to the community bank business model. And our goal through this intense period of regulatory activity has been to faithfully implement Congress' instructions. Those instructions also speak to a broader need, and one central to our ongoing work, which is to ensure that our regulatory regime is not only simple, efficient, and transparent, but also coherent and effective.

Financial regulation, like any area of policy, is a product of history. Each component dates from a particular time and place, and it was designed, debated, and enacted to address a particular set of needs. No rule can be truly evergreen. Gaps in areas for improvement will always reveal themselves over time. Our responsibility is to address those gaps without creating new ones, to understand fully the interaction among regulations, to reduce complexity where possible, and to ensure our entire rulebook supports the safety, stability, and strength of the financial system.

My colleagues and I are paying particular attention to coherence in our capital regime and in the full set of post-crisis reforms, to a smooth transition away from LIBOR and other legacy benchmark rates, to sensible treatment of new financial products and technologies, and to clear, consistent supervisory communication which reflects and reinforces our regulations and laws. My written testimony and the accompanying supervision and regulation report cover each of these areas in greater detail. And, again, I appreciate the opportunity to discuss them with you today.

Thank you, and I look forward to answering your questions.

[The prepared statement of Vice Chairman Quarles can be found on page 113 of the appendix.]

Chairwoman WATERS. Thank you. I now recognize myself for 5 minutes for questions.

Earlier this year, my colleague, Representative Meeks, held a subcommittee hearing focused on the Community Reinvestment Act. We heard expert testimony demonstrating that more than 40 years after the passage of the CRA, 98 percent of banks consistently pass their CRA exams, while at the same time we have redlining in more than 60 metro areas across the country. There is something out of sync. Instead of working together to make CRA exams more stringent and taking steps to ensure banks fairly serve all communities, we have at least the OCC, if not also the FDIC, in a rush to get a rulemaking out this year in a brazen attempt to weaken the CRA with or without the Federal Reserve. As we have seen in the growing list of deregulatory actions in recent months by these agencies, I am concerned that this new CRA proposal will simply make life easier for banks that have been making record profits.

So, Chair McWilliams, Comptroller Otting at the OCC, who unfortunately was unable to testify today in person, seems to be in a rush to get a proposed regulation out the door this year, and it appears the Federal Reserve does not agree with this proposal. Instead of signing onto the OCC's plan, would it not be helpful to encourage Mr. Otting to take more time to work with the Federal Reserve and see if there is a mutually-agreeable path forward? If we have two different CRA regulations, will that not lead to regulatory arbitrage and inconsistent application of the law?

This was in his testimony. He said, "The OCC is working with our colleagues at the FDIC to issue it jointly. A joint rule with the FDIC would cover all national banks and State banks that are not members of the Federal Reserve System and Federal/State savings associations." So, you are here today to speak for yourself? Is that what you are doing?

Ms. MCWILLIAMS. Yes, we are engaged in interagency negotiations on how to best modernize and improve the CRA.

Chairwoman WATERS. Are you working with Mr. Otting and the OCC to issue a joint proposal?

Ms. MCWILLIAMS. We have been working with both the Federal Reserve and the OCC on—

Chairwoman WATERS. The Federal Reserve does not agree with you. How do you plan on resolving that?

Ms. MCWILLIAMS. I don't know how to resolve the Federal Reserve not agreeing with us. It wouldn't be the first time that the Federal Reserve and the FDIC have a difference of opinion on a particular matter, but I do know that there is an opportunity—since 1995, this Act has not been revised, and there is an opportunity to do more for minority depository institutions. There is an opportunity to do more—

Chairwoman WATERS. That opportunity to do more for minority institutions, how does that work?

Ms. MCWILLIAMS. That is a great question, and thank you for that. Right now, the non-minority depository institutions can qualify for CRA credit if they engage with a minority depository institution. Right now, the definition of how that partnership can be structured is more narrowly interpreted for the purposes of the CRA, and I believe there is an opportunity for us to expand what qualifies and what types of investments in community development activities with MDIs would qualify for CRA credit. There is also more to be done on small farms. There is a whole lot more we can do on CRA for small businesses, for Indian Country, and a number of different entities that, frankly, the CRA could be doing more for.

Chairwoman WATERS. Do you think it is important to work with this committee on such a huge change dealing with the CRA that is extremely important to so many communities? It seems as if you and Mr. Otting have just made a decision, despite the Federal Reserve and without any interaction with the committee. Why do you want to work in that way without trying to get in tune with all of the entities that are involved with trying to make a decision of this magnitude?

Ms. MCWILLIAMS. Chairwoman Waters, I have nothing but the utmost respect for this committee, and I look forward to working with you on any issues that are important to your constituencies. And as a former congressional staffer, I certainly would pay a lot of deference to your opinions and input on matters that are important.

Chairwoman WATERS. You have not demonstrated that to date. I appreciate your indicating that here at this hearing today. We are very concerned about this, and we are not accepting of any proposal that is being put together by you and Mr. Otting that undermines the original mission of the CRA. With that, I will—

Ms. MCWILLIAMS. If I may just add something?

Chairwoman WATERS. Thank you very much. The gentleman from North Carolina, the ranking member, Mr. McHenry, is recognized for 5 minutes.

Mr. MCHENRY. So to that extent, Chair McWilliams, safety and soundness is a primary obligation you have—economic growth, safety, and soundness. When you are inhibiting economic growth through old regulations on the books, that is bad, right? But when you are also impacting financial stability by not reviewing regulations, that is even worse, and I think that is malpractice. So I would encourage you to review these old regulations and take reasonable steps to ensure that we have financial stability on a going-forward basis.

Vice Chair Quarles, in September, there was tremendous volatility in the repo market. This is overnight lending. It is a very technical aspect for most Americans, but it is of concern to us as policymakers. Rates moved well beyond the Fed's targeted rate, which prompted the Fed to intervene in a pretty significant way, and for a significant amount of time pledged going forward. So given that, if you could comment on what policies might have contributed to the shortage of cash in the repo market?

Mr. QUARLES. Thank you. As you have noted, there was a complex set of factors that contributed to those events in September. Not all of them were related to our regulatory framework. But I do think that as we have considered what were the driving factors in the disruptions in the repo market in September, we have identified some areas where our existing supervision of their regulatory framework, less the calibration or structure of the framework itself, may have created some incentives that were contributors. They were probably not the decisive contributors, but they were contributors, and I think we need to examine them.

Particularly among them are the internal liquidity stress tests that we run that create a preference or can create a preference at some institutions for central bank reserves over other liquid assets, including Treasury securities for the satisfaction of their liquidity requirements under the liquidity framework that is put in post-crisis.

Mr. MCHENRY. That would be considered an unintended consequence of regulation rather than an intended consequence, would it not?

Mr. QUARLES. The regulation was intended to be structured so that banks would be indifferent between central bank reserves and other forms of liquid assets, particularly Treasury securities, in satisfying their high-quality liquid asset retention requirements, and the liquidity coverage ratio itself does not make any distinction.

Mr. MCHENRY. But in practice, it appears that there is a distinction.

Mr. QUARLES. Some banks, from their internal assessment of how their liquid assets will perform in a future period of stress, have put a heavy emphasis on central bank reserves as the most liquid assets. Treasury securities take a day to settle. Markets can be disrupted in the event of extreme unexpected events, so that does create a thumb on the scale for central bank reserves. So I think that it is worth reviewing, and we are reviewing some of these supervisory measures to see how they contribute.

Mr. MCHENRY. I would encourage you to review the regulatory and supervisory issues, and I think it is important for Congress to also hear back on that review. We understand the independence of monetary policy, but where regulatory policy is impairing or impacting monetary policy, I think we need to make sure that we are doing the right thing with these regulations.

Mr. QUARLES. I completely agree.

Mr. MCHENRY. I want to pivot as briefly as we can to the conversion from LIBOR to SOFR, and this change—the repo market issues in September highlight the deficiencies of this new SOFR standard. You commented publicly, Mr. Quarles, on some challenges related to that, and I think it would be important for Congress to hear back on the financial stability challenges, and the intention of the Federal Reserve to ensure that this new rate doesn't cause greater stress on the financial system or unnecessarily create financial instability. And so I would encourage that undertaking by the Fed, but I know it also impacts the FDIC and the NCUA as well. So with that, I yield back.

Chairwoman WATERS. The gentleman from California, Mr. Sherman, is recognized for 5 minutes.

Mr. SHERMAN. Shortly after you all testified in May, Daniel Tarullo, the Federal Reserve Governor who spent 8 years following the crisis, rewriting the Wall Street rulebook, denounced what he reviewed as the Trump era's low-intensity deregulation of the financial services industry. He described it as, "a large number of small tweaks to existing regulations that individually gather little notice by the press, but taken together will undermine the regulatory framework designed to prevent another crisis." He said that somewhere down the line, someone else will suffer the damage, and in all likelihood, it will be the most vulnerable households and businesses. Vice Chair Quarles, how do you respond to former Governor Tarullo's comments? Do you have a concern that easing the Volcker Rule, and dialing back on swap margin requirements, and reducing the leverage ratio for megabanks will not push the system a little closer to a crisis?

Mr. QUARLES. As we have looked at the recalibration of some of the post-crisis reform rulebook in order to ensure that we are not creating sort of perverse regulatory incentives and avoiding unintended consequences—it would be very surprising if there weren't some of those in such a complex body of post-crisis regulation—one of our principles has been to ensure that we do not reduce in any material way the loss-absorbing cushion of the institutions. And I think we have succeeded in doing that. Statements like that, that there is a low intensity deregulation, I think, have to be held to empirical account. And we have maintained the quantitative resiliency of the industry, and the changes that we have made, I think, actually improve the safety and soundness of the industry because they eliminate perverse regulatory—

Mr. SHERMAN. Obviously your predecessor, the Federal Reserve Governor, disagrees, but I want to go on. Resolution plans have been a valuable tool for improving resolvability through bankruptcy. Living wills have helped large banks be better organized, but now the FDIC seems to be dialing back those requirements.

Why should megabanks, like Wells Fargo, only have to update their complete living wills in only 4 years?

Ms. MCWILLIAMS. Thank you for that question, Congressman. The living will process has evolved since its inception in the enactment of Title II of Dodd-Frank. For a couple of cycles, we have received submissions that have been in the tens of thousands of pages, and we now have enough information where we can hone in and zoom in on the things that we actually think are more essential to resolving a bank and better our understanding of how that bank would be resolved. Frankly, what we are trying to avoid is having these banks just update the 20,000-page submissions every few years and not really look at some of the essential issues that are underlying. So I have asked staff to identify the critical areas that we need to do a deeper dive on, and to focus on those areas in particular.

Mr. SHERMAN. I would think that things change over years, and you might want to require updating more currently. The criteria for individuals seeking employment in the banking and financial services industry with minor criminal offenses are under review. First, Mr. Hood, what are you doing, and what could Congress do?

Mr. HOOD. Yes, sir. Thank you for that question. We, at NCUA, recently put forth a final rule regarding the Second Chance Act where we recognize that individuals who have committed nonviolent criminal offenses, who have paid their debt to society, should have opportunities to work in federally-insured credit unions. We look forward, sir, to partnering with you to see if opportunities exist to remove barriers.

Mr. SHERMAN. Ms. McWilliams?

Ms. MCWILLIAMS. I believe that the policy you are discussing—we are calling it our Section 19 policy at the FDIC—is an important social justice issue. And we are currently undertaking an effort to both publicly seek comments on what more the Agency can do. We have made some revisions, but I personally believe we can go a long way in enabling these individuals to reenter the workforce, and also allowing more prosperity in the economy by allowing them the opportunity to have a job.

Mr. SHERMAN. I will ask you to focus on that, and I yield back.

Ms. MCWILLIAMS. Thank you.

Chairwoman WATERS The gentlewoman from Missouri, Mrs. Wagner, is recognized for 5 minutes.

Mrs. WAGNER. Thank you, Madam Chairwoman. Vice Chairman Quarles, thank you for joining us today—and I thank all of you for joining us today—in September of 2019, you delivered a speech in which you reiterated the Fed's plans to finalize the stress capital buffer proposal in time for the 2020 Comprehensive Capital Analysis and Review, or CCAR, which means the rule would need to be proposed in the very, very near term. The goal of the stress capital buffer is to provide clarity and harmonization to the overall capital framework for financial institutions that are subject to stress tests. Vice Chairman Quarles, is it still the Federal Reserve Board's intention to have the stress capital buffer finalized in time for the 2020 CCAR?

Mr. QUARLES. We are still aiming to have that done in time for this stress testing cycle. You are absolutely right. That time is short.

Mrs. WAGNER. Given a re-proposal would need at least a 60-day comment period, and the CCAR instructions are typically issued in January, it seems like it would be very difficult to have that finalized. This proposal was originally released in April of 2018, so what is the reason for the significant delay in moving forward?

Mr. QUARLES. The proposal raises a number of complex issues. I think the most significant one is one that I have talked about publicly, and which is part of the answer to a previous question, which is that we do want to maintain the quantitative aggregate level of loss absorbency in the system to be the same, notwithstanding some of the incentive changes, some of the, I think, unwarranted assumptions and practices in the current stress testing regime. And calibrating and creating the methodology for keeping that aggregate capital level the same while addressing these incentives has proved to be complex. You are absolutely right that the time is short, but it is not impossible for us to get this done.

Mrs. WAGNER. When we can we expect a re-proposal of the stress capital buffer?

Mr. QUARLES. We have not decided yet whether we would re-propose or proceed in a different administrative procedure fashion.

Mrs. WAGNER. I have asked you this question before along with many of my colleagues, but given that the stress capital buffer will preserve the global systemically important bank's (G–SIB's) surcharge, when does the board plan to update the rule as it explicitly said it would in 2015?

Mr. QUARLES. We are always looking at all of the elements of the current regulatory framework to determine when a particular calibration might be out of whack. We regularly look at the calibration of the G—SIB surcharge, and we are considering it in the context of the overall body of regulation. In particular, as you know, there is the remainder of the international Basel III agreement, the so-called Basel III end game, or the banks sometimes call it Basel IV, that remains to be implemented. I think that we should look at all of this as a package. The implementation of that remainder of Basel III could have the effect of significantly raising the aggregate level of capital in the industry. As both I and Chairman Powell have said, we think that that aggregate level of loss absorbency should remain, and essentially is pretty much proper where it is. And so as we consider that implementation, I think we also then need to consider the overall calibration of—

Mrs. WAGNER. You told us, Vice Chairman—and pardon me for interrupting—but it explicitly said that in 2015, you were going to update the rule. When can we expect this? Given the many post-crisis reforms that have been implemented, is now not the logical time to recalibrate the surcharge to reflect economic growth and reforms?

Mr. QUARLES. I think we should not be considering these issues piecemeal. That is one of the reasons why we are where we are, in my view. We have the opportunity, and, I think, the responsibility to look at the remaining implementation of this Basel III endgame as a package, and we would look at that as a package

with the calibration of other existing elements of the regulatory framework, which would include the G–SIB surcharge. But we should look at that as a package, and that is a project that we are actively underway on.

Mrs. WAGNER. Well, I truly hope that you move expeditiously. The CCAR is up in January of 2020. You have been talking about this for years. Package or piecemeal, we need these rules updated. I thank you, and I yield back.

Chairwoman WATERS. The gentleman from New York, Mr. Meeks, who is also the Chair of our Subcommittee on Consumer Protection and Financial Institutions, is recognized for 5 minutes.

Mr. MEEKS. Thank you, Madam Chairwoman. Ms. McWilliams, I want to pick up briefly where the chairwoman left off, because I am very concerned about recent reports, and I want to find out and be clear, has the FDIC signed on to the OCC-led CRA process and not doing it in an interagency process? Have you signed onto that?

Ms. MCWILLIAMS. The FDIC board meets to vote on any proposals before it, and that meeting has not taken place. So if you ask, have we formally signed on, the board has not voted on this yet, but we are—

Mr. MEEKS. But it is likely that you will do that?

Ms. MCWILLIAMS. It is likely that we will present an opportunity for the board to vote on the improvements to the CRA.

Mr. MEEKS. Just based on the OCC, without the interagency process? So, that means that you agree with, which I don't understand, the OCC's single ratio approach as the right way to go with regards to CRA, even though that risk-breaking and direct link between bank lending and the specific communities that the CRA was intended to benefit? Have you all gone down that path already?

Ms. MCWILLIAMS. No, that is incorrect. There is no single-ratio, single-metric approach. I am not sure where that information was derived from. The draft that I have seen, that we have been working with, does not include a single metric.

Mr. MEEKS. Well, some of this has come from my conversations with the OCC.

Ms. MCWILLIAMS. I would have to defer to the OCC on those conversations.

Mr. MEEKS. But if you are joining on to them, then, therefore, I just want to make sure that you are engaged more. And that is why the interagency process is tremendously important so that it is more than just one idea, multiple ideas, on how we can make sure that are we moving forward with the modernization of CRA so that we are not leaving out the original intent of the CRA that was put forward. So I just would urge the FDIC to re-look at how you are doing this to make sure that you are working with the Fed also so that as we come to a modernized CRA, we make sure that we are not undoing the reason why the CRA was initially implemented.

Let me move on, because I want to ask you another question, Ms. McWilliams, on brokered deposits. As you may know, I am working on legislation now to address what I consider antiquated rules which fail to account for the 30 years of technology innovation and

new organizational structures that we can reasonably agree pose no systemic risk to the banking sector. Which elements do you expect the FDIC to address in its rulemaking, and which ones do you believe Congress needs to address through legislative action?

Ms. MCWILLIAMS. Thank you for that question. If I may just for a second go back to the CRA, I would not sign onto a proposal that in any way undermines the original intent of the law. And the proposal that I could sign onto is a proposal that would actually yield more benefits for the communities that it was intended to protect. So you have my assurance that I would not sign onto anything that does not profess to do so.

On the brokered deposits, like you, I agree that it is an antiquated law. We have not touched the FDIC brokered deposits in about 30 years. I believe there are some things that Congress could do as we are undertaking a review of the existing regulations and the practices in the marketplace and now technology has changed the way consumers do banking, and banks do banking, frankly. I think there is an opportunity for us to work together on improvements. We will try to do what we can on the regulatory side, and to the extent that I have any recommendations to Congress, I would like to take you up on your offer and give you those as well. Thank you.

Mr. MEEKS. Thank you for that. Mr. Quarles, let me ask you quickly, the Fed published information that over half of the supervisory findings issued in the past 5 years were related to governance and risk management control issues. In 2017, I submitted a letter in response to the Fed's request for comments on its proposed guidance of supervisory expectation of board directors advocating for the importance of picking diverse nominees when picking board directors. Now, when I looked at the Fed's guidance, it speaks of diverse experience, but it says nothing about diversity of board members themselves. So to my question to you is, what are you going to do to deal with the urgent issue of making sure that there is diversity in the board members themselves?

Mr. QUARLES. I think that is the intention of referring to diversity of experience, that as a board and as the corporation, as the firm considers the composition of its board, it will look to all the attributes of the board members to ensure that they have that relevant diversity. That is the purpose of that guidance.

Mr. MEEKS. But it just seems to me that the language is clear. It says, "diverse experiences," not talking about the diversity of the board members themselves. So someone could come in and say, well, I have that experience because I worked in it, but they are not diverse individuals. My concern is to make sure that we have diverse individuals on those boards.

Chairwoman WATERS. Thank you. The gentleman from Oklahoma, Mr. Lucas, is recognized for 5 minutes.

Mr. LUCAS. Thank you, Madam Chairwoman. First, I would like to thank all of you for your leadership in promoting transparency and efficiency in supervising and recognizing our financial institutions. This panel has implemented the major provisions in the Economic Growth, Regulatory Relief, and Consumer Protection Act, and I believe the resiliency of our financial system is now greater than ever before.

Vice Chair Quarles, Chair McWilliams, we have discussed at length on various occasions, inter-affiliate margin requirements, and I am pleased to see your agencies have recently proposed to amend these swap margin requirements. Thank you. The recent rule to exempt inter-affiliate swaps from initial margin requirements is an important step forward in identifying which areas can be simplified, harmonized, and streamlined to eliminate inconsistencies and overlap. And I look forward to continuing our discussion as you develop a final rule that will harmonize the treatment of margin requirements. We have also discussed the commercial end user concern with CCAR. Again, I am pleased to see your agencies revise the rule to amend the capital requirements for derivative contracts with commercial end users.

You all know the nature of my district. It is capital-intensive. It is agriculture. It is energy. So, the actions of the Federal Reserve and the FDIC have a tremendous impact back home on my constituents. Now, in light of the CCAR rule, what are the Agencies' plans for moving forward with the implementation of Basel III? How do the Federal Reserve and the FDIC plan to analyze the impact of those revisions across the U.S. framework to ensure coherence and capital neutrality?

Mr. QUARLES. I will start with that one. As I indicated, I do think that there are a few principles that we will need to keep in mind as we consider the implementation of the remainder of Basel III. And those principles are that we will maintain the current level of loss absorbency with the industry. We don't believe that the aggregate level of loss absorbency needs to be increased or that it needs to be decreased, and in order to do that, we should look at this implementation as a package. We should consider how the remaining elements work together, and how they will work together with the already-enacted elements. And while I think that each of them is a useful addition to the overall regulatory framework because of the incentives that they will create for particular actions, we also need to ensure that they are maintaining capital level. I should say that they are essentially capital neutral. I think that we will be able to do that by looking at everything as a whole rather than implementing them piecemeal.

Ms. MCWILLIAMS. If I may add, I do think that with the efforts of Basel, we need to take a holistic and comprehensive look at everything and not address the rulemakings piecemeal, and I agree with Vice Chairman Quarles on that. I also think that the Basel Committee can do a little bit more on analyzing the impact of these rules. There are so-called quantitative impact studies (QISs), that the Basel Committee can do, and something that the U.S. delegation at the Basel Committee has been insisting on for some time.

I can tell you this. When the Basel III rules were promulgated on capital and liquidity, the initial rules, the Basel Committee did do a QIS study, and that study, if I recall correctly—the numbers may evade me, the correct numbers—but it was done based on the balance sheets of banks on December 31, 2009, which was one of the worst times for their balance sheets. And it took into account about 220 financial institutions around the world, only 14 of which were U.S. banks. If I were in this position where I do have representation on the Basel Committee and the working groups, I

would have insisted on a more specific impact at home here in the United States and analysis done by the regulatory agencies on how these rules will impact our banks and not look at 14 out of 228 banks on one of the worst days for their balance sheets in their history.

Mr. LUCAS. In a previous hearing, I raised an issue with Chairman Powell that we have been watching here in the committee for quite some time, and that is the implementation of the Volcker Rule, and I laud the panel for taking on the task of trying to improve the Rule. I suspect my colleagues will raise this issue as well. Chairman Powell indicated at that time that he does not consider long-term investments to be an activity that causes safety and soundness concerns.

Vice Chair Quarles, you know I have a tendency to ask things that are semi-reasonable and rational. So with that—

[laughter]

Yes, that is actually true. Can you commit to us that you will take into consideration how important it is for banks to make these long-term investments while you are working to finalize this portion of the Rule?

Mr. QUARLES. We will definitely take that into consideration.

Mr. LUCAS. See, it was reasonable. I yield back.

[laughter]

Chairwoman WATERS. The gentleman from Missouri, Mr. Clay, who is also the Chair of our Subcommittee on Housing, Community Development, and Insurance, is recognized for 5 minutes.

Mr. CLAY. Thank you, Madam Chairwoman. Last month, the FDIC and the OCC issued a proposed rulemaking to clarify that when a loan is nonusurious when originated by a bank, it remains nonusurious if the loan is sold or signed or otherwise transferred to a non-bank. In 2015, the Second Circuit held in *Madden* v. *Midland Funding* that non-bank debt collectors that had purchased debt originated by a national bank could not benefit from the bank's exportation power. The OCC stated that the proposal was intended to address confusion resulting from the *Madden* decision. Consumer groups and legal experts have raised serious concerns that the proposal will encourage predatory rent-a-bank schemes that are designed to evade State usury caps. Chairman McWilliams, what is the FDIC's intentions with this proposed regulation? Is it intended in any way to administratively override the Second Circuit decision in the *Madden* case?

Ms. MCWILLIAMS. In fact, it is meant to clarify the confusion that has been caused by the *Madden* decision. Since 1828, there has been Supreme Court precedent that if a loan is not usurious at the time when the loan is made, nothing subsequently makes that loan usurious. And in 1865, Congress, this body, gave national banks the ability to adopt those principles. In 1980, Congress gave the FDIC the ability to approve the same principles for State-chartered banks, and everything was going fine, frankly. We have had an existing guidance in place for over 20 years on this issue until the Second Circuit Court of Appeals in *Madden* decided to just ignore the longstanding procedural and case precedent and regulatory precedent in this area.

And we would not have had had to act at all, frankly, if it were not for the decision in *Madden*. Once the decision in *Madden* was made, we felt there was a necessity to re-uphold the longstanding principles we have had, and to reissue our statement that has been in existence for over 20 years.

Mr. CLAY. Okay. So would your proposed regulation effectively rent out these banks' charters to third parties, hoping to evade State usury limits?

Ms. MCWILLIAMS. No. In fact, at the FDIC, and we have stated this explicitly as well as implicitly, we look unfavorably upon such arrangements, and in the cases where there are such arrangements, we will take supervisory action that is appropriate, if any State or Federal laws are being violated.

Mr. CLAY. So you will supervise the third party then, and make sure that there is not an overcharging or—

Ms. MCWILLIAMS. We have a couple of different statutory authorities that allow us to supervise third parties that do business with banks or end up affiliating with banks in any form.

Mr. CLAY. I see. In November of 2019, the FDIC issued a proposal seeking public comment to codify a statement of policy related to Section 19 of the Federal Deposit Insurance Act, which provides criteria for individuals seeking employment in the banking industry with certain minor criminal offenses. In addition, the NCUA board approved a final interpretive ruling and policy statement allowing people convicted of certain minor offenses to return to work in the credit union industry without applying for the board's approval.

Chairman Hood and Chairman McWilliams, what steps can Congress take to give ex-offenders who have minor offenses a second chance, to be able to get a job in the credit union industry? Mr. Hood, first?

Mr. HOOD. First and foremost, this is an issue that I have taken quite seriously since I became Chairman of the NCUA board. I think it is possible for us to sit down and perhaps discuss what happened—I'm sorry, I am fighting a cold.

Mr. CLAY. I am too, but go ahead.

Mr. HOOD. I would love to sit down with your staff and maybe have some of our colleagues to discuss what have been some of the barriers that continue to prevent these individuals from seeking able employment. But we, as a board, are doing our level best to at least create opportunities now for these individuals who have paid their debt to society to get meaningful employment so they can get access to financial inclusion and have upward mobility. But we do look forward to following up with you and your staff.

Mr. CLAY. I look forward to that conversation.

Ms. McWilliams, quickly?

Ms. MCWILLIAMS. Oh, sure, and I will be very quick. Thank you. As I mentioned, from my personal perspective it is a social justice issue that we need to be focused on. I have heard from civil rights groups, from community groups and community activists, and we are soliciting comments on what more we can do. And should we have any recommendations for Congress, I would be more than happy to engage with you.

Mr. CLAY. Thank you. My time is up.

Chairwoman WATERS. The gentleman from Missouri, Mr. Luetkemeyer, is now recognized for 5 minutes.

Mr. LUETKEMEYER. Thank you, Madam Chairwoman. CECL is something the Fed will have to enforce, as you all know, and you and I have spoken with other members as well about this, what I regard as a terrible accounting standard. However, you have remained on the sidelines as FASB has promulgated and eventually implemented this standard. This morning, you have talked a number of times about different new capital rules and how you are going to be implementing them, and looking at them. You made the statement a number of times, I believe, that the average capital that is in the system today, as well as reserves, is at an adequate level.

Now when you implement CECL, there are going to have to be some additional reserves for most banks to be put in place. How do you do the Fed's two-step on trying to make sure that you continue to enhance the ability to be able to increase capital yet not over-reserve, as you indicate this may happen?

Mr. QUARLES. The effect that you describe is one that we are very sensitive towards. There have been a lot of ex ante assessments of the potential size of that effect. That is the reason why the bank regulatory agencies together have said that we would essentially phase in the effect of CECL. So when CECL becomes effective—and it is now effective at different times for different banks—as an accounting standard, we will phase it in, over the course of 3 years, what the effect of that is in the capital regime for the banks. And if we see that there is a large increase in the reserve position of the banks, that is one of the reasons why I have been emphasizing that we think that the total amount of loss absorbency in the system is about right.

I think, then, as part of this overall assessment of the implementation of the remainder of Basel III, of the implementation of CECL, of looking at the effect of the existing framework, in order to ensure that we keep the existing high level of loss absorbency without either lowering it or increasing it, there will be recalibrations of a number of things that may be appropriate and we will look at that as it evolves.

Mr. LUETKEMEYER. Thank you for that answer. I am sure I agree with all that, but we will move on.

Ms. McWilliams, one of the top two issues of CECL and data aggregators is data privacy. When I talk to banks and credit unions, this is their number one and two issues. Data aggregators is something we had a hearing on a couple of weeks ago, and there was a big article in one of the political rags just yesterday or the day before with regards to the hearing that we had. And the concerns that are there with regards to these data aggregators coming in, screen scraping—I have had discussions with one bank, and in fact, it has been verified by a couple of other banks I have talked to since then, that basically 80 percent of the transactions and searches that are done on their computers at night are done by these debt aggregators, screen scraping. And they have actually had to increase the amount of computer power to allow their own customers to access their own accounts, as well as these data aggregators.

Do you see the risk in this, because there have been some huge losses in this already? What do you think you need to do, as a regulator? Or is the industry going to take care of this? Is technology going to take care of this? Where do you think this is going? Does this concern you?

Ms. MCWILLIAMS. It does concern me and, frankly, it concerns me both from a regulatory perspective but also from a private citizen perspective. And having grown up in a system that did not have and afford privacy protections for its citizenry, I am concerned whenever anyone's privacy could be invaded, even inadvertently.

From a regulatory perspective, there are a number of different privacy laws that we can implement. A lot of those privacy protection laws have been shifted to the Consumer Financial Protection Bureau (CFPB) by Title X of Dodd-Frank. In fact, 17 consumer protection statutes were sent over to the CFPB. We have some ability to implement and protect consumers in this space, but a lot of that ability now rests with the CFPB and the Federal Trade Commission (FTC).

Mr. LUETKEMEYER. Chairman Hood, do you have any concerns with that at all?

Mr. HOOD. Oh, I share those same concerns as Ms. McWilliams. These are efforts that we all need to work together on. We certainly work with the CFPB in addressing these issues.

Mr. LUETKEMEYER. Okay. I see my time is about up here. Just maybe a shake of your head would work here. But another issue has come up to me with regards to the credit unions buying out banks, and that is something that is on the radar in both groups, and I am fearful of a war beginning to break out. Are you at all concerned? Mr. Hood and Ms. McWilliams, are you concerned at all?

Mr. HOOD. Sir, these are voluntary, market-based transactions.

Mr. LUETKEMEYER. Ms. McWilliams?

Ms. MCWILLIAMS. About 28 banks have been acquired by credit unions since 2011. There are additional mergers pending. Yes, we are looking at this. The two entities are just not set up in the same way, and Congress did it in a particular reason—

Mr. LUETKEMEYER. Thank you.

Chairwoman WATERS. The gentleman from Georgia, Mr. Scott, is recognized for 5 minutes.

Mr. SCOTT. Thank you very much, Madam Chairwoman. This is an important hearing, but we have a hole right in the middle of it, and that is because Mr. Otting is not here, for whatever reason. But let me just tell you why. We are dealing with this burgeoning industry of fintechs. There is a crying need for us to understand, and I hope, Madam Chairwoman, that we will get Mr. Otting here.

Now, let me tell you why this is a missing hole. As you know, Chairwoman Waters, the OCC has announced this special order for non-bank fintech companies. However, that order has been opposed by State regulators, and also failed to generate any interest from the fintech industry itself. And that has been likely due to a lot of concerns, and I want to get all of your responses on what these concerns are, as much as you can.

There are some real concerns, and Mr. Otting not being here creates a hole in our discussion. Some fintech companies are dis-

appointed in the OCC charter because of its limited purpose nature. It does not allow fintech companies to hold deposits or secure FDIC insurance for deposits. Then, we have legal concerns. The OCC has been engaged in a lawsuit with the New York Department of Financial Services regarding the charter. And in October, the Federal judge sided with New York, against the OCC, and said that the OCC does not even have the authority to issue a charter for non-bank entities in fintech that cannot secure FDIC insurance. Do you see why this is so important? And the OCC says it will appeal. Mr. Otting should be here to give us some answers to this, to speak to this.

I think it is also important, Madam Chairwoman, to find out why he isn't here. Everything that I am saying, he knows. We can't move forward. This is why there is a crying need for the bill we are working on with Ms. Waters, Mr. Lynch, I think Mr. Hill, as we are dealing with the need for you all to harmonize. And here is the main actor not even here at this meeting.

Now I want you, Ms. McWilliams, to respond to some of these concerns. Are you aware that the New York FLSA said that the OCC doesn't even have the authority? Are you aware of the legal ramifications here? Can you imagine if you were a fintech and you have a charter, and there is no harmonization between you, between the Fed, between the CFPB, between the CFTC? We have seen all of these regulators here, biting at the bit to pounce on these fintechs, and regulate them, and the chief regulator, who has put forward an order that has been declared unconstitutional, isn't even here.

Ms. MCWILLIAMS. Thank you for the question on fintechs. I can't speak to OCC's intention or actions but I can tell you this. At the FDIC we are very focused on making sure that there is both harmonization of the rules and a comprehensive look at our regulatory framework.

Fintechs are something that is happening. Financial technology innovation is not new. But the ability of these companies to actually both do business and evolve with technology, and their agility, is something that is very new. So at the FDIC we are looking at this. We are creating an office of innovation to deal exactly with these issues. And I can tell you also that any entity that seeks to collect deposits has to go through our application process for deposit insurance, and no matter what the entity's structure is, they will be subject to the same statutory requirements.

Chairwoman WATERS. The gentleman from Michigan, Mr. Huizinga, is recognized for 5 minutes.

Mr. HUIZENGA. Thank you, Madam Chairwoman, and I am going to quickly move through a number of things.

Chairman Hood, I understand that credit unions purchasing banks—traditional banks, I believe, was the phrase was that you used—is a private-market transaction. I fully understand that. The question is, do you see any problems with that?

Mr. HOOD. Well, sir, these are transactions, again, that are voluntary.

Mr. HUIZENGA. I understand that. Is there a problem with those transactions?

Mr. HOOD. These are transactions that must be approved by both the FDIC and—

Mr. HUIZENGA. So, you see no problem with them. Okay. That is fine if that is your answer. That is fine.

Chair McWilliams, if you could elaborate a little bit on that?

Ms. MCWILLIAMS. I do believe that—and we have data to support this—there is a great consolidation in the community banking sector, and frankly, I am concerned about the communities that are losing banking presence. We have over 120 counties that have a single banking presence in their county, and we have—

Mr. HUIZENGA. I understand.

Ms. MCWILLIAMS. —30 counties. So with respect to the credit unions and community banks, Congress set up credit unions in a certain way. They are not subject to taxation and they also don't have CRA requirements imposed on them.

Mr. HUIZENGA. So I think you are getting to that there might be a problem?

Ms. MCWILLIAMS. I am getting to that the playing field may not be exactly level.

Mr. HUIZENGA. Okay. Fair enough. Chair McWilliams, I want to talk a little bit about industrial loan companies (ILCs). The critics of ILCs claim that banks owned by non-financial companies are unsafe because these parent companies might conduct unsafe transactions with the subsidiary bank. Can you describe the existing statutory and regulatory framework that prevents such transactions?

Ms. MCWILLIAMS. Congress gave us the ability to approve ILC applications based on the same statutory requirements that we approve the deposit insurance applications for banks. So if a bank or an ILC applies for deposit insurance, they have a set of about five or six different statutory requirements which we have interpreted through our regulations over time. We certainly look to the parent. We want to make sure that the parent is profitable. We also have the ability to ask for a capital and liquidity agreement between the parent and the subsidiary, so that the—

Mr. HUIZENGA. Okay. So at the end of the day, you believe that the regulatory structure is there in place, correct?

Ms. MCWILLIAMS. I believe that Congress gave us enough to successfully manage and regulate.

Mr. HUIZENGA. Well, I will just note that in 2007, former FDIC Chair Sheila Bair had testified exactly to that, in that they may actually contribute significantly to community reinvestment. So, I would assume you believe that still applies today?

Ms. MCWILLIAMS. I don't know exactly the full statement she said, but in general—

Mr. HUIZENGA. She just said that they proved to be strong, responsible parts of the nation's banking system and offered innovative approaches to banking.

Ms. MCWILLIAMS. I would agree with that.

Mr. HUIZENGA. Okay. Chair McWilliams and Vice Chair Quarles, your respective agencies study consumer financial welfare, and your data has shown that nearly half of Americans cannot afford a $400 emergency that could creep up into their lives, and they simply don't have the cash to deal with that. For many of these

folks, including many in my district who are not prime borrowers, this source of a small-dollar credit line is a lifeline on those small-dollar loans. And based on your experience and research, what do you believe would be the impact of a national 36 percent APR cap on the access to this type of credit for these consumers? Mr. Quarles?

Mr. QUARLES. We haven't studied, in fact, what we think that the quantitative impact on that would be.

Mr. HUIZENGA. Okay.

Ms. MCWILLIAMS. I believe that wherever Congress were to set that cap, there would be a significant portion of small-dollar borrowers who would be excluded from the ability to get access to credit.

Mr. HUIZENGA. You certainly have been looking at the validity of loan terms, I am assuming. It is my understanding that you are tackling serious systemic issues on safety and soundness. Is that true?

Ms. MCWILLIAMS. Yes. I will take a holistic look at the underwriting standards to understand how they impact safety and soundness and consumer protection.

Mr. HUIZENGA. And what does that mean for the greater marketplace for those types of loans?

Ms. MCWILLIAMS. For small-dollar loans, in particular, there is definitely a need.

Mr. HUIZENGA. Okay.

Ms. MCWILLIAMS. And that need has been identified by, I believe, about 40 percent, if I recall that—

Mr. HUIZENGA. And how does the *Madden* decision figure into that?

Ms. MCWILLIAMS. The *Madden* decision, frankly, disrupts the over a century-long precedent that we have had, that allows—Congress made it legal to allow banks to originate loans. And basically, what *Madden* disrupted was the ability of a bank to sell the loan and the ability of the purchaser to assume the interest rate under which that loan was sold. Frankly, it is a disruption in the secondary market which affects safety and soundness.

Mr. HUIZENGA. Thank you.

Chairwoman WATERS. Thank you. The gentleman from Illinois, Mr. Foster, is recognized for 5 minutes.

Mr. FOSTER. Thank you, Madam Chairwoman, and thank you to our witnesses here.

Prior to the last crisis, one of the fundamental mismodeled risks was that the bond ratings produced by the rating agencies were just flat-out wrong. And U.S. corporate debt has now swelled to nearly $10 trillion, which is almost 50 percent of GDP, and is well in excess of any previous record, and well in excess of where it was pre-crisis. Experts from the IMF to asset manager Blackrock to the Fed have recently warned that the risk posed by ballooning allegedly investment-grade debt may pose to our economy.

According to the IMF report on financial stability this year, it was the weakest firms that accounted for most of the growth and are increasingly using debt for financial risk-taking, such as investor payouts that lever up the company, M&A activity, rather than capital improvements such as plant and equipment. And they are

doing this, apparently, in response to both interest rate and tax policy.

The problem is, of course, exacerbated by the fact that the bond ratings remain fundamentally suspect due to Congress and everyone's failure to deal with the fundamental conflict of interest in the issuer-pays model for bond ratings.

So, Vice Chairman Quarles and Chairman McWilliams, would you agree with this assessment of the increasingly risky nature of corporate debt that has emerged over the last year?

Mr. QUARLES. I think that is a complex question. Corporate debt has been growing. The debt service burden has not been growing, because of the low level of interest rates. The structures in which the riskiest debts are held are generally not runnable structures, by which I mean—

Mr. FOSTER. Could you elaborate on that?

Mr. QUARLES. Yes. By which I mean that the terms of the—a lot of this leverage lending is being sold into collateralized loan obligation vehicles, and the holders of those vehicles, the maturity of their obligations, their exposure, is longer than the maturity of the exposure inside of the institution, and therefore it is difficult for them to run from the institute, from a precipitous change in the value of the underlying assets.

So what does all of that mean? I look at that as saying there is much less of a financial stability risk of this, but I do think that there is a possibility that there could be a decline in value of these assets, and that could exacerbate some future business downturns.

Mr. FOSTER. Yes. So how do you model, in your stress testing, the potential detonation of this $10 trillion unexploded bomb?

Mr. QUARLES. Our models take into account the expected losses of different classes of assets. We do take the credit quality of these assets into account.

Mr. FOSTER. Do you model the possibility that there are just fundamental errors in the bond ratings?

Mr. QUARLES. Our model does not rely entirely on the bond ratings in determining the losses that are expected here, and certainly not for the loans as opposed to the bonds that are part of this phenomenon.

But I do think that there are supervisory actions that we can take, and that the agencies together have taken through the Shared National Credit Program to address this issue. We have looked at leveraged lending in each of the last two Shared National Credit examinations. It has been a particular focus. And where we have seen origination practices that we don't think are consistent with safety and soundness, we have taken supervisory action against those as part of that process.

Mr. FOSTER. Chairman McWilliams?

Ms. MCWILLIAMS. As Vice Chairman Quarles said, it is a very complicated issue. We have engaged in this so-called Shared National Credit, or SNC, review every Q1 and Q3 of each year. Our teams get together and do a review and we publish the findings in January, so there should be a forthcoming review of the Shared National Credit portfolios of the banks.

The $10 trillion that you mentioned, not all of that is leveraged. That is corporate debt, in general. According to our estimates, less

than a quarter of that is so-called leveraged. One of the issues that we are running into is that there is no common definition of leveraged loan, and so, we—

Mr. FOSTER. It is sort of similar to what became toxic assets, where there wasn't a clear definition of what was what there.

Ms. MCWILLIAMS. I would say there is some distinction there. And I know this is important to you. It is important to us as well. I have instructed our examiners and supervisory folks to go back and take a look at, what are these banks claiming as leveraged lending? So when you look at the $10 trillion number, some of these definitions for leveraged lending are 20 to 25 pages long. And some include indirect exposure and some include only direct exposure. So we are trying to get to a best place where we understand what is being held directly by banks, which we know, versus what is being held indirectly outside of the banks.

Mr. FOSTER. Thank you. I yield back.

Chairwoman WATERS. The gentleman from Ohio, Mr. Stivers, is recognized for 5 minutes.

Mr. STIVERS. Thank you, Madam Chairwoman. I want to thank you for holding this hearing. It is an important hearing and I, like you, look forward to speaking with the Comptroller when he does come before the committee, because I think it is an important regulator. But I appreciate the three of you being here.

My first couple of questions are for Vice Chair Quarles. You recently had a conference in Abu Dhabi and the International Association of Insurance Supervisors (IAIS), and Treasury, and sort of Team USA was there. Treasury put out a statement afterwards saying they couldn't support the IAIS proposal on Version 2.0 because they didn't feel like U.S. insurers should face pressure to participate in a reference insurance capital standard (ICS) that is not expected to apply to the United States and doesn't fit our markets. They also thought that this current ICS could risk limiting U.S. consumers' access to important long-term savings products.

Do you agree with the statements that the Treasury put out?

Mr. QUARLES. I think that Treasury articulated serious issues, and I agree that those are issues. As you know, the—

Mr. STIVERS. And is Team USA together with one strategy and goal at these meetings? That is the intention of the question here.

Mr. QUARLES. Yes, I mean, I think that—

Mr. STIVERS. There we go.

Mr. QUARLES. —the Team USA, the three elements of it—the National Association of Insurance Commissioners, the Fed, and the Treasury—continue to work to the same objective. As you are aware, in Abu Dhabi the NAIC sort of took the lead in negotiating a compromise. As with any compromise, there are issues around it. I think that Treasury was correct in highlighting those issues. The Fed believes that it was, however, a compromise that allows us to continue to achieve U.S. objectives in the ongoing IAIS process, and so we are supportive of it.

Mr. STIVERS. It at least moves the ball forward, but I think we need to keep our eye on the ball and make sure that we are all looking out for the American consumer and American companies being competitive internationally. So I appreciate that, Governor.

Mr. QUARLES. Yes. I completely agree with that.

Mr. STIVERS. Great. The other thing I want to talk about is the aggregation method and buildings blocks approach that you are working on. The Fed is developing a building blocks approach for a number of insurers that are supervised by the Federal Reserve Board, and it is significant in an international context, given that the first proposal included a realization that the aggregation method is being considered by the IAIS.

And I am just curious, and I hope you will consider it, because this is a pretty complicated thing. I believe the Federal Reserve has gotten letters from the U.S. Chamber of Commerce, the American Property Casualty Association (APCIA), the American Council of Life Insurers (ACLI), the National Association of Mutual Insurance Companies (NAMIC), and the Insurance Coalition, asking you to extend your December 23rd comment period deadline, because these are very complicated proposals that affect a lot of people in a lot of different ways.

And so, this is not a question so much as a statement. I genuinely hope that you will consider their request to extend the comment period, because these are very important outcomes and very complicated matters.

Mr. QUARLES. Thank you, and we will—

Mr. STIVERS. And I am not going to put you on the spot to ask you whether you will or won't, because you might say no and I don't want you to say no. I want you to consider it.

Mr. QUARLES. We will consider it.

Mr. STIVERS. Great. And I want to follow up on something my colleague from Missouri, Mr. Luetkemeyer, talked about, the CECL rule. And I think his next grandson is going to be named Cecil, because he talks about it so much.

But Governor Quarles, will the Fed consider giving institutions credit for their CECL reserves in overall capital standards as we move forward? That seems to be the way we can make a change that allows what could be excessive reserves to be normalized and still end up with the right amount of capital and not deny these institutions the ability to lend and grow our economy.

Mr. QUARLES. Yes. While we haven't made any sort of decision until we see exactly how CECL operates in the real world as opposed to through modeling, I think that is something that has to be on the table.

Mr. STIVERS. Great. And really quick, down the line, should we have a consolidated approach, an interagency review of CRA to make sure it works for all institutions? I know it doesn't apply to credit unions today, but frankly, a lot of big credit unions, I think, do need it. So, I'm going to ask you to comment anyway.

Mr. HOOD. The credit unions' mission is based on the premise of people helping people. They are serving people of low to moderate incomes already through the products that they are offering, through their activities in the community, by way of investments. So I would say that credit unions do not need government fiats if you encourage them to do the right thing.

Mr. STIVERS. I will follow up in writing. Thanks, Madam Chairwoman.

Chairwoman WATERS. Thank you. The gentleman from Missouri, Mr. Cleaver, who is also the Chair of our Subcommittee on Na-

tional Security, International Development and Monetary Policy, is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Madam Chairwoman. Mr. Quarles, let me make sure that I get a good understanding. A lot of us, primarily our leader, were instrumental in getting Dodd-Frank approved, and there were provisions in Dodd-Frank that gave the responsibility to the Fed to implement a number of our provisions, the provisions of Dodd-Frank, including the mandate to preserve and promote MDIs.

The numbers are ugly: 66 MDIs have been lost since 2008. We had 215 in 2008 compared to 149 in—I should have provided this before we started. But this is a chart that deals with MDIs, and it is not a pretty chart.

I am interested in you or someone explaining to me, how did you handle the mandate to preserve, and maybe even more importantly, promote MDIs?

Mr. QUARLES. Thank you for that. We have taken that responsibility very seriously. We have established what we call the Partnership for Progress (PFP) throughout the Federal Reserve System, which is a national outreach effort using the resources of the Fed to help minority depository institutions know how to address the unique challenges of their business model. That PFP program, as we call it, is very active in all of the reserve banks. And we have the resources behind it in order to help majority institutions throughout the country.

Mr. CLEAVER. So you are saying you have promoted and continued to push for a reversal of the trend—

Mr. QUARLES. Yes, absolutely.

Mr. CLEAVER. So I am interested, if you did, why has it failed? You would agree that—I will give you the shortest. It is very ugly. So it means that something has not worked. If you are putting forth an effort and we go from 215 in 2008, to 149, we are hustling backward.

Mr. QUARLES. The challenges that face minority institutions and community banks, in general.

Chairwoman WATERS. The gentleman will suspend.

Mr. Cleaver, I want to put your chart up, that you are referring to, so everybody can see it. So just hold on for a minute and we will get it up. I want to make sure that it is available to both sides and to everybody.

Mr. CLEAVER. I apologize. I didn't know I was going to go there, until I listened to him.

Mr. QUARLES. May I talk for a bit while the chart is going up?

Chairwoman WATERS. The gentleman will suspend.

[pause]

Chairwoman WATERS. Please go right ahead.

Mr. CLEAVER. Thank you, Madam Chairwoman. You can see this FDIC-insured minority depository insurance, and then if you look down you can clearly see, as time moves on, things get worse. And hopefully, you can take this with you when you leave.

But my question is, if that is correct, and I am 100 percent certain that it is, who is working on this?

Mr. QUARLES. I believe that it is correct, and we are concerned about that trend.

Mr. CLEAVER. No. I don't like to interrupt people, but you are saying you are concerned. I am, too.

Mr. QUARLES. But we are regularly engaged with these minority depository institutions. In addition to the Partnership for Progress, where we provide them technical assistance, we have other sorts of technical assistance programs. We have a regular minority depository institution leaders' forum that we host at the Fed. The interagency process has a separate minority depository institution technical assistance program that we provide, conferences that we provide for them.

Mr. CLEAVER. Okay. Thank you. Anybody else?

Ms. MCWILLIAMS. I would like to, if you don't mind, just add something. Section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) gave us the responsibility to protect and preserve the minority depository institutions and we take that mandate very seriously.

We have done a number of things at the FDIC to strengthen the ability of the MDIs to survive. I, like you, am actually, frankly, very concerned about the disappearing landscape of American minority depository institutions, and, in particular, of the African-American depository institutions. One of the things that I asked our staff to do is to analyze exactly what is the impact of our regulations, and do we understand how these MDIs can be helped.

This is the bottom line. A lot of them need capital infusion, and frankly, I think there is an opportunity to address that in the CRA. And that is why I would just ask you to be open-minded to the changes we can make in the CRA to benefit the MDIs.

Chairwoman WATERS. The gentleman's time has expired. The gentleman from Kentucky, Mr. Barr, is recognized for 5 minutes.

Mr. BARR. Thank you, Madam Chairwoman. To the witnesses, as you know, Kentuckians have a deep history and interest in the production, cultivation, and sale of industrial hemp. That dates back to Speaker Henry Clay. The hemp industry in the commonwealth is booming. However, despite the legalization of industrial hemp in the 2018 Farm Bill, hemp farmers and producers and hemp-related businesses have had trouble accessing financial services.

As you may know, I authored an amendment on this issue that was included in the Safe Banking Act, which the House passed in September. My amendment would require your regulatory agencies to issue guidance confirming that industrial hemp and hemp-derived products are legal and that banks don't need to file suspicious activity reports solely because a transaction relates to hemp.

I want to thank you and your agencies, along with FinCEN for issuing that very guidance—I believe it was issued yesterday—along those lines that will help the hemp industry in my district gain access to financial services.

Chairman McWilliams and Vice Chairman Quarles, your agencies issued that guidance that clarifies the legality of industrial hemp and states that banks are no longer required to file suspicious activity reports simply because their customers are engaged with hemp growth or production. I have heard from Kentucky bankers about this. They welcome this guidance, and it will go a long way toward helping the hemp industry to thrive.

Chair McWilliams, what plans do you have in place to train your examiners about how they should supervise institutions in light of hemp's legality and your guidance?

Ms. MCWILLIAMS. We do thank you for that question, and I think that the guidance that we issued was crucial in making sure that there is at least some form of a roadmap for banks engaged in banking hemp-related businesses.

We have done training with our examiners, and we will continue to do extensive training with our examiners to understand exactly how to look at these filings and to make sure that they understand that the suspicious activity report filings are not required for hemp-related transactions.

Mr. BARR. Thank you. And Chairman Hood, thank you for being first in line on this with your August 19th interim guidance on credit unions serving hemp businesses. What is your timeline for releasing updated guidance?

Mr. HOOD. We are continuing now, sir, to work with the industry to provide training to our examiners. We are also working with the State supervisory authorities to engage them in the process as well. We will now be working with the USDA and other related parties to ensure that we get it right. We will be hosting a series of roundtables to glean insight from entities, particularly insight around best practices. So, we are moving forward.

Mr. BARR. Thank you. Thank you to all of you on this. One of the specific financial services which has been either unreliable or unavailable is card processing services. Does your guidance from yesterday clarify for card processing businesses that they can freely serve customers of hemp-related, and specifically CBD retailers, without any legal risk or liability?

Ms. MCWILLIAMS. I don't have the guidance in front of me but we can circle back. I don't recall.

Mr. BARR. I have read the guidance closely, as you can tell, and I didn't see that in there, and that is the financial service that has really been unreliable and spotty. And so if you need to update that guidance to give more legal clarity to card processing businesses, I think that might be in order. Do you have a response to that?

Ms. MCWILLIAMS. We will certainly take a look and make sure that we communicate to our regulated entities to see what is working and what is not, vis-a-vis our guidance. And to the extent that we need to do additional explaining, we are more than happy to engage in that process.

Mr. BARR. I will just tell you that congressional intent is not only that the regulators confirm the legality of industrial hemp and hemp-related retailers under the Farm Bill, but that those retailers and merchants can use card processing services to sell the product itself, and that has been the financial services issue for the most part. So I would ask all of you if you need to revisit the guidance to do so, to make sure that hemp-related businesses, legal under Federal law, can offer those card processing services.

Ms. MCWILLIAMS. We will, and we will certainly make sure that we implement congressional intent as intended.

Mr. BARR. Great. Thanks. Let me move on really quickly. Vice Chairman Quarles, would you describe the criteria you use to evaluate non-G–SIB firms for inclusion in the Large Institution Su-

pervision Coordinating Committee portfolio, the LISCC portfolio? Would you describe the criteria?

Mr. QUARLES. The issue with that question is that actually the criteria are under active review, so we are in the middle of developing a more concrete and transparent—

Mr. BARR. I would encourage a clear offramp that firms may elect to exit the LISCC portfolio.

Finally, on leveraged lending, Vice Chair Quarles, do CLOs provide liquidity in stress market environments as long-term, market-to-market investors, and how might an overreaction to leveraged lending undermine financial stability?

Mr. QUARLES. I am not sure. I will follow up with you.

Mr. BARR. Thank you. I yield back.

Chairwoman WATERS. The gentlewoman from Ohio, Mrs. Beatty, who is also the Chair of our Subcommittee on Diversity and Inclusion, is recognized for 5 minutes.

Mrs. BEATTY. Thank you so much, Madam Chairwoman, and I thank the ranking member and our witnesses. Thank you for being here. I have a few questions I am going to try to get through in my time period, but first, after being in the anteroom and hearing part of the testimony and questioning from Congressman Cleaver, I would like to share with the witnesses that Congressman Meeks and I both have a bill that deals with MDIs. Since it was brought to my attention that you could not answer the questions about the MDIs, would you be willing to send me a briefing page on your analysis or whatever you have, and maybe our staffs can work together. Is that a problem for anyone?

Ms. MCWILLIAMS. Our staffs can always work together, and we would be happy to engage.

Mrs. BEATTY. All right. Thank you.

Mr. HOOD. Congresswoman, I just wanted to share that our credit union data was not reflected in the chart. We at NCUA are working with roughly 500 minority depositories. We continue to marshal resources to ensure their viability, so they can serve communities in need.

Mrs. BEATTY. Thank you so much, Mr. Hood, for that, and we will see if when you all get together, you can certainly incorporate that data.

We have heard a lot about the role I play as Chair of the Diversity and Inclusion Subcommittee, and it is very important to me for a whole host of reasons, because I think it goes far beyond Dodd-Frank and Section 342. I am very appreciative that you have Office of Minority and Women Inclusion (OMWI) Directors. But I think it goes over into other things, whether that is MDIs, whether that is looking at what happens on November the 19th, with the FDIC, when you voted unanimously to issue a proposed rule to codify longstanding guidance that allows applicants with minor criminal records to work in banking.

And Ms. McWilliams, this question is going to be for you. While I understand clearly the intent of the law, but it is a lifetime ban for any criminal offense regarding dishonesty, breach of trust. It seems to me that it goes far too far and captures too many other minor offenses.

I was just at a meeting this morning when someone shared with me that in college, their child's roommate had a fake ID, and the consequences ended up being more than just a slap on the wrist. And so as we talk about moving forward, let me just be really direct: I really have a problem with the decision and what you just did.

So, Ms. McWilliams, can you explain why the FDIC made the decision to move forward with this rulemaking? And let me remind you, it was a rulemaking from 1950.

Ms. MCWILLIAMS. I believe we have a common problem, and I am not in disagreement with you. What we tried to do on Section 19 in the proposal we issued was basically to update, as you mentioned, some of the archaic standards that Congress put in place for the inability of persons who committed minor infractions and have paid their debt to society and redeemed themselves to be able to re-enter the workforce at banks.

I am in complete agreement with you that we can do more, and our November initiative was exactly aimed at that, and the initiative received a unanimous vote of the FDIC board. So, I am not sure exactly where we are in disagreement.

Mrs. BEATTY. Okay. We will take a look at that.

Can you tell me, Mr. Quarles, what is the topic of today's hearing?

Mr. QUARLES. Oversight of the bank regulatory agencies.

Mrs. BEATTY. Everybody else had other words in there. It's like safety and diversity. It was a long title. And so, let me just make an observation. When I look at Mr. Hood's testimony and what was sent out to all of us, it does say that it is the oversight, but it says ensuring safety, soundness, diversity, and accountability. And both of your colleagues took great pains to write about diversity and inclusion, and to share that.

So if I were doing just a mock little study, and I would say we have an African American, and we have a female, and we have a majority, I find it quite interesting that the female and the minority talked about diversity and inclusion as it related to soundness and as it related to regulations, and nowhere in your written testimony did it say anything—anything—about diversity, at all. But yet you had some very interesting statements when you said financial regulation, like any other policy, is a product of our history.

And so, I am going to use that and say back to you, I think diversity, or lack of it, is a product of our history. I yield back.

Chairwoman WATERS. Thank you. The gentleman from Colorado, Mr. Tipton, is recognized for 5 minutes.

Mr. TIPTON. Thank you, Madam Chairwoman, and I appreciate the panel taking the time to be here today. I did want to follow up a little on my colleague, Mr. Luetkemeyer's, questions in regard to CECL. There was a recent CSVS survey of 571 banks that found that only 60 percent of the banks think that they have adequate internal controls to be able to handle CECL; 22 percent think that they will need to obtain more, and 18 percent do not know.

Vice Chair Quarles, I guess one of the concerns that I have is, some of the banks, 60 percent, think that they are going to be able to handle it, but is the ultimate outcome in terms of a downturn in the economy, the ability to be able to make loans to consumers

maybe when they need it the most? Is that part of the equation being included in some formulation for CECL?

Mr. QUARLES. As you know, there is a limit to what we can do with the accounting standard, because we don't create the accounting standard. But as we look at what the potential effect will be, and as we monitor the implementation of the accounting standard during this 3-year phase-in that we have established, we obviously would be looking at all of the effects that it has on the industry and on individual institutions.

Mr. TIPTON. One thing, just really to encourage—I come from a rural area, and oftentimes, it is hard for businesses to get access to capital to operate. Some of the impacts that this could ultimately have on some of our regional banks, in particular, they play a very critical role, is something that I hope you will give a lot of consideration to.

And I did want to also be able to return to some of the CRA. I appreciate the comments my colleague, Mr. Meeks, made. But Chair McWilliams, we didn't really get to hear from you, some of the goals of the CRA modernization that you would like to see if you do, in fact, join with the OCC in putting forward those proposals.

Ms. MCWILLIAMS. Thank you for the opportunity to clarify that. From my personal perspective, the CRA reform—frankly, the regulators have not touched the CRA regulations since 1995. The way the banks do business has changed tremendously since that time. We have more banks engaged in digital offerings and yet the definition of the assessment area is decades old.

And so the goal that I have, personally, is to modernize the provisions to address some of the digital lending channels, to figure out how can we do more to encourage long-term investments and not just have banks look at a 3-year cycle as they look to make these investments. I believe if they have a long-term view, they will have a bigger impact on their communities.

I think there is a whole lot more we can do for rural areas, for small family farms. There is more we can do for small businesses, minority depository institutions, as I discussed. There is certainty that we can provide in the marketplace that, frankly, is now lacking. We do not want to have, at least from my perspective, an exercise in Community Reinvestment Act compliance where the banks just get the numbers and check the box and they are done. We want to have meaningful impact on the ground in the communities that they serve.

Mr. TIPTON. I appreciate that, and I really encourage broadband development in rural America as probably one of the more important issues that we need to have.

Vice Chair Quarles, could you explain some of the reservations that you might have in joining the FDIC and the OCC in regards to CRA modernization?

Mr. QUARLES. I think it is important to stress that we have been working jointly with the OCC and with the FDIC on CRA modernization, and that there is a shared view among all of the regulatory agencies, among community groups, among banks, among everyone who is affected by this regulation, that the regulation can

be improved, that the implementation of the statutory requirement is not as well-served as it could be by existing practice.

And I wouldn't get too wrapped around the axle myself, around the agencies potentially moving at different speeds. The OCC came out with its advance notice of proposed rulemaking (ANPR) by itself a while ago, without the FDIC or the Fed. The Fed had a broad outreach in all of the reserve banks in order to get input. The OCC chose to do it through an ANPR. We had a different mechanism. The FDIC had its own mechanism. And then, we all took that input and worked together to reach an endpoint.

We are only at the point of whether a notice of proposed rulemaking will go out. We are not at the point of a final rule, and the objective ought to be that at the end, all three agencies will join in a final rule, and we have our independent processes for how we will get there. So, I think it is premature to say that we are parting ways.

Mr. TIPTON. I yield back. Thank you.

Chairwoman WATERS. Thank you. The gentlewoman from Michigan, Ms. Tlaib, is recognized for 5 minutes.

Ms. TLAIB. Thank you, Madam Chairwoman. I appreciate all of you being here. I want to talk a little bit about rent-a-bank schemes. Banks are generally exempted, as you all know, when they offer credit from State rate caps that cover payday lenders and other online lenders. For many years, these payday lenders and others have attempted to take advantage of this exception by entering into rent-a-bank schemes, where they launder their loans through banks and then purchase those loans back, but continue to charge the higher rates that would be illegal under current State laws in those places.

Chairwoman McWilliams, you had expressed your desire to see responsible lending take place inside banks. You have also said the agency frowns upon arrangements between banks and non-bank lenders for the sole purpose of evading State law. However, the proposed rule, if I may submit it for the record, Chairwoman—

Chairwoman WATERS. Without objection, it is so ordered.

Ms. TLAIB. Thank you. The proposed rule says the complete opposite. You allow the exemption to continue under these proposed rules from the OCC.

As we speak right now, FinWise Bank, in Utah, is facilitating essentially a shadow banking scheme right now in Michigan, where they—so the OppLoans, or whatever they call them, make predatory lending 160 percent APR, but in Michigan, we pass laws that basically say the rate installment loan should be at 37 percent.

I am just curious, Chairwoman McWilliams, isn't the OppLoans' rent-a-bank scheme's sole purpose to evade State law?

Ms. MCWILLIAMS. I can't speak for a specific bank or a specific product. I can tell you that—and I hope that you have the IDIC proposal in front of you—the only thing we are trying to do in that proposal, and we did, was basically seek information on almost 200 years of case law, extending to the Supreme Court—

Ms. TLAIB. But isn't the sole purpose evading State law?

Ms. MCWILLIAMS. We did not touch on the issue that you are discussing, which is the—

Ms. TLAIB. Why? You said that you wanted to focus on making sure that we have responsible lending.

Ms. MCWILLIAMS. I don't—

Ms. TLAIB. My district is the third-poorest congressional district. We are literally front-line communities for these payday lenders. And we advocated, on the local level, within the legislature for 6 years. We said we have to push back because it is increasing the cycle of poverty, right? And we are asking for us to know that when we see a scheme like this that is targeting communities that we are supposed to be protecting, that we are issuing proposed rules that basically protect it, and to stop these schemes.

I know these are not folks on the street. These are bankers. But these are so-called folks from the business sector and corporations, but they should be treated the same way as any criminal on the street would when they are trying to push something that is obviously laundering money through a rent-a-bank scheme. Correct?

Ms. MCWILLIAMS. There has been a lot of confusion about what we did and what we didn't do, and I believe you are talking about the doctrine of so-called true lender, which our proposal did not touch. Our proposal, the only thing it did—if you have the proposal in front of you, you will see the only thing it did is, in fact, address our longstanding principles that Congress gave us the authority to do in 1980, which is to say that when a loan is made and the interest rates are not usurious at a time when the loan is made, no subsequent event makes those loans usurious, basically preserving the sanctity of a contract to ensure that there is a secondary market for the sale of these loans.

States do have an opportunity to opt out of that regime. Congress, you, gave them that authority in Section 27 of the FDIA Act as well. And, frankly, we frown upon and we look disfavorably upon the schemes that you are talking about.

Ms. TLAIB. But why aren't we addressing that in the proposed rule?

Ms. MCWILLIAMS. Do you have our rule in front of you?

Ms. TLAIB. Yes. No. It actually still does not allow—it allows them to evade the State laws. It allows them to—

Ms. MCWILLIAMS. That is incorrect.

Ms. TLAIB. So right now, you are telling me these rent-a-bank schemes are illegal?

Ms. MCWILLIAMS. The rent-a-bank schemes, what you are referring to as rent-a-bank, is not a regulatory term.

Ms. TLAIB. I know. What do you call it?

Ms. MCWILLIAMS. Those schemes and arrangements are provided under the so-called true lender doctrine, which we didn't touch. It is up to States to decide what rate caps are appropriate, if any, and whether or not the States want to opt out of the ability of the interest rates to be preserved when an out-of-State entity purchases that loan product.

Ms. TLAIB. I think we need to shut down these schemes. We can call them whatever we want. My folks call them rent-a-bank schemes. We need to shut them down. State laws out there, across the country, are preventing this form of predatory lending, and we, as the government, are not preventing it from actually happening. We are not creating the safeguards that are available.

So, Chairwoman, before I end, I would like to submit some articles from the Center for Responsible Lending, as well as the National Consumer Law Center, that are talking about where around the country these schemes continue to target people that we all represent. Thank you.

Chairwoman WATERS. Without objection, it is so ordered.

Ms. MCWILLIAMS. We are certainly not in favor of predatory lending.

Chairwoman WATERS. The gentleman from Texas, Mr. Williams, is recognized for 5 minutes.

Mr. WILLIAMS. Thank you, Madam Chairwoman, and I thank all of you for coming today. With last week being Thanksgiving, I spent some time thinking about how blessed we are to live in the greatest country in the world. We are a nation of opportunity and incentive, and because of those principles, we are a nation of hope where everyone can benefit.

At its core, it is capitalism and the free market that helps make this country so great. So it is a system that rewards innovation because it maintains demand for the best products at the best price. I am a car dealer, and I can tell you we have really good prices right now out there, so you need to know that.

With that in mind, though, capitalism is the greatest force in the history of our world for lifting people out of poverty, and I pray that we will instill this virtue in future generations.

Chairwoman McWilliams, back in May, when I asked you if you were a capitalist or a socialist, you mentioned that you grew up in communism, spent time in socialism, and now choose capitalism. So, I would assume nothing has changed in your decision since May?

Ms. MCWILLIAMS. Nothing has changed in my decision since May. Correct.

Mr. WILLIAMS. So given your unique life experience with these economic systems, can you quickly elaborate on the beauty of capitalism?

Ms. MCWILLIAMS. I don't think that 5 minutes, or 3 minutes and 38 seconds of your time is going to allow me an opportunity to speak on my appreciation of this system, but I can tell you that I am teaching my daughter about the privilege of being born in the United States and the benefits bestowed upon anyone who has that privilege. I can tell you that as I was growing up, my father had to give up a small piece of farm land in order for me to qualify for a free school lunch, which was then revoked about 6 months later. And having the ability to protect private property ownership rights and the ability to live in a free and prosperous economic society that preserves the rights of the individual is something that I think is the greatest blessing in my life.

Mr. WILLIAMS. Well said. Thank you.

Vice Chairman Quarles, my colleague, Mr. Stivers, touched on this earlier about the meeting in Abu Dhabi, and I think that maybe we could talk about that a little bit more. I understand that the IAIS agreed to enter a monitoring period for its global insurance capital standard but did not formally implement the ICS due to ongoing concerns raised by the Department of the Treasury.

While last month's meeting seems to be a step in the right direction, I still have some concerns, considering our State-based regulatory system that has been effective for the last 150 years. We must do all we can to ensure that whatever international standards are agreed to, it will not put the U.S. insurance companies at a competitive disadvantage.

So I have two questions for you, Vice Chairman. First, will you commit to staying engaged on this topic moving forward? And second, do you feel as if the results of the meeting in Abu Dhabi give us the ability to create our own domestic standard for insurance regulations?

Mr. QUARLES. I will definitely remain engaged on this going forward, both through my work at the Federal Reserve and as Chairman of the Financial Stability Board, of which the IAIS is a member. Did the agreement in Abu Dhabi give us the ability to continue to pursue American interests in this process? I think that it did. As I indicated earlier, it was a compromise. It was a compromise that was negotiated by the National Association of Insurance Commissioners. By definition, no compromise gives every side everything that it would want, but I think that it gave us enough, the United States enough to continue to ensure that the international process takes account of our system.

Mr. WILLIAMS. Chairwoman McWilliams, in an op-ed you wrote for the American Banker in October, you stated the following: "If our regulatory framework is unable to evolve with technological advances, the United States may cease to be a place where ideas and concepts become the products and services that improve people's lives."

I completely agree with you, with your statement. I think that one area that would be especially beneficial to update would be the broker deposit rules and regulations. As you know, these rules haven't been updated in over 30 years, and are so overly broad that they capture a wide variety of new companies that have been working to get more people to the traditional financial system.

I know you have been working diligently on this issue and can't comment on specifics, possibly, but I hope we will see something soon out of the FDIC on broker deposits. So, Chairwoman, other than the broker deposit rule, what has the FDIC been doing in the fintech space to work innovation in the banking system and modernize supervision?

Ms. MCWILLIAMS. Thank you for that question. Yes, I think this is one of the underappreciated areas in the regulatory world, because innovation seems to be happening and quite often it seems to be happening outside of the regulated entities. We want that innovation to happen inside the regulated entities, and I will submit for the record some of the initiatives we have undertaken.

Mr. WILLIAMS. Thank you very much. I yield back.

Chairwoman WATERS. The gentlewoman from Massachusetts, Ms. Pressley, is recognized for 5 minutes.

Ms. PRESSLEY. Thank you, Madam Chairwoman, for ensuring that oversight continues to be a priority for this committee. We have a government structure to work one way for banks and businesses and another for consumers and working families. That is why I pushed the Federal Reserve to provide everyday consumers

with the same settlement services it already provides for banks. Working families shouldn't have to wait 3 to 5 days for a check to clear.

Now, Mr. Quarles, you were the lone dissenter in the Federal Reserve's decision to develop FedNow, which was heralded by small businesses and consumer groups alike. I do believe how one chooses to spend their time reflects what they value, and, more importantly, whom they value.

Mr. Quarles, over the weekend the New York Times published a profile on your regulatory approach, and notably, you have chosen to spend your time in this role—in your first 21 months in office, you met with Goldman Sachs 24 times, you met with JPMorgan 19 times, you met with Morgan Stanley 17 times, and with Citi 12 times. In that same timeframe, how many consumer groups did you meet with?

Mr. QUARLES. Over the course of my first 21 months in office, I met with approximately, at a conservative estimate, 15,000 to 20,000 people. The great majority of those—you have noted that 26 of those were Goldman Sachs out of 15,000 to 20,000 people. That is, again, at a conservative estimate, 14/100ths of 1 percent of my time was spent with that and the other 99.86 percent of my time was spent with others.

Ms. PRESSLEY. Okay. Consumers? Because again, who you spend your time with speaks to whom you value.

Mr. QUARLES. Yes.

Ms. PRESSLEY. And the fact that you were the lone dissenting voice about whether or not to expedite payments of hardworking Americans, so that they can get what they have worked for in a 3- to 5-day period, something banks already have, I think is indicative of something else.

Mr. QUARLES. But, ma'am, I dissented because I believed that the proposal would harm those consumers.

Ms. PRESSLEY. Reclaiming my time. Again, you were the lone dissenter on that, and I asked, did you engage consumer groups, and you didn't indicate any.

The Federal Reserve was notably missing from the recently issued notice of proposed rulemaking on the Community Reinvestment Act. A strong CRA is a top priority for civil rights groups and many members of this committee. Mr. Quarles, how many civil rights groups did you meet with in those first 21 months? Can you just name a few, specifically?

Mr. QUARLES. I met with many.

Ms. PRESSLEY. NAACP? ACLU?

Mr. QUARLES. I don't remember the names of them. I met with many of them and I will happy to provide that information.

Ms. PRESSLEY. I would like to see that list, but I am incredulous that you cannot immediately cite civil rights organizations, knowing what a priority a strong CRA is to these groups, and that you can't immediately detail or enumerate that you have met with any of them. So, I look forward to that list.

When Chairman Powell was before us, I called on the Fed to better reflect the interests of hardworking American people, a sentiment I echo to all regulators, including those who could not make it here today. However, when large banks have a greater access to

the Federal Reserve's leadership than even sitting Members of Congress, we have a problem.

I want to be clear. My colleagues and I are paying very close attention. Wherever gaps in oversight exist, we fill them. Hundreds of thousands of hourly employees doing the everyday business of banking—opening checking accounts, originating loans, detecting fraud and money laundering—all while complying with regulations.

However, we have seen how extractive sales quotas and performance metrics can result in disaster for low-level employees. The Wells Fargo scandal is a prime example of this.

So Ms. McWilliams, yes or no, do you track banks' employment practices and metrics?

Ms. MCWILLIAMS. When you say employment practices, can you elaborate?

Ms. PRESSLEY. Well, some that I already cited. I spoke about just the everyday business and practices of banking—opening checking accounts, originating loans, detecting fraud and money laundering—and again, these extractive sales quotas and these performance metrics, according to those practices, can result in disaster for low-level employees.

Ms. MCWILLIAMS. I don't disagree with you that certain bank culture can certainly create problems for both the employees and their customers. In terms of tracking performance, we do have supervisory tools to which we look at the number of accounts opened, we look at how banks are conducting the business of banking. We make sure that they comply with the consumer protection laws and statutes.

Ms. PRESSLEY. Thank you. I'm sorry. I am running out of time.

Mr. Quarles, do you track banks' employment practices and metrics?

Mr. QUARLES. We do.

Ms. PRESSLEY. Okay. And in the wake of that scandal, thousands of front-line workers lost their jobs, while only a handful of more senior-level employees faced similar consequences, and that is why, with the support of the AFL-CIO and the Communication Workers—I'm sorry. That is my time? Okay. Thank you, Madam Chairwoman.

Chairwoman WATERS. Thank you. The gentleman from Arkansas, Mr. Hill, is recognized for 5 minutes.

Mr. HILL. Thank you, Madam Chairwoman. Thanks for providing us the opportunity to have oversight over the bank regulatory system. I want to thank each of you for appearing today. Thanks for spending time with us. And congratulations for the hard work over the last few months to implement S.2155 across the agencies. You met together. You had your checklists. You got that work done and reported that to Congress in a timely way, and all of us and our constituents. Thank you for that attention.

Mr. Quarles, I wanted to follow up on a discussion that we have had on and off over the last few weeks and talk briefly about bank supervision by the Federal Reserve as it relates to the September 16th, September 17th disruption in the repurchase market. I know that is being studied by the Fed in earnest, led by the New York bank, and I appreciated that.

But when you see the amount of reserves held by the banks, they are extensive. They are far above any requirement of the Dodd-Frank rules. There is very little chance of a foot fault in those reserves that I think particularly the big banks hold. In fact, looking at the numbers, the four largest banks, collectively, have more cash at the Fed than the next 24 combined. So, there seems to be a lot of cash held at the Fed.

How does the Fed make clear to banks that inter-day lending is a good thing, in other words, that banks have access to those cash amounts that are far in excess of what they need regulatorily?

Mr. QUARLES. I think there are a variety of measures that we can take. We are actively looking at what will be effective. We do want to ensure that our supervisory, both the regulatory system and our supervisory practices are not creating undue incentives for the hoarding of central bank reserves by some institutions. Part of that is simply communication, ensuring that our supervisors are communicating clearly about what Fed expectations are. Some of it can be taking measures to ensure that banks are comfortable, that they will have access to immediate liquidity from other forms of—if they are holding other forms of liquid assets other than central bank reserves, and all of that is under active consideration.

Mr. HILL. Certainly, before the financial crisis, having a daylight overdraft at the Fed was considered a routine business activity. Would you agree with that?

Mr. QUARLES. Absolutely.

Mr. HILL. Has there been much to speak of in the ways of daylight overdrafts by the banking industry since the crisis?

Mr. QUARLES. Very little.

Mr. HILL. Would you say there is a stigma that has been attached to having a daylight overdraft during an inter-day process?

Mr. QUARLES. I think that is inarguable. We hear that from the industry.

Mr. HILL. That issue is curious to me, when I think Mr. Dimon at JPMorgan Chase just reported something like $60 billion in cash was required that he keep that at the Fed but his cash balance was like $120 billion, for example, on a daily basis. That seems like a lot of room to participate in that market if there was an economic incentive to do so. So assuming there is an economic incentive to have a rising repo rate, I am just curious why that stigma is so pronounced?

Mr. QUARLES. Among the consequences of the increased transparency after Dodd-Frank has been a decreasing willingness of institutions to take advantage of some of the credit provisions from the Federal Reserve and that has contributed, although I do want to emphasize that we don't think that it is the driving factor, but that it has contributed to some of—

Mr. HILL. Right. I have heard G–SIB surcharges might contribute to it, and others. But do you think Section 1103 of Dodd-Frank that requires the Fed to publicly disclose that banks borrowed at the discount window should be reconsidered?

Mr. QUARLES. I wouldn't go so far—I haven't concluded that it should be—well, it depends on the definition of "reconsidered."

Mr. HILL. Should we repeal it?

Mr. QUARLES. I certainly haven't concluded that it should be repealed, but we should be aware of the full range of its consequences.

Mr. HILL. Thank you. I want to touch on a couple of other things. Chairman Luetkemeyer talked about screen scraping. I would like each of you to answer this question: Do you support the use of APIs by financial institutions that you regulate exclusively for access to consumer data by data aggregators that aren't part of the bank. Mr. Quarles?

Mr. QUARLES. We do support the increased use of APIs as a more secure way of dealing with—

Mr. HILL. Would you require it, do you think, in the future, subject to a rulemaking and a process and all that?

Mr. QUARLES. We should give consideration to that. We haven't concluded we should require it.

Mr. HILL. Chair McWilliams?

Ms. MCWILLIAMS. I am generally in agreement, yes.

Mr. HILL. Mr. Hood?

Mr. HOOD. I am in general agreement, but I would have to study it for its impact on our smaller institutions.

Mr. HILL. Thank you, Madam Chairwoman. I yield back.

Chairwoman WATERS. Thank you. The gentlewoman from New York, Ms. Ocasio-Cortez, is recognized for 5 minutes.

Ms. OCASIO-CORTEZ. Thank you, Madam Chairwoman, and thank you to all of our witnesses who have come here today to testify and share your testimony.

I am here today, and my job here is to represent working people, and my district is quite working class. Many of my constituents are waitresses, they are teachers, they are nurses, and I am here today to get to the bottom of a problem that our taxi cab drivers have been facing.

As some of you may be aware, the New York City taxi medallion crisis has driven many owner-drivers, targeted by predatory loans, to financial ruin and suicide. Some of my colleagues and I have called on the City to forgive the debt of these drivers, and that has been met with resistance. But while you are here before the committee, Mr. Hood, I would like to discuss the role the NCUA played in the crisis and its ability to potentially provide relief as we explore solutions.

Mr. Hood, you are the primary regulator for all federally-insured credit unions. Correct?

Mr. HOOD. Yes, ma'am.

Ms. OCASIO-CORTEZ. And as such you would have been the primary regulator for Melrose Credit Union, LOMTO Federal Credit Union, Bay Ridge Federal Credit Union, which all failed because of a significant concentration of loans collateralized by taxi medallions and safe and unsound lending practices. Correct?

Mr. HOOD. The credit unions that you mentioned, they had pretty much an 80-year history of providing prudential mortgages to the taxi medallion industry. So, they have been doing it for 80 years, quite successfully.

Ms. OCASIO-CORTEZ. Yes. But they did fail because that concentration became untenable for them.

Mr. HOOD. It was a combination of concentration risk, but again, those were performing well. It was the introduction of the ride-sharing applications that really upended that traditional business model.

Ms. OCASIO-CORTEZ. I think there is an issue there, because the inspector general at your organization conducted a material loss review, and they found that the examiners repeatedly noted that these credit unions were engaged, and began to be engaged in unsafe lending practices, including failure of the credit unions to fully analyze borrower financial information, insufficient detail in credit memoranda, risky loan terms. Some of these drivers were making $30,000 a year and were given a million-dollar loan.

Do you agree with the characterization of the IG's report, Mr. Hood?

Mr. HOOD. I certainly support the IG report in the sense that we are taking some of those actions to date now.

Ms. OCASIO-CORTEZ. Great.

Mr. HOOD. We are issuing information around guidance on concentration risk. But I would like to note, ma'am, that also, one of the first things I have done in the 7 months of being at NCUA was to make sure that we have a senior leader whose sole responsibility is to look for borrower solutions for the individuals who have these loans. We are looking to provide them with restructurings, reduction in interest rates—

Ms. OCASIO-CORTEZ. Great.

Mr. HOOD. —all of the things it is going to take to make them whole. And I would also like to note, my heart goes out to them, and I empathize with the families who have been impacted. With me, when I looked at the taxi medallion situation, I know that behind every taxi medallion loan is a family who has been impacted.

Ms. OCASIO-CORTEZ. Yes. And you are aware that the examiners were sounding the alarm about this industry in 2012, 2013, and 2014, for 3 consecutive years, correct?

Mr. HOOD. I am aware of it because I am now at the agency, but those were activities that had already taken place, and again, most of the institutions that you have recognized, those have all been conserved. Those have all been merged into other entities. First and foremost, the individuals who were credit union members, their accounts will remain safe and sound. So, they never once lost their insured deposits.

Ms. OCASIO-CORTEZ. And I greatly appreciate the actions that have been taken to prevent some of these crises in the future. My concerns now are with those who have been impacted by these predatory loans. Do you believe the NCUA bears any responsibility for the findings in the inspector general's report?

Mr. HOOD. I think it was important that the IG did note some things that we can do to further enhance our supervision efforts, not just with this one particular asset class. But, in general, we are going to be looking at producing general supervision, or guidance, coming up in the next few months, I would say, around just concentration risk in general. The thing is, there were so many other folks in the ecosystem involved with originating these loans.

Ms. OCASIO-CORTEZ. Right.

Mr. HOOD. As you reference in your remarks, the taxi commission, you had State-chartered entities that were also making their originations.

Ms. OCASIO-CORTEZ. Thank you. And I am sorry.

Mr. HOOD. Of course.

Ms. OCASIO-CORTEZ. I just wanted to reclaim my time for the purpose of questioning. And as you said, there is a broad ecosystem. I am trying to figure out what we can do here, in this slice of it. Entities are currently selling the loans off to debt collectors at a discounted rate, yet owner-drivers are still on the hook for the original amounts. So, in other words, many of these predatory loans are being sold off for, say, $150,000 to a debt collector, but still holding the owner-driver to about a $600,000 debt for the loan.

Can I have your commitment before this committee that the NCUA will do everything in its power to ensure that any benefits extended to lenders could also be extended to owner-drivers in the form of principal reduction?

Mr. HOOD. We are looking at individual tailored solutions to address the matter at hand. It is not a one-size-fits-all approach. What I have instructed our staff to do is to work with those individual borrowers. To the degree that they are providing us with information, ma'am, we are able to reduce their interest rates. We are able to provide them with loan restructuring, so that they—

Ms. OCASIO-CORTEZ. And what about principal reduction, specifically?

Mr. HOOD. My statutory requirement is to protect the National Credit Union Share Insurance Fund for the safety and soundness of the overall system. We are now working within the means that we have to date to support providing solutions—

Ms. OCASIO-CORTEZ. Would you consider principal reduction?

Mr. HOOD. That is something that would be difficult to do in managing my statutory requirements to the National Credit Union Share Insurance Fund, but I am open to look at other activities to provide borrower relief by way of loan restructurings and interest rate reductions. I do want to work with these individuals.

Ms. OCASIO-CORTEZ. Okay. Thank you. We will be following up.

Mr. HOOD. Yes, and thank you for your recent letter.

Ms. OCASIO-CORTEZ. Of course. Thank you.

Chairwoman WATERS. The gentleman from Georgia, Mr. Loudermilk, is recognized for 5 minutes.

Mr. LOUDERMILK. Thank you, Madam Chairwoman. Thank you all for being here today. I have three questions so I am going to try to get through them in my limited time here.

First, Vice Chairman Quarles, I want to talk about LISCC. I trust you received the letter I led with 24 members of the committee regarding LISCC and the lack of clear, transparent criteria for designating firms. As you know, the GAO determined that three pieces of LISCC guidance are actually rules and must follow the rulemaking process. And so my question is, what is the Fed going to do to follow the required process and ensure that LISCC is transparent?

Mr. QUARLES. We are in the process right now of considering refinements, revisions to the LISCC designation process that will

make it more concrete, more rules-based, and more transparent, and we will be shortly working on those.

Mr. LOUDERMILK. So your intention is to follow the rulemaking process in that?

Mr. QUARLES. I don't know that it would go through sort of the Administrative Procedure Act (APA) rule process, but when we have completed re-looking, and re-thinking about how we can make it again more concrete and constrained and transparent, at that point then we will consider if it is—even if it is not an APA rule, it could be a Congressional Review Act rule, that we would send up.

Mr. LOUDERMILK. That was really a concern, is if it does go under the CRA, we want to make sure that it is transparent, that we are engaged and involved.

Mr. QUARLES. Absolutely.

Mr. LOUDERMILK. So we will be following up with you on that. And thank you for that.

Chairman McWilliams, I want to talk about the valid-when-made issue a little further. I know that has been brought up already. Since the *Madden* court decision in 2015, it has really created a fragmented interpretation of banking laws and regulations—valid-when-made has been in play for a century and has brought stability.

Ranking Member McHenry and I sent a letter to you that was signed by all of the Republicans on this committee, to you and Comptroller Otting in September, asking if you would provide clarity on the issue which will help keep credit accessible and affordable. Some have made the argument, as you have heard, that this rulemaking will allow non-bank lenders to evade State interest rate laws. Can you explain how that is not the case?

Ms. MCWILLIAMS. It is not the case, and I will have to correct you, that the original case was an 1820 Supreme Court case.

Mr. LOUDERMILK. Okay.

Ms. MCWILLIAMS. So it is a little bit more than a century, almost 2 centuries.

The only thing we did in our rulemaking, frankly, was take the guidance we have had, based on the laws that Congress gave us in 1980, to ensure that there is clarity, especially in the secondary market, which we view as important for the ability of banks to maintain safe and sound standards as they look to sell the loans. That is all we did. We did not change the existing status quo on the authorities Congress gave us in 1980.

Mr. LOUDERMILK. So based on what you are doing, you can say that this rulemaking will not allow for non-bank lenders to evade existing State laws?

Ms. MCWILLIAMS. That is correct. The issue that the Congresswoman from Michigan mentioned is something that we did not touch on in our rulemaking. In fact, we specifically said the only even close reference that is we look unfavorably and we will consider it unfavorably in our supervisory approach if banks engage in the practices that basically are deemed as predatory.

Mr. LOUDERMILK. Okay. And I appreciate that because I think this is something that definitely needs to be done. It does affect the

lending especially between the fintech industry and banks, and I appreciate the direction that you are taking on it.

One last question for you, and it is regarding technology and especially artificial intelligence. As the new ranking member on the Artificial Intelligence Task Force, I sent you a letter recently about the planning, that you are planning to issue guidance regarding the bank's use of artificial intelligence, I think it is really important that as we develop the guidelines for banks regarding artificial intelligence, that the efforts are coordinated among regulators. And so, will you make every effort, really, to everybody up here, to work together to make sure that whatever regulatory guidelines that we put out there for the banking institutions regarding artificial intelligence are coordinated, so we don't have disparity between the different regulators?

Ms. MCWILLIAMS. Yes.

Mr. HOOD. Yes.

Mr. LOUDERMILK. Thank you. Mr. Quarles?

Mr. QUARLES. Absolutely.

Mr. LOUDERMILK. Thank you. I yield back.

Chairwoman WATERS. The gentlewoman from Virginia, Ms. Wexton, is recognized for 5 minutes.

Ms. WEXTON. Thank you, Madam Chairwoman, and thank you to the witnesses for joining us here today. I would like to talk about something that impacts every American, and especially my constituents in the 10th Congressional District of Virginia, and that is government shutdowns. The last shutdown that we had lasted for 35 days. It was only a partial shutdown but it still cost the economy billions of dollars, 800,000 Federal employees went without pay, tens of thousands of contractors were laid off, and unlike Federal workers, they did not receive any back pay for their lost hours of work.

During this time, a lot of banks and financial institutions stepped up and offered to help folks who were affected by the shutdown. They offered things like flexible payment options, no-interest loans, and this was really important to especially people who work in the national security area, because financial difficulties can impact their security clearance and then that jeopardizes their livelihood.

It was great to see so many lenders take these proactive steps, but there were still issues and confusion at some financial institutions and regulatory guidance from your agencies was very slow to come. In fact, it wasn't until the 20th day of the shutdown that joint guidance was released, encouraging banks to work with borrowers who were affected by the shutdown and let them know that such efforts would not be subject to regulatory criticisms.

During the shutdown that we had in 2013, it wasn't until the 9th day that guidance was issued. So this is not an isolated problem and, believe me, I don't ever want to assume that shutdowns are the new normal, but we, right now, are operating under a Continuing Resolution that is only good through December 20th. And I introduced a bill, the Shutdown Guidance for Financial Institutions Act, which passed the House of Representatives, that would basically automate the process and require that financial regulators get that guidance out within 24 hours of a shutdown.

Like hundreds of other wonderful bills that we have passed in the House of Representatives, it is sitting over in the Senate. It obviously won't become law in time for the December 20th deadline that we are facing.

So what I am seeking from each of you is an assurance to not just me and the members of this committee, but to Federal workers, contractors, and the financial institutions who are looking for this guidance, that there will be a timely issuance of guidance if we are not able to keep the government open come December 20th. So can I get that assurance from each of you? Mr. Hood?

Mr. HOOD. The credit unions were not involved in that particular guidance. I am pleased to report that our credit unions were making emergency loans and providing financial services without any regulatory guidance. They were doing it under their own volition, because they wanted to help their members have access to financial services during the shutdown.

Ms. WEXTON. And you will make sure that continues in the unlikely event it becomes necessary again?

Mr. HOOD. They have done it with or without my imprimatur, but, yes, I will certainly encourage them to continue serving the needs of their member owners. But again, to date, they were doing it without any prompting from our agency.

Ms. WEXTON. Good.

Mr. QUARLES. Thanks for highlighting the issue. We should be able to move much faster.

Ms. MCWILLIAMS. As a fellow Virginian, and somebody who has spent a decade in public service, prior to this job, dependent on those Federal Government checks to make my mortgage payments, I actually want to thank you personally for your effort in this area. We took too long last time, and it shouldn't repeat.

Ms. WEXTON. Very good. Thank you very much, and I will yield back with that.

Chairwoman WATERS. Thank you. The gentleman from Ohio, Mr. Davidson, is recognized for 5 minutes.

Mr. DAVIDSON. Thank you, Madam Chairwoman. I thank our witnesses for your expertise and the service you are trying to render to keep our banks and our markets sound. And as we look at the hearing prior, one of my colleagues highlighted the Fed's faster payment program, and Mr. Quarles, your "no" vote, as you said earlier you felt that it could harm consumers, I would like to allow you a brief response.

Mr. QUARLES. I think there are questions about the speed with which a faster payment system can be implemented in the United States and what measures will ultimately be effective in doing that. At the end of the day, those arguments weren't persuasive to my colleagues on the board. There, I do think that one of the factors that was very reasonable for them to take into account is that the Federal Reserve, with respect to the payment system, generally does not have regulatory authority, unlike most central banks in what we would consider most of our peer central banks.

So in the absence of direct regulatory authority over the payment system in order to address some of the concerns that were being raised by consumer groups, it was felt that the only way to really do that was through standing up a direct Federal Reserve offering.

I didn't think that was the most effective way, but I do think it highlights that weakness in our regulatory framework that other than doing this we don't have a way of trying to ensure that some of these concerns are addressed.

Mr. DAVIDSON. Thank you for your explanation. Frankly, I had hoped that you would talk about the Fed's previous commitment that the private sector would take care of that, and frankly, having invested substantial capital in that space, now the Fed essentially wants to borrow that intellectual property for their own use. And I thought it was highly inappropriate, frankly, for the Fed to decide to move in on what they had already signaled to the market they would not move in on.

And as you look at it, I hope that the Fed will continue to look at ways to tokenize the dollar, digitize the dollar, because that payment could be very swift, and could make use of the underlying blockchain technology that is going to transform central banking around the world, and hopefully doesn't leave out the United States. And certainly, it is easier to implement than some of these things.

Now, it does eliminate some intermediaries, which I understand some of those intermediaries might like to make a lot of money on the transaction, fees or carry trade or what have you.

But that highlights one of the other things where liquidity is just not happening the right way. Some of my colleagues have already looked at the repo market, and I just am particularly curious about the moral hazard of essentially the Fed interjecting $100 billion or so a day, at times, into the repo market. Do you see a moral hazard in that?

Mr. QUARLES. It is an interesting question. I don't think actually that there is a moral hazard there. Given the operating framework for monetary policy that we have described, and have said that we will be following going forward, we have to ensure that there is an ample level of reserves. We always expected that as the level of reserves shrank, at some point we would know when we got there because we would see a price response in the market. We hadn't expected that it would be so dramatic.

Mr. DAVIDSON. How would the price response happen correctly if the Fed intervenes? And so you are preventing the market from functioning, in a way, because of Fed intervention. And when you look at the purpose of the hearing, I think nothing highlights better the fact that we might not have a regulatory framework dialed in correctly for financial institutions than the fact that our repo market is in chaos right now, and the only way to bridge that gap is to essentially print money. Although we are not calling it quantitative easing, and it has maybe a different intent, how does it have a different effect?

Mr. QUARLES. I think it has a different effect because of the nature of the intervention. We are only trying to ensure that we get to that level of reserves that ensures that our administrative right, in fact, is the price of money as opposed to the—

Mr. DAVIDSON. But rather than putting money into the system, why wouldn't you look at the regulatory framework that created the problem in the first place? And as we close in on the end of

the year, many people are anticipating another surge in demand for liquidity. Is the Fed expecting that?

Mr. QUARLES. I do think that we need to look at the regulatory framework. I don't think that it is the only contributor, probably not even the driving contributor to what has happened. But we do need to look at it.

Mr. DAVIDSON. Thank you. My time has expired.

Chairwoman WATERS. Thank you. The gentlewoman from North Carolina, Ms. Adams, is recognized for 5 minutes.

Ms. ADAMS. Thank you, Madam Chairwoman, and thank you to all of the witnesses for being here today. My first question is to you, Chairman Hood. In October of 2018, NCUA amended its 2015 risk-based capital rule to delay the effective date until January 1, 2020, and raise the asset threshold from $100 million to $500 million in assets. In June of 2019, the NCUA again delayed the effective date to January 1, 2022.

At this point, the proposed risk-based capital standards have been postponed multiple times. So does the NCUA have a timeline for finalizing the standards within the next 2 years?

Mr. HOOD. Yes, ma'am. NCUA, first and foremost, the credit union system to date has a very strong net worth of over 11.39 percent. Because of that reason, ma'am, the recent NCUA board made the decision to delay implementation so the new members—two-thirds of our board all started in April of this year. So with that being said, we are studying solutions and we are looking to provide a holistic approach to injecting capital into the credit union system.

Were the aggregate net worth to date not at 11.39 percent, we would not have the comfort in taking this necessary time to study. But we do have the risk-based capital rule that is already in effect today. In fact, we have a rule that is not identical to that of the FDIC, but is comparable. So there is a risk-based capital structure in place, and when credit unions fall below the statutory cap of 7 percent, we take enforcement and corrective action.

Ms. ADAMS. Okay. So we don't really need to be concerned about the capitalization within the credit unions?

Mr. HOOD. I would say that we are well-capitalized. We will continue to look for innovative and adding new tools to buttress its capital adequacy. But right now it is hovering over 11.39 percent, 400 basis points, so 4 percent above the statutory requirement. So we have time to pursue innovative options, and I hope to present them to you when I next testify.

Ms. ADAMS. Okay. Thank you, sir.

Vice Chair Quarles, in S.2155, the Fed was directed to undertake a formal study to determine if banks with less than $250 billion in assets are not systemic. Is the Fed still planning to conduct this study, and if you are not, then why not?

Mr. QUARLES. The reason I was looking back at my colleagues there was that I wasn't aware that there was a study requirement, and they have confirmed for me that we did not believe there was a study requirement. We are always looking at the systemic situation of the industry as a whole, but I don't think that the law required us to conduct a study.

Ms. ADAMS. Okay. That is a fake question, I guess. So let me ask you, in terms of the loophole, in 2016, the Fed issued a report call-

ing for the ILC loophole to be eliminated, that generally exempts ILCs from the Bank Holding Company Act. So does the Federal Reserve still support that recommendation?

Mr. QUARLES. We have not had cause to address that. We have not changed our official position on that.

Ms. ADAMS. Okay. Let me move on to the CRA. I think all of us can agree that it has served as an important tool in helping meet the credit needs of our underserved communities and populations. This question is for everyone. Briefly, can you speak to how we can better align financial profit incentives and the CRA incentives to ensure that more low- to moderate-income borrowers, small businesses, and entrepreneurs can have access to affordable, prudent loan options?

So if each of you can quickly—

Mr. HOOD. Credit unions aren't governed by CRA, but I support all financial institutions serving people of modest means.

Ms. ADAMS. Chair McWilliams?

Ms. MCWILLIAMS. I believe we can reform the CRA to get exactly to the point you are addressing, and that is the effort I am trying to engage in to make sure that there is a greater impact on the communities that the CRA was supposed to and intended to affect.

Ms. ADAMS. Thank you. Sir?

Mr. QUARLES. Yes, absolutely. I share those sentiments. We can do more and we can do it efficiently.

Ms. ADAMS. Thank you all for your testimony and your responses. Madam Chairwoman, I yield back.

Chairwoman WATERS. Thank you. The gentleman from North Carolina, Mr. Budd, is recognized for 5 minutes.

Mr. BUDD. Thank you, Madam Chairwoman. Chairman Hood, it's great to see another North Carolinian in the room.

Mr. HOOD. Thank you.

Mr. BUDD. Vice Chair Quarles, welcome. One topic that I and others continue to be concerned about is the proper calibration of the overall capital framework. I have asked you and Chairman Powell several times about plans to update the G–SIB surcharge, given that the Fed said it would do so in the final rule in 2015. So we hope to see some progress on that in the very near future so that the U.S. can continue to level the international playing field.

Chairman McWilliams, thank you to you as well for being here. I want to briefly echo the comments made earlier by my friend, Mr. Tipton from Colorado, and add my support to the FDIC to utilize its upcoming broker deposit rulemaking to make some long-overdue changes in updating how it interprets that area of the law, in particular, if the deposits are coming from an affiliate of the bank.

And Vice Chair Quarles, back to you, regarding the topic of insurance, last July I sent you a letter following a dialogue that we had at a hearing very similar to this, where I asked a number of questions about the Fed's activities at the International Association of Insurance Supervisors, including for evidence from a solvency standpoint to prove it is necessary to construct a new capital requirement for U.S. insurers.

In your response, you said that the Fed remains committed to engaged dialogue and pursuits of outcomes on international standards that are appropriate for U.S. insurers and their policyholders.

Last month, representatives from the U.S., specifically the Department of the Treasury, the Fed, and the National Association of Insurance Commissioners, attended a meeting of the International Association of Insurance Supervisors (IAIS) in Abu Dhabi, and during the meeting, the IAIS agreed to enter a monitoring period for its global insurance capital standards, but did not formally adopt implementation.

Significantly, Treasury registered their official opposition to the deal, and making it clear that the ICS, in its current form, still does not work with the U.S. State-based system of insurance regulation that has served American consumers for nearly 2 centuries, while the Fed did not register any official opposition at the same time.

The Treasury position was heard loud and clear on the global stage. There is much more work to be done in my legislation to ensure any international deal must recognize our system will play an important role in this process.

Vice Chair Quarles, as you indicated in your response to my letter last year, the one in July, going forward, is the Fed committed to opposing any international proposal such as the ICS that does not work with the State-based system of regulation and the policyholders that it serves?

Mr. QUARLES. Yes, we continue to believe that the international process has to work for the U.S. It can't be successful if it doesn't. As you know, the IAIS doesn't have any ability to impose its decisions on the United States, so it really, if it doesn't work for the U.S., it won't be implemented here, and so it really can't be effective.

Mr. BUDD. Just to be clear, so that I don't have any lack of clarity leaving here, you do continue to oppose, in ICS, anything that doesn't serve the State-based system of regulation?

Mr. QUARLES. Yes. We believe that the international standard has to accommodate the U.S. system.

Mr. BUDD. Thank you very much. Madam Chairwoman, I yield back.

Chairwoman WATERS. Thank you. The gentleman from Illinois, Mr. Garcia, is recognized for 5 minutes.

Mr. GARCIA OF ILLINOIS. Thank you, Madam Chairwoman. And thank you to all the panelists for being here today.

I want to address my first questions to the Federal Reserve and the FDIC. Both the Federal Reserve and the FDIC approved the merger between BB&T and SunTrust on November 19th, but the Fed simultaneously issued a consent order against SunTrust for unfair and deceptive practices. SunTrust repaid $8.8 million in fees that they had charged customers for those misleading practices, but the practice of misleading consumers was not exactly out of character for either bank. SunTrust and BB&T ranked 3rd and 12th, respectively, in the most banking-related consumer complaints last year.

Did the Fed and the FDIC investigate those complaints in the process of reviewing the merger proposal?

Ms. MCWILLIAMS. Are you referring to the—I'm sorry, which customer database? I want to make sure I understand your question correctly.

Mr. GARCIA OF ILLINOIS. Did you investigate those practices when they came forward with their merger proposal?

Ms. MCWILLIAMS. We looked at it generally. We are a primary regulator for BB&T, at the FDIC, and we have extensively—

Mr. GARCIA OF ILLINOIS. Did you investigate those things?

Ms. MCWILLIAMS. If you can just repeat, what's the database or the survey? I don't want to—

Mr. GARCIA OF ILLINOIS. I didn't mention a database. I mentioned banking-related consumer complaints against those two entities.

Ms. MCWILLIAMS. To the extent that we get consumer complaints about our regulated entities, including BB&T, we do investigate.

Mr. GARCIA OF ILLINOIS. So you did investigate those? Is that within the purview of what you do?

Ms. MCWILLIAMS. I would assume we did, because without a list and understanding, did these complaints come through the BB&T—

Mr. GARCIA OF ILLINOIS. Governor Quarles?

Mr. QUARLES. Yes. We certainly took into account consumer complaints and looked into them. We have to take the convenience and needs of the—

Mr. GARCIA OF ILLINOIS. So, that is a yes? Okay. I think that poor consumer compliance records of banks seeking to merge should be a factor in whether big banks are allowed to get bigger. I don't want to reward bad behavior. If the Fed and the FDIC are going to scrutinize the consumer protection implications of mergers, I think that the CFPB should be given a formal say in the bank merger review process. That is why I announced today that I am introducing the Bank Merger Review Modernization Act, which strengthens the process for reviewing bank mergers and gives consumers a voice in whether they are approved.

Governor Quarles, is it fair to say, in that your experience with bank mergers is quite extensive—a 1997 article in the International Financial Law Review described your work at Davis Polk as follows, "He advises domestic and foreign banks and bank holding companies on a broad variety of matters, including mergers and acquisitions. He has been active in advising bank holding companies and security firms in proposed business combinations, including the merger of Morgan Stanley with Dean Witter, Discover JPMorgan's investment in the American Century mutual fund company, and Bank of America's purchase of Robertson Stevens." You also worked on Deutsche Bank's acquisition of Bankers Trust and JPMorgan's merger with Chase Manhattan.

This past weekend, the New York Times, as I think was mentioned previously, did a profile of you, and noted that you have met 22 times with lawyers from your former employer, Davis Polk, since October of 2017. Is it possible for you to be a neutral arbiter when it comes to big bank mergers?

Mr. QUARLES. Well, as you note, you were quoting from something from 1997, which is almost a quarter of a century ago. It has been 20 years since I had anything to do with Davis Polk. I do

think that I have a lot of expertise in the area, but I have no particular—

Mr. GARCIA OF ILLINOIS. Do you feel that you are a neutral arbiter?

Mr. QUARLES. Absolutely.

Mr. GARCIA OF ILLINOIS. Have prospective bank mergers been a topic of discussion during any of your meetings with Davis Polk?

Mr. QUARLES. Prospective bank mergers. I can't think of any, but if there were, it would be confidential supervisory information (CSI). So, maybe it's confidential supervisory information for me to say that I can't think of any, but I can't think of any.

Mr. GARCIA OF ILLINOIS. Thank you. My time is about up, so I yield back, Madam Chairwoman.

Chairwoman WATERS. Thank you. The gentleman from Ohio, Mr. Gonzalez, is recognized for 5 minutes.

Mr. GONZALEZ OF OHIO. Thank you, Madam Chairwoman, for holding this important hearing, and thank you to our panel for your contributions and your service.

I want to start with Vice Chairman Quarles and Chairman McWilliams. I sent both the Federal Reserve and the FDIC a letter this week about the importance of establishing a regulatory framework that promotes investment opportunities in startups and small businesses. I know the Volcker regulators are considering revisions to the covered funds portion of the Volcker Rule, and I just want to encourage you, as part of that process, to allow banks to sponsor or invest in long-term and/or venture capital funds that I believe are an important source of funding for companies seeking to grow.

As someone who previously ran a startup in Silicon Valley, which is awash with private capital, I think it is important for companies that need capital but aren't located in capital-rich centers like that, especially States like mine and regions like mine, in northeast Ohio, I want them to have as many opportunities as humanly possible, and I think that vision is shared.

And so I guess my first question to both of you would be, as you are looking through this, how do you think about the covered fund definition and the ability for banks to be able to provide this?

Mr. QUARLES. We are looking at ways to try to ensure that we effect the purposes of the statute, but in a way that allows the greatest amount of financing for the real economy, as is consistent with the purposes of the statute. I think there are amendments that we can make that will do that. They are under active discussion currently, and we will propose them and get a lot of comments on them, so I don't want to prejudge where that is going. But the considerations that you are raising are considerations that are on the table for us.

Mr. GONZALEZ OF OHIO. Ms. McWilliams, same answer? Yes or no?

Ms. MCWILLIAMS. Likewise. And I can also tell you, from my experience in Silicon Valley, working with startups, that capital investment is crucial.

Mr. GONZALEZ OF OHIO. It is unbelievable, yes.

Ms. MCWILLIAMS. Especially in the earliest stages. And we are cognizant of the ability of small businesses to create opportunities in America.

Mr. GONZALEZ OF OHIO. And then back to Mr. Quarles, with the SOFR transition that is coming, does the Fed support an extension of LIBOR beyond 2021 for existing contracts? Not for new ones, but for existing contracts that are already out there?

Mr. QUARLES. The issue is, and there has been some confusion about it, is that it is not a question of the regulators prohibiting LIBOR beyond the end of 2021 for existing contracts, but the risk that it simply won't be available, because the banks that participate in the production of LIBOR have indicated that they may be unwilling to continue participating.

Mr. GONZALEZ OF OHIO. But if it is available, would you support it?

Mr. QUARLES. We would have to consider what that meant, how it was being produced, how many banks had dropped out, how arbitrary was it then, given the remaining production process. But in connection with your question, the issue of how we handle the legacy contracts, the existing contracts, is a big one, and we are wrestling with an efficient way to do that, that ideally would not require the renegotiating of millions of contracts.

Mr. GONZALEZ OF OHIO. Yes. I think that would be chaotic, to put it lightly.

And then one concern I also hear with SOFR is it could be procyclical, just due to the nature of SOFR itself. Do you believe in the creation of credit-sensitive overlays to SOFR or an alternative rate with credit spreads?

Mr. QUARLES. I think that is a question that we ought to examine more than we have. I don't have a view, ultimately, as to whether that is something that ought to be there, but I do think that it deserves more examination than we have given it.

Mr. GONZALEZ OF OHIO. Thank you. And then with my final question, I want to focus on the repo market, which has been mentioned a little bit. I have heard—and I don't mean this as a criticism, but I am just sharing my view—a lot of different explanations of kind of, yes, it might be that, it might be this, we are not entirely sure. Do you have a sense that the Fed has a good grasp of what exactly has happened, what the driving factors are, and how we can correct it going forward?

Mr. QUARLES. I do think we have a good grasp on what the driving factors have been. I think that it is a complex question. I don't think that it is an easy answer to say this was the factor, or here are the two factors. But I do think we have a good grasp on the various factors that contributed, and I think we have a good grasp on the measures to be taken to address them, both the short-term measures and the longer-term measures, and all of them are under consideration at the Fed.

Mr. GONZALEZ OF OHIO. Thank you. And I guess with my final few seconds, I would just encourage you to share that with us, because right now it feels like we are more in the dark than I think is appropriate, given our role.

Thank you, and I yield back.

Chairwoman WATERS. Thank you. The gentleman from Texas, Mr. Green, who is also the Chair of our Subcommittee on Oversight and Investigations, is recognized for 5 minutes.

Mr. GREEN. Thank you, Madam Chairwoman. I thank the witnesses for appearing as well, and I am pleased to announce that I have in my hands a statement from the CFPB. It is styled, "Federal Regulators Issue Joint Statement on the Use of Alternative Data in Credit Underwriting." And the agencies would include the three that are here, and it includes five of the regulatory agencies.

My assumption is that some considerable amount of thought went into this decision. Is that a fair statement, when you issue a joint statement that considerable thought goes into it? If you agree just raise your hand, please.

[Show of hands.]

Mr. GREEN. Okay. All agree. Let the record reflect that all agree.

And my assumption is that you would not make this statement unless you concluded it was absolutely something that could be of benefit to our economy, to consumers. Is that a fair statement? If so, would you kindly raise your hand.

[Show of hands.]

Mr. GREEN. All seem to agree.

I would like to read the last sentence. In fact, I will read just a portion of it. It is a rather long sentence, but I would like to read a portion of the last sentence in the statement. It indicates that in doing this, it might improve the speed and accuracy of credit decisions and it may help firms evaluate creditworthiness of consumers who currently may not obtain credit in the mainstream credit system.

Strong statement. So, let's have our person who is representing NCUA, could you give some indication please, sir, as to how this will do what I have just read, that you have published?

Mr. HOOD. Yes, sir. We are really hoping to bring additional individuals into the mainstream economy by looking at alternative means of credit such as how do they pay their bills, utility, telephone payments. These are just other options that it is going to take to give individuals an opportunity to demonstrate their ability to repay.

So in signing onto that, we really want to make sure that we are helping people who are low to moderate income. There are many folks who are what we would call credit invisible. This is one of the many tools, and one of many I hope to come that would, again, enhance financial access and services to people who have never been a part of the mainline economy.

Mr. GREEN. Thank you. If you concur with what was just said, would you raise your hand, please?

Ms. MCWILLIAMS. With a caveat.

Mr. GREEN. With a caveat? Okay.

Ms. MCWILLIAMS. The caveat is that we have 24.2 million unbanked and underbanked households in the United States, and I believe it is 8.4 million who are unbanked. And a lot of these householders are, frankly, first-generation immigrants with no credit history and people who live in low- and moderate-income areas, a lot of minorities. And for them, to the extent that they don't have credit established, according to the traditional understanding of credit underwriting criteria, we would like to be able to allow companies to extend credit to them based on their transactions such as cell phone bills and utility bills, but our existing

guidance in place made it questionable exactly how entities would engage in that type of extension of credit.

So I believe this is an issue that has a broad economic impact, but I also believe it is an issue that is an equalizer for a number of people who have not been able to obtain traditional credit.

Mr. GREEN. If you agree with what was just said, would you kindly raise your hands, please?

[Show of hands.]

Mr. GREEN. I assume you agree with your statement, so let the record reflect that all agree with the statement that was just made. Given that you all agree, and you seem to indicate that this will have some positive impact on the economy, does anyone have any thought as to what this impact might be? This might be a question for the Fed. I am not sure. You do a lot of paperwork at the Fed where you analyze data. Do you have any thoughts please, sir?

Mr. QUARLES. We do a lot of research, and I don't have that research at hand, but we would be glad to provide you any work that we have done on the quantification of that.

Mr. GREEN. In a broad sense, would you think that this could have a positive impact on the economy overall?

Mr. QUARLES. Absolutely.

Mr. GREEN. Thank you very much. I bring this up because we passed a bill out of committee, H.R. 123, that addresses this additional credit scoring, alternative additional credit scoring. We have to go with "alternative additional" because of the confusion with "alternative," some people thinking that it might replace the traditional system. And I am pleased that you have come to this conclusion, and I am hopeful that we will be able to get this bill to the Floor.

Thank you, and I will yield back the balance of my time.

Chairwoman WATERS. Thank you. The gentleman from Virginia, Mr. Riggleman, is recognized for 5 minutes.

Mr. RIGGLEMAN. Thank you, Madam Chairwoman, and thank you all for being here. I want to first echo the sentiments of my colleague, Mr. Barr, regarding the hemp statement issued yesterday. I had some questions for you, Chair McWilliams, but I will follow up in writing, because after hearing Ms. Pressley's questions on FedNow, I want to spend my time focused on that issue.

Ms. MCWILLIAMS. Thank you.

Mr. RIGGLEMAN. Thank you, ma'am.

[laughter]

Mr. RIGGLEMAN. I am not quite sure. That is a good thank you, though.

[laughter]

Mr. RIGGLEMAN. Vice Chairman Quarles, you were the lone dissenter at the vote in August to proceed with the development of FedNow, and I understand why you voted that way at that time. I introduced a bill that will require the Fed to adhere to its own policy statement, including cost recovery. When will we know the cost, as far as you can tell, Vice Chairman Quarles?

Mr. QUARLES. We obviously had estimates of the costs that were considered as part of the approval. We would necessarily need that because the ability to recover the cost is a statutory requirement.

Mr. RIGGLEMAN. Yes.

Mr. QUARLES. And we believe that we can recover the costs.

Mr. RIGGLEMAN. And do we know what that cost is right now?

Mr. QUARLES. I can't tell you off the top of my head, but we do have estimates of it.

Mr. RIGGLEMAN. Okay. Thank you. I would love to see that. And when do you expect that cost recovery will be achieved?

Mr. QUARLES. It would only be over an extended period of time. I think the law requires 10 years, doesn't it? It is long term, but it would be over a long period of time.

Mr. RIGGLEMAN. A long period of time? Thank you for that. And I will have more questions on that later, but we have this 5-minute beautiful thing here. So on November 20th, in the FAQ published by the Fed, your Agency states, "The board does not have plenary authority to regulate payments." What does that mean exactly?

Mr. QUARLES. It means that we don't have direct regulatory authority. Among the concerns that were raised with the private sector system was that they could have discriminatory pricing. They could have pricing that disadvantaged some. And while they had said that they would not do that, that they would have one price for all, the Federal Reserve does not have the direct regulatory authority to address that if, in fact, they change their minds. That is what that meant.

Mr. RIGGLEMAN. Thank you. And as proposed by your Agency, FedNow will be operational by 2024, give or take. Is that correct?

Mr. QUARLES. Give or take.

Mr. RIGGLEMAN. Give or take. Some of my colleagues have introduced legislation that would dramatically expedite that service despite the current operational and functional existence of a private market platform. If Congress arbitrarily, without understanding, required the Fed to move ahead of its own timeline, what would be the effects, particularly on consumers and markets, as we went forward with that?

Mr. QUARLES. I would be concerned about a significant acceleration just because of the difficulty of execution. It is a very, very big project. I am not sure that the laws of physics would actually allow its acceleration very much from what has been proposed.

Mr. RIGGLEMAN. Yes, sir. I love the law of physics, and we are looking at the proposed regulation as far as the arbitrary timeline. Do you still think 2024 is a valid date for execution of FedNow?

Mr. QUARLES. Yes, I think that is reasonable.

Mr. RIGGLEMAN. Reasonable? Here are the issues and why I am asking these questions. On innovation—and my experience has taught me, and that has really been my background is research and development or quick reaction capabilities, things of that nature, the Department of Defense has taught me that if you want to solidify a monopoly or duopoly, then you should have the Federal Government get involved. And in the payment space, RTP is new, but it is likely not the ultimate or final development. So how do you see the Fed's involvement as potentially stifling innovation and even maybe hurting consumers as we go forward?

Mr. QUARLES. I think that it will be a task that we will have to ensure that it doesn't do that. As you have noted, innovation here is very rapid, and while I do have concerns, they ended up not being shared by my colleagues on the board, that we would not be

able to keep up with the innovation. The fact that the Federal Reserve was implementing something on the basis of current technology could, in fact, be outdated by the time that we were completed with it, that is a task that we will have to address. The Federal Reserve will devote resources to ensuring that we try to address that, and my colleagues were convinced that we could.

Mr. RIGGLEMAN. Yes, and that is why I found it interesting, Vice Chairman. We talked about the initial cost based on the report and what that would cost. Is there any costing on the sustainment cost of keeping up with technology after the initial implementation of FedNow?

Mr. QUARLES. With respect to all of that, we will be required to recover the costs under the law, and so as we would make amendments to that rapid payment system in the same way as we make additions or refinements, improvements to the current payment system that we provide, we will recover the cost of those investments.

Mr. RIGGLEMAN. Thank you so much, and thanks for your time.

Chairwoman WATERS. Thank you. The gentleman from Florida, Mr. Lawson, is recognized for 5 minutes.

Mr. LAWSON. Thank you, Madam Chairwoman, and I welcome the witnesses to the committee. I was happy to learn from your discussion about what the institutions are doing to provide credit to those who are underbanked, which I think has been very successful. Unfortunately, many people are turning to alternative sources of borrowing, including payday loans, in order to get access to capital when they are turned away from banks, sometimes including credit unions. Ms. McWilliams, can you talk more about the payday alternative loans and how this has helped bring more people into the banking sector?

Ms. MCWILLIAMS. I believe there is an opportunity for banks to engage more in the small-dollar lending space. And as was mentioned previously, there is a Federal Reserve study that says that a large percentage of the population, about 40 percent, do not have $400 every month for emergencies. And unfortunately, we don't have a lot of banks in the small-dollar space, and the consumers are now going through alternative channels for those products. We have ample consumer protection laws at the banks and the bank regulatory agencies. And, frankly, I would like to see some of those products return to banks where we can make sure that the consumers are protected.

I also think that there is a lot of dichotomy in the Federal regulatory framework with respect to small-dollar loans. From the FDIC, there is a 2013 guidance. There is a bulletin from the OCC, from 2017. There are supervisory letters from the Federal Reserve. There is a rulemaking at the CFPB. They are not all, quite frankly, synchronized, and I think there is an opportunity for us to synchronize these rules to make sure that consumers who need small-dollar credit and are in dire need of responsible small-dollar credit can do so through banks, which we regulate.

Mr. LAWSON. Okay. Thank you. Mr. Hood, I have probably been a member of credit unions for some 40 years, I guess, since I first started off. In the area I am in, in the capital city, there are a lot of credit unions and some small banks. But there have been more

concerns since I have been up here in Congress from some of the smaller banks about the growth of credit unions. And I know that when you are in a government town, a university town and so forth, where I am, you don't really think about that because people want to have access to capital. Do you feel that the concern from the smaller banks is going to continue to cause more regulations to be put on credit unions?

Mr. HOOD. I think that the important thing is that there are banks and credit unions that are all competing in today's dynamic marketplace where at the end of the day, it is the end user, whether it is a credit union member or a bank customer, they are getting access to regulated, affordable financial services. I would much rather have banks and credit unions continuing to grow in today's economy because we know what happens if that doesn't occur. Then, it leaves all of these communities that are underserved vulnerable to pernicious payday lenders.

So I don't want to pit banks versus credit unions. I want to say aye, and the credit unions, they are growing the credit unions because of members wanting to have institutions where they can get affordable capital. So when I made my opening statement this morning, credit unions now serve a third of the American public, and I think that is because of their commitment to providing access.

Mr. LAWSON. That is a very good answer, and my next question would be, before my time runs out, credit unions now take members from all over. Should there be any limitation on the memberships outside of the institutions that they are formulated on?

Mr. HOOD. That is an area that we, first of all, we do have field of membership restrictions. No matter which credit union one joins, almost everyone in this room can join a credit union, but just not the same one because of those field of membership restrictions. So if there is a particular question you have in mind, I would be happy to sit down with you. But, no, the credit unions' models were based on, for instance, you would have a plant or you would have a company. Now, as credit unions and sometimes in some instances companies have left markets, well, then those credit unions will apply for a community charter and things of that nature. So at the end of the day, credit unions still are governed by membership restrictions.

Mr. LAWSON. Should you be kept at a certain limit of the number of memberships that you could have?

Mr. HOOD. I think, sir, that is a free market decision, and I think that is up to the credit union and the member of that credit union. But, again, as long as that member has the field of membership restrictions in mind, then as a regulator, I can't impose that. I can only ensure the safety and soundness of the credit union system and the shared insurance fund that guarantees the deposits.

Mr. LAWSON. But after you go to a certain level, the tax implication or the tax exemption that you have, how does that affect you?

Mr. HOOD. Oh, you are talking about the tax-exempt status of the credit unions in terms of their size. Well, sir, I, again, am looking at the safety and soundness. Regardless of whether you are a million-dollar credit union or a $100 billion credit union, it is up

to Congress to determine whether or not credit unions maintain their tax-exempt status.

Mr. LAWSON. Okay. With that, I yield back.

Chairwoman WATERS. Thank you. The gentleman from Indiana, Mr. Hollingsworth, is recognized for 5 minutes.

Mr. HOLLINGSWORTH. Mr. Quarles, I really appreciate you being here. As you and I have talked about many times over the past couple of years, CCAR is really important to me in ensuring that we revise and become more transparent with some of the stress capital buffer rules. And I was delighted to hear earlier today, I think in response to Mrs. Wagner's question, you say that you are still aiming to have that done in time for next year's stress test cycle. I wondered if you would start kind of daisy row today how we get there because you alluded to, I think, in your answer to her question as well about how challenging the timeline might be to do so, but it still felt like it was reasonable.

Can you kind of walk us through, what does the comment period look like? How long does it take to distill that into a rule? How long does it take to get that rule out so that there's some transparency in it beforehand given these large institutions are relying a lot on that test, and with some of their capital planning thereafter, we want to make sure that they get adequate time beforehand to understand what that test looked like?

Mr. QUARLES. In order for it to be effective, at least for the next cycle, at least some elements of it would have to go final as opposed to being re-proposed.

Mr. HOLLINGSWORTH. Correct.

Mr. QUARLES. And we have the ability to do that on the basis of the comments we have received for the proposal that is out there currently. Over the course of the next several weeks, we can do that. We haven't determined if that is the right approach, which is why I say we can do it, and it is still our aim to do it, but we haven't finally decided if that is our approach.

Mr. HOLLINGSWORTH. When do you expect to make that decision? I guess what I am looking for is, when can I follow up? When can other members of the committee, those who have a significant stake in this, when can we follow up and say, okay, this was the next point at which we expected a decision, the next point at which we would expect a step taken by the Fed in order to reach that outcome by that date certain? When is the next step we can expect that we could follow up and find out whether that step was taken?

Mr. QUARLES. Whether we go final will be clear at the time we go final. I think we have about another month if we were to take that view.

Mr. HOLLINGSWORTH. Okay. And the decision would have to be made before than obviously in order to lay that out, right?

Mr. QUARLES. Right.

Mr. HOLLINGSWORTH. Okay. So it would be reasonable if we followed up within the next couple of weeks, to ask whether a decision was made to go forward with that and whether steps are in place to be able to forward with that?

Mr. QUARLES. Certainly.

Mr. HOLLINGSWORTH. I just believe that this is a really important aspect of what I hear from large institutions today, more

transparency in this process, more clarity in this process so that they can plan long term their own capital. And hopefully, that continues to support the economy overall, so I appreciate that answer.

Mr. Hood, you and I had a great conversation a couple of weeks ago as we talked about how I have had some institutions that have come into the office concerned about our recent trend of credit unions purchasing smaller banks. But at the same time, I have had some great Hoosiers who have come into the office and said, were it not for that acquisition of a bank by a credit union, my local branch probably wouldn't be here. That community wouldn't be served by that. And I felt like, frankly, you really articulated so well in that call how you think about this, how you approach this, and the rubric by which you are discerning those. I wonder if, in a minute-and-a-half, you might give us all a preview and a review of how you think about this.

Mr. HOOD. Yes, sir. Thank you for the question, and thank you for our recent call. Yes, to date, there have been 32 credit unions that have required bank assets, 32 over the past 7 years, or actually since 2013, whereas there have been roughly 250 bank-on-bank acquisitions just over the past year alone. I would like to note for the record that these are voluntary market-based transactions.

At the end of the day, it is the FDIC and the NCUA who must approve these transactions. In approving those transactions, we at NCUA are going to look to ensure that the bank is going to have the members that could qualify for the membership. We are also going to ensure that other statutes of the Federal Credit Union Act are implemented, such as the fact that business lending is capped at 12.25 percent of assets, and also credit unions are not allowed to have anything other than retained earnings for their capital. The credit unions are not going to be able to have any of the stock that an acquired institution would have had.

Also, I would like to note that in many of these areas, as you noted in your introduction, if it weren't for credit unions acquiring some of these banks, the community would be left without a financial institution. It would leave them vulnerable to, again, pernicious payday lenders. I also would like to note that at the end of the day, the bank does get to choose or select who that acquiring entity is, and, again, let's note, dual approval. Both the FDIC and the NCUA approve these, and they are not happening arbitrarily and capriciously.

Mr. HOLLINGSWORTH. Right. I think that is important to remember, and I really appreciate that. I knew your comments would help give some comfort to those who think this is happening in the absence of oversight, so I really appreciate your thoughtfulness about that.

Mr. HOOD. And we have had also a bank that has acquired a credit union.

Mr. HOLLINGSWORTH. Fair enough, and I will follow up with you, Mr. Quarles, as well. Thank you so much for your time.

Chairwoman WATERS. Thank you. The gentleman from Utah, Mr. McAdams, is recognized for 5 minutes.

Mr. MCADAMS. Thank you, Chairwoman Waters, and thank you to our witnesses for being here today. Chair McWilliams, previously when you testified before this committee, I asked about

whether the FDIC had the authority needed to properly regulate and oversee ILCs. And you testified that you believed that the FDIC did indeed have all the authority it needed to regulate ILCs and to ensure that they operate in a safe and sound manner. Do you still agree with that statement?

Ms. MCWILLIAMS. I do. I believe that Congress gave us ample authority to supervise the ILCs, yes.

Mr. MCADAMS. Thank you. And you also stated that you would not approve an ILC application for deposit insurance if you believed that it would put the insurance fund or the financial system at risk. Since that time, the topic of ILCs has gotten a lot of press and legislative attention with some calling to effectively end the ILC charter as we know it. Some of what I hear in support of ending the ILC charter is that ILCs are unregulated and pose a significant risk to the U.S. financial system.

I would like to say that I strongly disagree with both of those points, and I would like to use a bit of my time to follow up on them. My State is home to many ILCs, and in our experience, these institutions have proven to be remarkably safe and well-regulated. First, in regards to the claim of ILCs being unregulated because their parent companies are not subject to the Bank Holding Company Act, isn't it correct that the FDIC has authority to regulate the relationship and transactions between the parent company and the ILC to ensure that the ILC and our financial system remain safe?

Ms. MCWILLIAMS. In fact, we are actually able to require the so-called CULMA agreement, which is an agreement that provides for minimal capital and liquidity standards that the parent would be obligated to bestow upon the ILC to ensure that the ILC is safe and sound.

Mr. MCADAMS. Right, and I would also add that the FDIC has authority to issue cease-and-desist orders. The bank-centric model requires the bank to have an independent board and management. Section 23(a) and 23(b) sets terms around the transactions, et cetera. Do all of these provide the FDIC with adequate authority over those relationships and transactions, in your view?

Ms. MCWILLIAMS. On Sections 22 and 23, I would have to defer to the Fed. But Congress gave us ample authority to regulate the ILCs, and I certainly have staff I am paying to regulate the ILCs.

[laughter]

Ms. MCWILLIAMS. So if we are not regulating them adequately, I think some people are getting a lot of money for not doing their job, but that is not the case. We have a lot of experience recognizing the ILCs, and unless Congress decides to treat ILCs otherwise, we will continue under the existing congressional authorities.

Mr. MCADAMS. Thank you. And second, regarding the risk posed by ILCs to the U.S. financial system, for decades, ILCs have proven to be some of the safest and most stable banks in the nation. Can you tell me how ILCs compare to most other banks in the capital that they hold and in their failure rates over the past 30 years?

Ms. MCWILLIAMS. They are generally better capitalized than banks, and we don't have that many ILCs, frankly, so it is a limited universe of entities we are talking about. They are all capitalized. It is our experience that they are generally well-managed.

Again, it depends on an institution-by-institution basis, but we have not experienced issues with the ILCs.

Mr. MCADAMS. Thank you. That is my understanding as well. Moving to a different topic, I want to discuss CRA, and with respect to the Community Reinvestment Act, more of a statement than a question. I have spoken with you all previously about the need to preserve the spirit and the intent of the CRA to benefit low- and middle-income communities and individuals, while also updating the CRA for a 21st Century financial system. I understand that the OCC and the FDIC may be moving forward on a proposal without current buy-in from the Fed, and I do have concerns about this not being a unified rulemaking.

It is one thing for financial institutions to comply with the CRA regulations, but CRA also involves numerous community partners, as I know as a former mayor myself, many of which don't have the resources or time to understand potentially conflicting CRA regulations. So I would urge all of the agencies to come together on a single proposal that strengthens and modernizes CRA. And additionally, I share many of the concerns that my colleagues have expressed with respect to CECL and the impact that it may have on credit availability, in addition to the compliance requirements for financial institutions.

Moving on to another topic, Vice Chair Quarles, the Federal Reserve has been contemplating, as my colleague, Mr. Hollingsworth raised, the stress capital buffer for some time now with the proposal released in 2018, more than a year-and-a-half ago. Ensuring that we have rigorous stress tests and appropriate capital levels is important, so I just want to reiterate that I share my colleague, Mr. Hollingsworth's, concern and goals about achieving this and having this completed by 2020. And lastly, Mr. Quarles, it looks like I am about of time, so I will yield back. I may have some additional questions for the record, including on the Agency's future work on covered funds and fund structures. So thank you, and I yield back.

Chairwoman WATERS. Thank you. The gentlewoman from California, Ms. Porter, is recognized for 5 minutes.

Ms. PORTER. Thank you. Chairwoman McWilliams, you told Mr. Lawson, my colleague, that you want to return small-dollar lending to banks. Were you referring to the FDIC's looking the other way when FDIC-supervised banks are helping predatory lenders charge up to 160 percent in 26 States and the District of Columbia, where that rate is legal?

Ms. MCWILLIAMS. No.

Ms. PORTER. Are you aware of this practice?

Ms. MCWILLIAMS. I am aware of some examples of the interest rates that you cited.

Ms. PORTER. Are you aware that FDIC banks that you supervise are engaged in rent-a-bank schemes that are allowing predatory lenders to make loans with those interest rates in States that have chosen through the democratic process to prohibit those rates?

Ms. MCWILLIAMS. I am aware of partnerships that banks have created with entities that are offering those loans, and I am also aware of the enforcement action that we engage in specifically in

institutions that do so in a manner that is not consistent with consumer protection or Federal laws.

Ms. PORTER. What is consistent with consumer protection about lending at a rate that is prohibited under State law?

Ms. MCWILLIAMS. The rates are set by State law. Where we look at consumer protection, as you all know, is, are there issues with fair lending practices? Are there issues with unfair and deceptive practices—

Ms. PORTER. Pardon me, Chairwoman. I think I didn't make myself clear. Today, FinWise Bank and Republic Bank are engaged in partnerships with entities, like OppLoans and RISE/Elevate. And what they are doing is making loans at rates like 160 percent APR in States that have banned that rate. How is it consistent with the FDIC's supervision of consumer protection rules to allow these State-chartered, FDIC-supervised institutions to engage in these partnerships that evade State law, democratically-passed State law regulations on interest rates?

Ms. MCWILLIAMS. We don't regulate State interest rate caps or what is permissible or usury under State law, and I can only say this because we did have an enforcement action against one of the entities you mentioned. It is a public enforcement action—you can find it on our website—where we thought that their consumer compliance record was not, frankly, of the expectations and qualities we have of our supervised entities.

Ms. PORTER. And so are you aware of statements made on earnings calls by lenders in California in the wake of California's new lending law? Several payday lenders announced on their earnings calls that they plan to use rent-a-bank schemes to evade California's new law that outlaws 100 to 200 percent installment loans.

Ms. MCWILLIAMS. I am not, and I, frankly, don't listen to payday lenders' investors calls. I just don't have the time. I can tell you that States actually have an opportunity to opt out of the ability of out-of-State entities to provide interest rates that are prohibited in that State, and that is up to States to decide. Congress gave the States that authority, and it is, frankly, implemented in Section 27(a) of the FDI Act.

Ms. PORTER. Okay. Thank you. I wanted to follow up on what my colleague, Mr. McAdams, was asking about with regard to the Community Reinvestment Act. I am confused. I read the statement of Mr. Otting on November 20th when he announced that the Fed is not going to participate in the CRA modernization effort. I then read the statement of the Federal Reserve spokesperson. I am confused. Who here, and just feel free to raise your hand, who here is the good guy?

[Hands raised.]

[laughter]

Ms. PORTER. Okay. Now, you understand that you two are on different sides of this, so I am concerned that—

Ms. MCWILLIAMS. Not necessarily.

Ms. PORTER. I am pretty knowledgeable about the CRA, and I can't tell which one of you is in favor of which proposal. I share what Mr. McAdams said about, why is this coming unraveled. I am very concerned that it isn't a joint rulemaking, but I can't even tell which of you I should be sending a letter to, to complain. And I

think this obfuscation is really unhelpful to the American people who need to be engaged in the CRA process. Mr. Quarles?

Mr. QUARLES. I think it is inaccurate that we are on opposite sides. We have been pursuing a joint rulemaking, and the objective will continue to be at the end of the day, we will have final joint rule among the three agencies.

Ms. PORTER. Okay. If I'm not mistaken, Comptroller Otting, who is not here today, of course, announced that the Fed will not participate in the CRA modernization. Are you contradicting that?

Mr. QUARLES. Fortunately, my time is up.

[laughter]

Chairwoman WATERS. Do you yield back the balance of your time?

Ms. MCWILLIAMS. Oh, there is time, right? No, there isn't. Actually she is over, 19 seconds over.

Chairwoman WATERS. We have indicated that you may answer questions in writing and send your responses to any of our Members who have not had the opportunity to have them answered today.

I would like to thank our distinguished witnesses for their testimony today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

This hearing is now adjourned.

[Whereupon, at 1:35 p.m., the hearing was adjourned.]

A P P E N D I X

December 4, 2019

NCUA
National Credit Union Administration

Embargoed until Delivery
December 4, 2019 10 a.m.

Congressional Testimony

Rodney E. Hood
Chairman
National Credit Union Administration

House Committee on Financial Services

Hearing on Oversight of Financial Regulators: Ensuring the Safety, Soundness, Diversity, and Accountability of Depository Institutions

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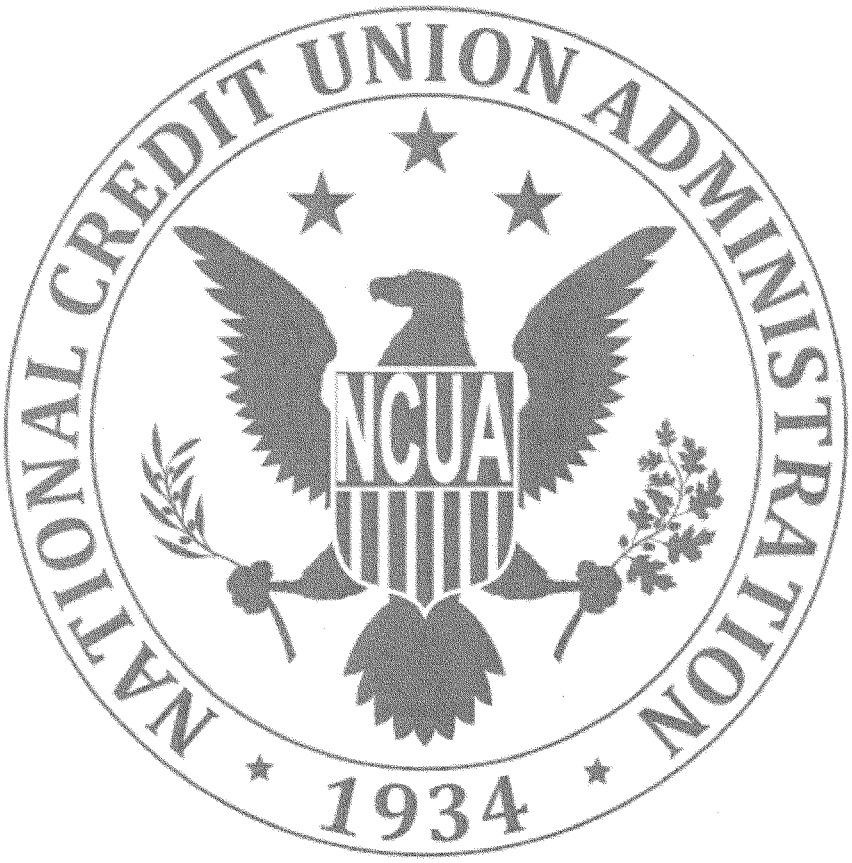

NCUA
National Credit Union Administration

Congressional Testimony

Chairwoman Waters, Ranking Member McHenry, and Members of the Committee, as Chairman of the National Credit Union Administration (NCUA) Board, I appreciate the invitation to testify today about the state of the credit union industry and to provide background on the NCUA's most recent initiatives.

The NCUA's mission is to "provide, through regulation and supervision, a safe and sound credit union system, which promotes confidence in the national system of cooperative credit."[1] This system is vital to the American economy, touching more than one-third of all U.S. households.[2] In turn, the NCUA is charged with, and focused on, ensuring the safety and soundness of the National Credit Union Share Insurance Fund (Share Insurance Fund). The agency takes seriously our paramount responsibilities to regulate and supervise approximately 5,281 federally insured credit unions with more than 119.5 million member-owners and more than $1.53 trillion in assets across all states and U.S. territories.[3] As part of that mission, we have developed initiatives to help credit unions, within the bounds of safety and soundness, serve their members more effectively, including members of modest means and those in underserved areas.[4]

I will first focus on the strong state of the credit union industry and the Share Insurance Fund and then discuss the NCUA's efforts to meet the goals the agency set out in our *2018–2022 Strategic Plan*: [5]

(1) Ensuring a safe and sound credit union system;
(2) Providing a regulatory framework that is transparent, efficient, and improves consumer access; and
(3) Maximizing organizational performance to enable mission success.

In describing how the NCUA is meeting these goals, I will focus on the NCUA Board's ongoing efforts to improve the agency's efficiency and effectiveness in light of the ever-changing financial services marketplace. The NCUA is striving to reduce the

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[1] See NCUA Mission and Vision, https://www.ncua.gov/about-ncua/mission-values.
[2] NCUA calculations using the Federal Reserve's *Survey of Consumer Finances, 2016*.
[3] Based on September 30, 2019, Call Report Data.
[4] *Serving the Underserved*, National Credit Union Administration, https://www.ncua.gov/support-services/credit-union-resources-expansion/field-membership-expansion/serving-underserved. The Federal Credit Union Act, the statute governing this agency and federally insured credit unions, specifies that this national system is intended to meet "the credit and savings needs of consumers, especially persons of modest means." Credit Union Membership Access Act, Pub. L. No. 105-219, § 2(4), 112 Stat. 913, 914 (1998).
[5] See *NCUA's 2018–2022 Strategic Plan*, https://www.ncua.gov/files/agenda-items/AG20180125Item3b.pdf.

regulatory, reporting, and examination burdens facing credit unions without sacrificing the safety and soundness of the credit union system and, in turn, the Share Insurance Fund.

I will also address some of the ways we are promoting financial inclusion and making it easier for credit unions to serve their members more effectively, including the underserved, those of modest means, people with disabilities, and those in vulnerable communities.

State of the Credit Union Industry and the Share Insurance Fund

Federally insured credit unions continued to perform well in 2019. As of September 30, 2019, credit union membership had grown by more than 3 percent over the preceding year to more than 119 million members. Assets in the credit union system increased to $1.53 trillion, and the system's aggregate net worth ratio stood at 11.39 percent, well above the 7-percent statutory level for well-capitalized credit unions.

As I said in my testimony before the Committee in May, the NCUA continues to be a responsible steward of agency funds and remains dedicated to sound financial management practices. In May, the agency paid dividends to more than 5,500 institutions eligible for a $160.1 million Share Insurance Fund distribution. This was part of the nearly $900 million in equity distributions the agency has issued over the last 18 months; money that is going back into communities to support small businesses, promote economic growth, and improve the financial well-being of credit union members across the country.

Examination and Supervision of Regulated Entities

The NCUA's supervision of federally insured credit unions consists of periodic onsite examinations and continuous offsite monitoring. The examination program is designed to deploy resources on a proportionate basis, taking into account the risk profile and size of institutions. The frequency with which the NCUA conducts examinations is consistent with the approach of the federal banking agencies.

Lower-risk federal credit unions with assets of less than $1 billion may qualify for an examination every 14 to 20 months, while all other federal credit unions receive an examination every 8 to 14 months. For federally insured, state-chartered credit unions, NCUA coordinates examination timing with state supervisors.

Additionally, the agency has a three-tiered exam program based on a credit union's asset size and risk profile. The Small Credit Union Examination Program is targeted to federal credit unions with total assets of less than $50 million and a CAMEL composite rating of 1, 2, or 3. Small credit unions that are financially and operationally sound and present a lower risk will typically have shorter examinations and more concise examination reports.

The NCUA uses a risk-focused examination program for credit unions between $50 million and $10 billion in assets. During these examinations, field staff review areas that have the highest potential risk and evaluate a credit union's compliance with federal regulations.

Lastly, the agency has a separate program to identify, mitigate, and manage the risk in large consumer credit unions, those with assets greater than $10 billion. The large credit union program includes a continuous supervision model, including enhanced off-site monitoring and data analysis. Further, these institutions are subject to capital planning and stress testing requirements to assess their financial condition and risks over the planning horizon under both expected and adverse conditions. The examinations conducted in large consumer credit unions are also subject to heightened quality control, which is conducted by the NCUA's Office of Examination and Insurance.

The agency's examination and supervision program provides for active risk management and early detection of problems, which is critical to preserving the financial strength and well-being of the system. The NCUA strives to detect and resolve problems in credit unions before they become insurmountable. Of course, the NCUA takes credit unions' compliance with legal requirements seriously, and, when necessary, takes various administrative actions to compel institutions to correct violations of law. The agency has a variety of enforcement authorities available to it and carefully considers the types of enforcement actions that would be most effective.

Because fines imposed on credit unions must be paid by credit unions' member-owners, which ultimately takes money out of communities served, the NCUA makes judicious use of its civil money penalty authority. The NCUA favors using administrative actions when a credit union is not operating in a safe and sound manner, complying with applicable statutory and regulatory requirements fully, or both.

The NCUA uses both informal and formal actions to achieve resolution of problems. Informal actions include: documents of resolution, regional director letters, unpublished letters of understanding and agreement, and preliminary warning letters. Formal actions include: published letters of understanding and agreement, cease and desist orders, involuntary liquidations, conservatorships, removals, prohibitions, terminations of insurance, and revocation of charters.

The particular administrative action or progression of actions the NCUA uses depends on the facts and circumstances of the particular case. Based on our decades of experience, we have learned that most problems can be resolved through informal actions.

The NCUA does impose civil money penalties on credit unions from time to time. The amounts of those penalties are small, designed to correct the immediate problem, and are usually assessed in response to a credit union's failure to submit Call Reports or other required data to the NCUA in a timely manner. In these limited circumstances, we have found that small civil money penalties are effective.

Cybersecurity and Technology

Credit unions compete in a dynamic and changing marketplace where they face many evolving challenges and threats. Because of this, the NCUA is bringing fresh thinking to our regulatory approach to ensure that the credit union system remains safe and sound.

Cybersecurity is a priority across the financial system, both for institutions and regulators, and across the federal government. Information technology and cybersecurity have become an integral and ubiquitous part of the delivery of financial services. While advances in technology have generated vast benefits and efficiencies, they have come with emerging risks and threats. It is essential that the NCUA strike the right balance between promoting innovation and ensuring security. Credit unions must be able to safely and securely use technology to deliver member services and to adopt financial innovations to ensure the industry's long-term success.

NCUA's Cybersecurity Initiatives

This year, I appointed a cybersecurity advisor that reports directly to the Chairman of the NCUA, Mr. Johnny E. Davis, Jr. Under my leadership, and with the advice of Mr. Davis, the NCUA has adopted key cybersecurity initiatives in addition to our overall cybersecurity examination program:

- First, we are advancing consistency, transparency, and accountability within the NCUA's cybersecurity examination program;
- Next, we provide credit unions with information and resources to improve their preparedness and resiliency. This includes sharing best practices for cybersecurity to help credit unions successfully carry out their responsibilities; and
- Finally, we have established and improved safeguards to ensure that the NCUA's systems and the information we collect are secure.

The specific program activities associated with the NCUA cybersecurity initiatives are as follows:

Information Security Maturity Assessments

The NCUA established an *Assisted Information Security Maturity Self-Assessment Program* for credit unions in 2018. We did this by benchmarking and customizing the Cybersecurity Assessment Tool developed by the Federal Financial Institutions Examination Council (FFIEC).[6]

Ultimately, we created a specialized Automated Cybersecurity Examination Toolbox for credit unions, which we call the ACET. A central element of the ACET is an assessment of a credit union's cybersecurity maturity. This maturity assessment allows the NCUA and credit unions to determine the maturity of a credit union's information security program by answering as series of 500 questions. The questions assess five specific domains:

- Cyber Risk Management and Oversight;
- Threat Intelligence and Collaboration;
- Cybersecurity Controls;
- External Dependency Management; and
- Incident Management and Resilience.

We perform an ACET maturity assessment on each credit union at least once every four years. In the years we do not perform a full ACET maturity assessment, we incorporate an emphasis on critical security controls in a credit union's regularly scheduled examination. At the conclusion of the initial four-year cycle, the NCUA will have established a baseline for each credit union assessed and a benchmark for where the credit union industry stands against other financial services institutions. A subsequent four-year cycle will identify the progress the credit union industry has made in strengthening its cybersecurity maturity.

Specifically, the NCUA has conducted, and will conduct future, ACET maturity assessments, as follows:

[6] FFIEC CAT, https://www.ffiec.gov/pdf/cybersecurity/FFIEC_CAT_May_2017.pdf

- In 2018, all scheduled institutions with $1 billion or more in assets were assessed [7];
- In 2019, all scheduled institutions that have between $250 million and $1 billion in assets have been assessed; and
- In 2020, all scheduled institutions that have between $100 million and $250 million in assets will be assessed.

The NCUA will not conduct an ACET maturity assessment of those credit unions that have $100 million or less in assets. Beginning in 2020, such smaller credit unions will be able use the ACET maturity assessment to conduct a self-assessment. In addition, examiners will emphasize the effectiveness of critical security controls when examining smaller credit unions. The ACET will be available for download on our website.

Of note, our efforts to collect baseline and benchmark data on credit unions using the ACET maturity assessment have not been used in an enforcement capacity. In the event that a safety or soundness issue is identified, examiners are trained to stop the maturity assessment and then proceed with the associated examination procedures for the Gramm-Leach-Bliley Act that are incorporated into Part 748 of the NCUA's regulations.

Information Security Examination Program

In the spirit of examination harmonization, the NCUA is in the process of updating our cybersecurity examination capabilities by leveraging the Information Technology Risk Examination (InTREx) solution utilized by the Federal Deposit Insurance Corporation, the Federal Reserve System, and the State Liaison Committee members of the Federal Financial Institutions Examination Council.[8]

Similar to the tailored work required on the FFIEC's Cybersecurity Assessment Tool, the NCUA is ensuring that our smallest institutions can have their cybersecurity posture examined without undue burden given their respective size and complexities. The InTREx solution is structured in accordance with the Uniform Rating System for Information Technology (URSIT), which focuses on a core module for audit, management, development and acquisition, and support and delivery. It also contains an escalated expanded module that has additional considerations.

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[7] Scheduled examinations and contacts are not done for all credit unions every year. Therefore, each year's demographic focus also includes any institution of the previous demographic that did not have a maturity assessment conducted (for example, in 2019, institutions of $1 billion or more in assets scheduled for examinations that were not conducted in 2018 will be subject to an ACET maturity assessment.

[8] See InTREx, https://www.fdic.gov/news/news/financial/2016/fil16043.html

The NCUA's new examination procedures described in Part 748 will be housed in our new Modern Examination and Risk Identification Tool (MERIT), which is being piloted through 2020 with full implementation scheduled for 2021.[9] The first phase of the InTREx pilot will focus on statements and questions, examination procedures, and associated job aids. The second phase will be the execution within MERIT.

Future discovery activities are also underway for the full adoption of the URSIT to ensure consistency within our cybersecurity risk ratings and appropriate weighting for IT and cybersecurity risk within the more traditional aspects of financial services.

Awareness, Training and Education Program

In accordance with the National Institute of Standards and Technology (NIST) National Initiative for Cybersecurity Education (NICE) Framework, we are enhancing our training for the following examiner roles:[10]

- Entry-level financial examiners;
- Seasoned financial examiners;
- Subject matter examiners with additional responsibilities unique to IT and cybersecurity; and
- Specialist [Information System Officers] dedicated to IT and cybersecurity.

The role-based training will emphasize the importance of critical security controls and IT service management and delivery, among other categories. The NCUA will focus on providing all agency examiners progressive training to ensure they have a common understanding of the importance of cybersecurity management, vulnerability assessments, and management specialty areas, with other specialty fields to follow.

Quality Assurance and Continual Service Improvement

To continuously review and evolve the cybersecurity examination programs effectiveness, the agency's Office of Examination and Insurance reviews the final examinations of all of our largest consumer and corporate credit unions, as well as the annual sample set of consumer credit union examinations conducted by the NCUA's regional staff. This provides a full lifecycle review on the program, analysis and help with the identification of trends. This process informs plans of action and milestones for improvements more broadly.

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[9] See MERIT, https://www.ncua.gov/regulation-supervision/examination-modernization-initiatives/enterprise-solution-modernization-program/ncua-connect-merit

[10] See NICE Framework, https://www.nist.gov/itl/applied-cybersecurity/nice/nice-cybersecurity-workforce-framework-resource-center.

Going forward, the NCUA is strengthening our review process to map more specifically with a set of NIST Cybersecurity Framework Key Performance Indicators, Key Risk Indicators, and their associated metrics.

Risk/Threat Profile Management

The NCUA is enhancing the collection of information on cybersecurity threats and risks to ensure we obtain and analyze actionable data and collaborate with the credit union industry to the fullest extent possible. We are doing this by distilling trends and tactics used by hostile actors into generic root causes. These root causes are typically in the form of critical security controls and they allow us to begin identifying the critical security controls that contribute to an array of nefarious activities. We can then develop best practice resources credit unions can use to combat the threat of cyberattacks.

Incident Management

Rapid detection and response within a credit union's incident management capabilities is an important root-cause security control. Part 748 of the NCUA's regulations require credit unions to report catastrophic events, including cybersecurity incidents, to their respective NCUA Regional Offices. The NCUA analyzes these reports for follow-on actions and to identify trends.

To improve our data collection and analysis, we are also developing an incident management system in partnership with our Office of the Chief Information Officer's Computer Security Incident Response Team.

Cybersecurity Exercise Management

The NCUA's primary initiative resulting from our relationship with the Financial Services Sector Specific Agency, U.S. Department of Treasury, the Financial Services Information Sharing Analysis and Center, and the National Credit Union Information Sharing and Analysis Organization is the agency's cybersecurity exercise management.

We consider our exercise program to be an extension of our awareness, training, and education program. Here, we focus on designing, developing, conducting, and evaluating exercises so the agency and the credit union industry can improve their resilience or the ability to prepare for, respond to, manage, and recover from adverse events as expeditiously as possible.

Special Projects and Initiatives

In support of the identified priorities and programmatic goals and objectives, the NCUA will engage in a variety of special projects and initiatives to promote cyber preparedness

within the credit union industry further. Some primary special projects and initiatives include:

- Monthly cybersecurity articles;
- Hosting cybersecurity forums;
- Hosting a national tabletop exercise;
- Enhancing our cybersecurity resource website; and
- Participating in an array of credit union-sponsored speaking engagements, workshops, and other outreach activities

Recent NCUA Rulemakings

I believe that the NCUA Board is obligated to consider the compliance burdens and the costs our institutions shoulder on a day-to-day basis. As a result, we are reducing, streamlining, and eliminating outdated or overly burdensome regulations where possible, so credit unions can simultaneously stay competitive in the changing environment and continue to provide financial services to their members and communities. We continue to improve the regulatory environment for credit unions without sacrificing our safety and soundness mission.

Bylaw Modernization

In September, the NCUA Board issued a final rule to update, clarify, and simplify the federal credit union bylaws. This final rule reflects an extensive, collaborative effort with the credit union industry dating back to 2013.

The rule was designed to clarify and update the bylaws and to provide significant flexibility in governance, balanced by the consideration of member rights and engagement. Because credit unions are member-owned cooperatives, it is important for us to get the bylaws right. They set the basic qualifications for, among other things, membership, member meeting requirements, the processes credit unions have to follow to protect member voting rights and election procedures, how bylaws and charter amendments may be adopted, and field-of-membership requirements.

One of the more significant changes we made to modernize the bylaws was to permit federal credit unions to conduct hybrid annual and special meetings. This change will be especially beneficial to federal credit unions that serve active-duty members of the armed forces who are serving our country throughout the world and who may be unable to participate in credit union meetings without virtual access. Allowing members to participate virtually, in addition to in-person meetings, has the potential to expand member engagement greatly.

We also wanted to support federal credit unions in their succession planning efforts. Credit union boards of directors are almost entirely composed of volunteers who are elected to these positions by their fellow credit union members. Succession planning in this context is extremely important, especially for smaller credit unions. To help federal credit unions maintain leadership continuity and create a pipeline of knowledge among their members, the final rule clarified that a federal credit union may establish associate director positions. These positions provide people with an opportunity to gain exposure to board meetings and discussions without formal director responsibilities. This is an important way for credit unions to increase their pool of potential board members.

Finally, we clarified that notices for events, such as annual and special meetings and elections, could be combined with regular communications from federal credit unions to their members. For example, under the new bylaws, a credit union is permitted to send a notice about the nomination process along with monthly or quarterly statements in the same mailing.

Public Unit and Nonmember Shares

This year, the NCUA Board also finalized a rule that raised the threshold on the amount of public unit and nonmember shares a federally insured credit union can receive. The rule delivers on the goals of extending responsible regulatory relief and giving greater flexibility to eligible credit unions to determine the funding structure most appropriate to support their operations.

Public unit and nonmember shares are the functional equivalent of, and no more volatile than, borrowings and, therefore, warrant a higher level of authority than the previous regulation allowed. Setting a higher, but prudent, limit on the amount of public unit and nonmember shares eliminates the need for credit unions to seek a waiver of the limit, as they had to do under the prior rule. This will save credit unions and the NCUA's regional offices valuable time and resources, and will eliminate onerous paperwork without sacrificing safety and soundness.

Most credit unions, however, will be constrained in the amount of leverage they can add to their balance sheets based on their respective levels of net worth. Many small credit unions have net worth levels high enough to take full advantage of this proposed new authority. So, while this final rule provides relief to all federally insured credit unions, it will likely benefit small and low-income-designated credit unions the most.

This final rule will provide individual credit unions with additional flexibility regarding funding options, but it will not materially increase the aggregate level of public unit and nonmember shares and borrowings the credit union system can collectively utilize. Federally insured credit unions currently have about $70 billion in outstanding public unit, nonmember shares, and borrowings, representing 4.5 percent of total assets.

In doing our research for the rule, we looked back on the overall trends for credit unions, and I'm pleased to say the industry has enjoyed solid share growth, a reflection of its financial strength and the high-quality service credit unions provide. Loan growth over the last several years has been very strong, also reflecting the value of credit unions to consumers, and has consistently outpaced share growth. However, this trend can create liquidity risk for some credit unions.

Our supervisory efforts will continue to keep a watchful eye on liquidity strength and include a more holistic view of credit unions' funding strategies, and this includes those utilizing public unit and nonmember shares as part of the mix. The final rule updates the regulations to recognize the significant changes the credit union industry has undergone in the 31 years since the original limit was adopted, including credit unions' growing need for diversified sources of funding to serve their members.

Commercial Real Estate Appraisals

As we continuously look for ways to rethink regulatory policies that could stand in the way of productive borrowing and lending to credit union members, particularly those in underserved areas — and this includes rural communities — I would like to bring to your attention a number of other rulemakings the agency has finalized this year to help credit unions serve their members better.

This past July, the NCUA Board approved a final rule to update the agency's commercial real estate appraisal standards for credit unions, raising the commercial real estate threshold from $250,000 to $1 million. This rulemaking also amended the agency's regulations to formally include the rural exemption for residential appraisals provided by the Economic Growth, Regulatory Relief, and Consumer Protection Act, or S.2155.

This particular regulatory relief matters to our communities right now. There are areas in the country that experience a scarcity of certified property appraisers. For example, some communities in the rural Midwest do not have a sufficient number of appraisers, which means the process of getting a loan to buy commercial property can get extended many weeks to enable time for a certified appraiser from another region to travel to the borrower's location and provide the necessary physical inspection and estimate of the property's value. This delay can mean significant cost, which has a material adverse impact on lenders and borrowers alike.

The agency conducted comparative analysis and due diligence to determine if raising the appraisal threshold would represent an undue risk to credit union lenders and the Share Insurance Fund. Importantly, we concluded that establishing a new threshold at $1 million does not. I want to be clear on this point. I would not move forward with a regulation that didn't adequately address safety and soundness. In addition, this only applies to real estate transactions, not to loans for other types of business assets.

Commercial lending represents a relatively small proportion of credit union assets, so these loans are not likely to be a source of undue risk to the Share Insurance Fund. Moreover, credit unions will still be responsible for adhering to the appropriate risk-management practices for underwriting commercial real estate loans, including use of written estimates of market value conducted by a qualified person independent of the transaction, such as a licensed appraiser. That is a critically important part of keeping faith with the borrowers, members, and the communities these institutions serve.

We took great care to listen to both the supporters of raising the appraisal threshold and to its critics. We considered their perspectives and weighed their concerns carefully in crafting this rule. I am confident that the final regulation is prudent and that it will facilitate lending while ensuring the safety and soundness of the financial institutions under our watch. At the same time, we instituted a number of additional safeguards to mitigate any concerns about the increased risk in these transactions. The higher appraisal threshold will be met with enhanced standards for written estimates of market value containing sufficient information to support the credit decision. These assessments will be conducted by independent and qualified professionals. This rule also allows credit unions to catch up with banks, whose qualified business loan threshold for appraisals has been at $1 million since 1994.

And, just last month we issued a proposed rule, which is currently out for public comment, to raise our residential real estate appraisal threshold from $250,000 to $400,000. Consistent with safe and sound banking practices and with the requirement for other transactions that fall below applicable appraisal thresholds, the proposed rule would require credit unions to obtain a written estimate of market value of the real property collateral in lieu of an appraisal.

We recently strengthened the regulatory standards for written estimates of market value by codifying independence requirements for persons conducting this type of valuation, and these individuals must be qualified and experienced to conduct such valuations. Raising the residential real estate appraisal threshold would bring us into alignment with the banking regulators, who raised their threshold earlier this year.

Field of Membership

The agency revived its rulemaking in the field-of-membership area, work that dates back to 2015 and 2016. On October 24, 2019, the NCUA Board unanimously approved a proposed rule to better explain its decision to eliminate the core area requirement, emphasizing that such a decision would increase flexibility to applicants for community charters, and, thus, increase the likelihood of providing financial services for low- and moderate-income individuals. The Board also re-proposed the combined statistical area provision. With this proposed rule, the agency took a critical step in the NCUA's

ongoing work to allow credit unions to alleviate some of the difficulties low-income and underserved Americans face in accessing financial services.

Payday Alternatives

Today, one of the many ways that credit unions fulfill their mission is by offering Payday Alternative Loans (PALs). While many credit unions offer some type of safer small-dollar loan product to their members, in 2010, the NCUA began authorizing a unique PALs program for federal credit unions. These loans have fewer fees and are offered at low rates capped at 28 percent, which is nothing close to the triple-digit rates charged by online and storefront payday lenders. Furthermore, as member-owned, not-for-profit financial cooperatives, credit unions play a key role in investing in their members' financial futures. They provide access to financial education, the possibility of establishing savings, and other services to ensure their members are on a pathway to financial stability. In fact, more than 80 percent of federal credit unions offering PALs report payments to credit bureaus, a critical step towards borrowers building access to mainstream financial services and breaking the cycle of debt.

At the end of 2018, 502 federal credit unions reported that they made payday alternative loans during the year. These credit unions reported making 211,574 loans amounting to $145.2 million during the year. In comparison, in 2012, 476 federal credit unions reported that they made 115,809 loans amounting to $72.6 million.

Earlier this year, the NCUA Board expanded the PALs program to give federal credit unions additional flexibility to offer their members meaningful alternatives to traditional payday loans while maintaining many of the key structural safeguards of the original PALs program. Known as PALs II, this new option is not intended to replace the current PALs program. Rather, it will be another option, with different terms and conditions, for federal credit unions to offer PALs to their members. PALs II incorporates many of the structural features of the original PALs program designed to protect borrowers from predatory payday lending practices. Those features include a limitation on rollovers, a requirement that each PALs II loan must fully amortize over the life of the loan, and a limitation on the permissible fees that a federal credit union may charge a borrower related to a PALs II loan. A federal credit union would also have to structure each loan as closed-end consumer credit. New or modified features unique to PALs II loans include: loan amount, loan term, membership requirement, number of loans, and a restriction on overdraft fees.

The original PALs program requires a borrower to be a member of a federal credit union for at least one month before the credit union can make a PALs loan to that borrower. The PALs II program does not have this minimum membership requirement. The purpose of this change was to allow a federal credit union to make a PALs II loan to any member borrower who needs access to funds immediately and would otherwise turn to a payday lender to meet that need. This is a better alternative than having those

borrowers take out predatory payday loans and wait for 30 days before rolling that predatory payday loan over into a PALs II loan, or worse, never applying for a PALs II loan. However, credit unions will be free to require a minimum length of membership for their PALs II loans if they so choose.

In contrast to the original PALs program, there is no minimum loan amount under the PALs II program, because it may not be prudent for a federal credit union to require a member to borrow more than necessary to meet their demand for funds. Establishing a minimum PALs II loan amount could require a borrower to carry a larger balance and incur additional interest charges when a smaller PALs II loan would satisfy that borrower's need for funds without the additional interest charges. The $2,000 maximum loan amount for PALs II loans is double the amount allowed under the original program and is designed to give a federal credit union the opportunity to meet increased demand for higher loan amounts from payday loan borrowers. It also provides some borrowers with an opportunity to consolidate multiple payday loans into one PALs II loan and a means for creating a pathway to mainstream financial products and services offered by credit unions.

While the original PALs program limited loan maturities to a minimum of one month and a maximum of six months, the PALs II program allows a federal credit union to make a loan with a minimum maturity of one month and a maximum maturity of 12 months. The longer loan term will allow a federal credit union making a PALs II loan to establish a repayment schedule that is affordable for the borrower while still fully amortizing the loan.

PALs II is a reflection of our experience overseeing the original PALs program and of working with consumer-focused organizations to craft financial solutions that make a difference to millions of Americans with low to moderate incomes. PALs is a program of prudent lending that directly helps households who have to date been relegated to the high interest rate, subprime payday lending industry. The NCUA is committed to building on our experience in this area and adjusting this program in a way that helps credit unions maximize sustainable and affordable service to their members.

Diversity and Inclusion

I have described financial inclusion as the civil rights issue of our era. By "inclusion," I mean not only broader access to affordable financial services, but also to employment and business opportunities. Our country is going through a period of profound demographic change, and our financial system should be leading efforts to respond to that change. Credit unions are growing stronger, and they serve their members and communities better when they promote greater diversity, equity, and inclusion as part of their business model.

The Committee asked specifically about the NCUA's compliance with Section 342 of the Dodd-Frank Wall Street Reform and Consumer Protection Act and our Office of Minority and Women Inclusion. The NCUA complies with every component of Section 342.

With respect to diversity within credit unions, the NCUA issues an annual voluntary self-assessment for credit unions to assess diversity and inclusion within their organizations. As the regulator, we model for the industry that diversity, equity, and inclusion are strategic imperatives. All three of the agency's board members continuously promote the value of these principles within the industry. We were the first among the financial regulators to issue the self-assessment tool. We are currently in our fourth year of collecting submissions from the industry. We strongly encourage credit unions to assess their diversity and inclusion policies and practices through the NCUA's Credit Union Diversity Self-Assessment. For example, we recently hosted an industry-specific diversity, equity, and inclusion summit to provide best practices and promote the value of diversity to the industry. We have committed to hosting such an event annually in different locations to promote greater opportunities for stakeholder participation.

The agency already provides guidance to the industry on supplier diversity and we will be issuing a guide on boardroom diversity. As Chairman of the Board, I have sent letters to all federally insured credit union CEOs expressing the NCUA's commitment to diversity, equity and inclusion and asking for their participation in the credit union diversity self-assessment. Similar communications have also been sent to all credit union leagues, asking them to encourage their members to submit the self-assessment.

The agency has taken the position of going beyond just assessing and setting standards for the industry. We are actively promoting the principles of diversity, equity, and inclusion, including providing guidance and sharing best practices.

In terms of supplier diversity, the NCUA has integrated supplier diversity principles into our own procurement process. As a result, we have grown from 6 percent in awarded contract dollars to minority- and women-owned businesses in 2010 to 45 percent in 2018.

With respect to workforce diversity and inclusion at the NCUA, we have a robust and comprehensive program that has allowed the agency to make improvements in the demographics of our entire workforce, including at the senior leadership level. As of the pay period ending on March 16, 2019, the NCUA workforce composition was as follows:

- The total NCUA workforce count was 1,120.
- Males made up 631, or 56.3 percent, of the total NCUA workforce.

- Females made up 489, or 43.7, percent of the total NCUA workforce.
- Minorities made up 333, or 29.7, percent of the total NCUA workforce.
- The NCUA senior leadership team was 46 percent female.
- The NCUA senior leadership team was 22 percent minority.

Our assessment of our diversity and inclusion initiatives is an ongoing process and one we continually seek to develop and improve.

Second Chance Initiative

Another initiative the Board undertook in the diversity, equity, and inclusion space earlier this year, and one which I consider to be one of our most important Board actions, involves extending "second chance" opportunities to job applicants with old criminal records for minor, non-violent offenses. It is hard to estimate accurately the number of Americans with criminal records, but one commonly cited number is 70 million. A great many of these Americans face barriers to hiring that leave them unemployed or underemployed. Fortunately, policymakers and corporate leaders have begun to rethink these punitive hiring practices and the financial services industry can and should play a leading role in welcoming these individuals back into the mainstream of American life.

The NCUA Board is making a concerted effort to provide second chances where we can.

Since I became Chairman, we approved an employment waiver for a woman who has a criminal record. But, she paid her debt to society, rehabilitated herself, and has no further history of criminal behavior. A drug addiction from nearly 25 years ago will not hold her back from working for a federally insured credit union.

On a broader policy level, the Board recently updated the agency's Interpretive Ruling and Policy Statement regarding statutory prohibitions on persons who have been convicted of any criminal offense involving dishonesty or breach of trust or who have entered into pretrial diversion or similar programs in connection with a prosecution for such offenses. Previously, such a person could not participate in the affairs of an insured credit union except with the prior written consent of the Board. By amending our guidance, we are reducing the scope and number of offenses that would require an application to the Board. Specifically, credit unions would not have to get prior Board approval to hire someone who, as a young adult, committed such violations as small-dollar theft, false identification, simple drug possession, and other isolated minor offenses.

My primary responsibility is the industry's safety and soundness. But, where appropriate, I want to encourage the financial services industry to take reform-minded steps that better meet the needs of the communities and citizens we serve.

Minority Depository Institutions

Another initiative we have developed to make it easier for credit unions to serve members of modest means and those in underserved areas is our minority depository institution (MDI) preservation program, through which we provide technical assistance, training, and mentoring opportunities to help MDI credit unions help their members.

Credit unions are by design different from other financial institutions. They are member-owned-and-controlled, not-for-profit, cooperative entities. Their boards of directors are made up of volunteers. Their central mission is to give groups of people access to affordable financial services and the ability to participate in their institutions' management.

MDI credit unions, more particularly, serve the financial needs of racial minorities because such populations traditionally have been underserved by the financial system. A credit union's designation as an MDI is defined by the minority composition of its current and potential membership and the minority composition of its board of director, consistent with the definition set forth in Section 308 of The Financial Institutions Reform, Recovery, and Enforcement Act of 1989.

The NCUA understands the significant value these credit unions represent to their members and communities, and recognizes the challenges they face. There are many benefits to having a diverse and inclusive financial services sector. It makes sense to have board members, managers, senior leaders, and employees reflect the community a financial institution serves. Diversity leads to better service, greater innovation, improved solutions and a larger customer or membership base. This is why the NCUA is committed to supporting MDIs and the communities they serve.

As of June 30, 2019, there are 526 federally insured credit unions designated as MDIs. Collectively, MDI credit unions serve 3.9 million members, manage $39.6 billion in assets, hold aggregate deposits of $34 billion, and own $27.5 billion in loans.

Earlier this year, the NCUA created a new pilot mentoring program for small low-income credit unions that are also designated as MDIs. I'm delighted we could help these small credit unions establish relationships with larger institutions to help them grow and thrive.

Diversity, Equity, and Inclusion Summit

Last month, the NCUA hosted its first Credit Union Diversity, Equity, and Inclusion Summit, bringing together industry leaders, regulators, and policy experts for a daylong series of conversations focused on what the credit union industry can do to better advance our commitment to a financial system that works for everyone. For too long, too many people have been overlooked or locked out of the financial mainstream. We know that the lack of access to affordable financial services holds working families back from taking that next step up the financial ladder. We need to remove the obstacles to financial security these Americans are facing.

Guidance on Serving Legal Hemp Businesses

One area I want to highlight, because of recent Congressional action in this space and ongoing Congressional interest, is the legalization of hemp as part of the Agricultural Improvement Act of 2018. Since the enactment of the law, we have been proactive in making sure that credit unions are aware that the law removed hemp from the Controlled Substances Act and the framework Congress has created for the U.S. Department of Agriculture (USDA) to regulate domestic hemp production.

We expect to continue updating the credit union community now that the USDA has published its interim final rule. We have received interest from credit unions eager to know the rules of the road for serving hemp-related businesses in their communities, and we want to make sure those credit unions have what they need to make informed decisions in this area.

Some credit unions have lawfully operating hemp businesses within their fields of membership. Businesses dealing with hemp and hemp-derived products include manufacturing, distribution, shipping, and retail companies, among others. With the recent changes in federal law, more hemp-related businesses may be founded, and existing ones expanded. Growth in hemp-related commerce could provide new economic opportunities for some communities and will create a need for such businesses to be able to access capital and financial services. In turn, we continue to advise credit unions that they must be aware of the federal, state, and Indian tribal laws and regulations that apply to any hemp-related businesses they serve, and they need to understand the complexities and risks involved. We are advising credit unions that they must continue to have Bank Secrecy Act (BSA) and Anti-Money Laundering (AML) compliance programs commensurate with the level of risk and complexity involved in the services and accounts they offer.

Many credit unions have a long and successful history of providing services to the agriculture sector. Hemp provides new opportunities for agricultural communities. The NCUA is encouraging credit unions to thoughtfully consider whether they are able to

safely and properly serve lawfully operating hemp-related businesses within their fields of membership, and we stand ready to work with them.

Incentive Compensation

The Committee asked for an update on the interagency rulemaking that stems from Section 956 of Dodd-Frank regarding enhanced compensation structure reporting, otherwise known as incentive compensation. Section 956 requires the NCUA, the federal banking agencies, the Securities and Exchange Commission, and the Federal Housing Finance Agency to prescribe regulations or guidelines jointly with respect to incentive-based compensation practices at covered financial institutions. The regulations or guidelines must prohibit incentive-based compensation arrangements that either encourage inappropriate risks by providing excessive compensation or that could lead to material financial loss to the covered financial institution.

The agencies have previously published proposed rules to implement Section 956, once in 2011 and again in 2016. I am committed to doing my part to comply with this Dodd-Frank mandate.

Merger and Acquisition Activity

The declining number of federally insured credit unions reflects a long-term trend of consolidation within the financial services industry overall. The vast majority of credit union merger activity is voluntary, with credit unions citing economies of scale, the ability to offer relevant online banking services, and succession planning as the top reasons for mergers. However, each year, a relatively small number of institutions are merged or acquired at a cost to the Share Insurance Fund. Seven federally insured credit unions that were merged or acquired in 2018 required assistance from the Share Insurance Fund.

Bank Secrecy Act/Anti-Money Laundering

NCUA conducts a BSA/AML review during every examination and takes appropriate action when necessary to ensure our regulated financial institutions meet their obligations under applicable BSA/AML regulations.

The NCUA continues to partner with fellow federal financial regulators, Treasury, and the Financial Crimes Enforcement Network (FinCEN), to improve transparency, efficiency and effectiveness of the BSA/AML regime in the United States. This partnership includes outreach to all industry stakeholders and continued work streams by agency staff, along with our partners at the other federal financial regulatory

agencies and Treasury, to continue improving transparency, clarity, and effectiveness while seeking ways to reduce burden and increase efficiency.

In October 2018, the NCUA joined other federal agencies in issuing a joint statement addressing improved efficiency through shared resources and collaborative relationships. The statement outlines ways in which institutions with limited BSA risk can share resources with other similar institutions, thereby lowering costs while in many cases improving effectiveness and efficiency. It addresses instances in which these institutions might decide to enter into collaborative arrangements to share resources to manage their BSA/AML obligations more efficiently and effectively. The costs of meeting BSA/AML requirements and effectively managing the risk that illicit finance poses to the broader U.S. financial system may be reduced through sharing employees or other resources in a collaborative arrangement with one or more other credit unions or banks. These arrangements may also provide access to specialized expertise that individual institutions may otherwise be challenged to acquire without the collaboration. This may benefit some credit unions, especially smaller institutions that may find hiring or retaining staff with the necessary knowledge a challenge.

In July of this year, the agencies issued a joint statement clarifying the consistent risk-focused approach used by the federal financial regulators, including the NCUA, during examinations. The statement helps regulated financial institutions better understand what they can expect during a BSA/AML examination as well as clarifying that the agencies tailor each examination to the unique characteristics and risk indicators that exist at each institution. It outlines common practices for assessing an institution's money laundering/terrorist financing risk profile, assisting examiners in scoping and planning the examination, and evaluating initially the adequacy of the BSA/AML compliance program. Using this approach, the agencies generally are able to allocate more resources to higher-risk areas and fewer resources to lower-risk areas when conducting BSA/AML examinations. This risk focus ensures meaningful examinations scaled up or down based on the risk presented by each unique institution.

The NCUA is also working closely with our partner agencies to revise and update the BSA/AML examination manual to clarify expectations for examiners. FFIEC agencies and Treasury are working diligently to ensure examiners appropriately apply a risk-focused examination consistently.

Finally, I meet monthly with my federal counterparts to closely monitor and provide direction to agency staff on priorities and initiatives designed to improve transparency, efficiency and, most importantly, the effectiveness of the BSA/AML regime in the United States.

Financial Technology Updates

While financial innovation holds promise, it is crucial that credit unions, consumers, and other stakeholders understand and mitigate associated risks. The NCUA's goal is to balance maintaining the safety and soundness of credit unions without stifling their use of innovative technology and related vendors. Credit unions need to embrace financial technology while also clearly understanding and managing any risks they may incur.

My top priorities with respect to fintech include outreach and education. The NCUA's Fintech Working Group is looking at ways federally insured credit unions can adopt and embrace fintech so they can compete in the changing financial services industry effectively. The agency will continue to solicit industry feedback about the competitive issues credit unions face, and the industry is collaborating with marketplace lenders and other fintech companies.

The NCUA will continue to promote technical assistance programs that low-income credit unions can use to support the acquisition and development of fintech-related digital services. I am also interested in exploring opportunities to partner with academic institutions to continue to research and monitor financial technology—such as online lenders, machine learning, artificial intelligence, and payment systems—to identify the benefits to consumers, especially those that are underserved and how fintech may affect credit unions.

The NCUA is actively coordinating on fintech issues with the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Consumer Financial Protection Bureau. The agency will continue to participate in interagency working groups and discussion forums, and any other opportunities for coordination.

Thank you for the opportunity to provide an update on the strong state of the credit union industry and to highlight NCUA's latest initiatives. I look forward to your questions.

STATEMENT OF

JELENA MCWILLIAMS
CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION

on

OVERSIGHT OF PRUDENTIAL REGULATORS: ENSURING THE SAFETY, SOUNDNESS, DIVERSITY, AND ACCOUNTABILITY OF DEPOSITORY INSTITUTIONS?

before the

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

December 4, 2019
2128 Rayburn House Office Building

Chairwoman Waters, Ranking Member McHenry, and members of the Committee, thank you for the opportunity to testify before the House Committee on Financial Services.

Exactly 18 months ago, I began serving as the 21st Chairman of the Federal Deposit Insurance Corporation (FDIC). During this period, the FDIC has undertaken a significant amount of work with a particular emphasis on three overarching goals:

- Strengthening the banking system as it continues to evolve;
- Ensuring that FDIC-supervised institutions can meet the needs of consumers and businesses; and
- Fostering technology solutions and encouraging innovation at community banks and the FDIC.

The FDIC has made significant progress in each of these areas, and I appreciate the opportunity to share with the Committee how we will continue to move each of them forward.

I. State of the U.S. Banking Industry

Before discussing the FDIC's work to strengthen the banking system, I would like to begin by providing context regarding the current state of the industry.

The U.S. banking industry has enjoyed an extended period of positive economic growth. In July, the economic expansion became the longest on record in the United States. By nearly every metric – net income, net interest margin, net operating revenue, loan growth, asset quality, loan loss reserves, capital levels, and the number of "problem banks" – the banking industry is strong and well-positioned to continue supporting the U.S. economy.

With respect to profitability, banks of all sizes are performing well. In the third quarter of 2019, the 5,256 FDIC-insured banks and savings institutions reported net income of $57.4 billion.[1] Nearly 62 percent of institutions reported annual increases in net income, and only about 4 percent of institutions were unprofitable. Notably, community banks reported net income of $6.9 billion, an increase of 7.2 percent from a year earlier. Net interest margin also remained stable, with an average of 3.35 percent across the industry and a particularly strong average of 3.69 percent among community banks. Finally, net operating revenue totaled over $208 billion, an increase of 2.2 percent from a year earlier.

Key balance sheet indicators are similarly robust. Total loan balances increased by 4.6 percent, up from the 4.5 percent growth rate reported the previous quarter. Again, community banks performed particularly well in this area, with an annual rate of loan growth that was stronger than the overall industry. Asset quality also remained strong, as the rate of noncurrent loans (*i.e.*, loans that are 90 days or more past due) declined to 0.92 percent. Finally, the industry's capacity to absorb credit losses improved from a year earlier, as the reserve coverage ratio (*i.e.*, loan-loss reserves relative to total noncurrent loan balances) rose to 131 percent.

[1] *See* FDIC Quarterly Banking Profile, Third Quarter 2019, available at https://www.fdic.gov/bank/analytical/qbp/2019sep/qbp.pdf. Unless otherwise indicated, all statistics are derived from this report as of the third quarter of 2019.

Although the current interest rate environment may result in new challenges for banks in lending and funding, the industry is well-positioned to remain resilient throughout the economic cycle, principally as a result of greater and higher-quality equity capital. Equity capital across the industry rose to $2.1 trillion, up $3.5 billion from the previous quarter. This capital increase translated to an aggregate common equity tier 1 capital ratio of 13.25 percent.

The number of institutions on the FDIC's "Problem Bank List" declined from 56 to 55, the lowest number since the first quarter of 2007, and four new banks opened during the third quarter for a total of 10 new banks in 2019.

Four banks failed during 2019 – the first failures since December 2017. It is important to recognize that, even in a healthy economy, some banks will inevitably fail. The economic expansion we have experienced resulted in an anomalous stretch in which there were zero bank failures. This expansion and consequent absence of failures cannot endure forever. It is normal – and indeed expected – for some banks to fail, and our job at the FDIC is to protect depositors and ensure that banks can fail in an orderly manner.

The key to the FDIC's ability to protect depositors is the administration of the Deposit Insurance Fund (DIF), which increased to a record $108.9 billion in the third quarter.[2] The DIF's reserve ratio (*i.e.*, the fund balance as a percent of estimated insured deposits) increased to 1.41 percent, the highest level since 1999.

In 2010, Congress instituted the DIF Restoration Plan, which required the FDIC to raise the DIF minimum reserve ratio from 1.15 percent to 1.35 percent by September 30, 2020. Although we continue to work toward our 2 percent target, the FDIC has met the statutory requirement and formally exited the DIF Restoration Plan. Accordingly, we have awarded $764.4 million in credits to banks with less than $10 billion in assets for the portion of their assessments that contributed to the increase.[3]

In addition, the FDIC recently proposed a rule[4] that would amend our deposit insurance assessment regulations to continue to apply small bank credits as long as the DIF remains at least 1.35 percent rather than the current 1.38 percent. This proposal seeks to make the application of small bank credits to quarterly assessments more stable and predictable for smaller institutions and simplify the FDIC's administration of these credits without impairing our ability to maintain the required minimum reserve ratio of 1.35 percent.

The FDIC will continue to manage the DIF prudently and responsibly in pursuit of our statutory mission to maintain stability and public confidence in the nation's financial system.

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[2] *See* FDIC Deposit Insurance Fund Trends, Third Quarter 2019, available at https://www.fdic.gov/bank/analytical/qbp/2019sep/qbpdep.html.

[3] *Id.*

[4] *See* Assessments, 84 Fed. Reg. 45443 (Aug. 29, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-08-29/pdf/2019-18257.pdf.

II. Strengthening the Banking System

While the state of the banking system remains strong, the FDIC is not standing idly by. We continue to monitor changes in the industry and work to further strengthen the banking system by:

- Modernizing our approach to supervision and increasing transparency;
- Tailoring regulations;
- Enhancing resolution preparedness;
- Assessing new and emerging risks; and
- Creating the workforce of the future.

I will address each of these efforts in turn.

A. Modernizing Supervision and Increasing Transparency

As the primary supervisor of the majority of the nation's small and medium-size banks, the FDIC oversees a segment of the banking system that plays a vital role in communities across the country.[5] Through our back-up examination authority, the FDIC also has the ability to examine the nation's largest banks.

Having worked both as a regulator and at a regulated entity before arriving at the FDIC, I have spent a great deal of time thinking about effective supervision and examination. Our supervisory approach should achieve the following objectives: (1) ensure that institutions are safe and sound; (2) provide clear rules of the road; (3) be consistent in its application; (4) be fair, effective, and holistic in the consideration of regulatory issues; (5) be timely and contemporary in providing feedback; (6) respect the business judgment of an institution's management team; and (7) promote an open, two-way dialogue between the regulated and the regulators.

In furtherance of these objectives, the FDIC has undertaken a number of reforms to modernize our approach to supervision and increase the transparency of our programs.

1. CAMELS Ratings

The FDIC and the Federal Reserve Board (FRB) recently issued a notice and request for comment on the consistency of ratings assigned under the Uniform Financial Institutions Rating System (UFIRS), commonly known as CAMELS ratings because of the six evaluation components (*i.e.*, Capital, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk).[6] This system, which was established in 1979, is critical to our supervisory efforts. Despite vast changes in technology, industry practices, and regulatory standards, the system has not been materially updated in nearly 25 years. We are seeking feedback on how CAMELS ratings are assigned to supervised institutions and the implications of such ratings in the

[5] As of September 30, 2019, the FDIC insures the deposits of 5,256 institutions and acts as the primary supervisor of 3,384 state-chartered institutions that are not members of the Federal Reserve System.
[6] *See* Request for Information on Application of the Uniform Financial Institutions Rating System, 84 Fed. Reg. 58383 (Oct. 31, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-10-31/pdf/2019-23739.pdf.

application and enforcement action processes. This request is consistent with our commitment to increase transparency, improve efficiency, support innovation, and provide opportunities for public feedback. We look forward to receiving public comments and engaging further with stakeholders and the other banking agencies on this effort.

2. "Trust through Transparency"

With the goal of increasing the transparency of our supervisory programs, my first major initiative as Chairman was "Trust through Transparency," which builds upon the agency's solid foundation of public trust and accountability by fostering a deeper culture of openness. As part of this initiative, we launched a new public section of our website where we publish FDIC performance metrics, including turnaround times for examinations and bank charter applications, call center usage and response times, and data on the status of supervisory and assessment appeals.[7]

This program is not *just* about publishing more information. Instead, we are using the heightened public scrutiny of our work to hold ourselves publicly accountable to high standards, and our effort is already yielding positive results.

3. Supervision Modernization

As part of our efforts to modernize supervision, FDIC examination teams are leveraging technology to reduce the amount of time they spend on-site at supervised institutions. This reduces the compliance burden for institutions – especially community banks – without sacrificing the quality of our supervision.

As a result, our examination turnaround time (*i.e.*, the time from when field work begins to when the examination report is sent to the bank) has significantly improved. During the 12 months ended September 30, 2019, more than 87 percent of safety and soundness examinations were conducted within our 75-day goal and more than 96 percent of consumer compliance and Community Reinvestment Act (CRA) examinations were conducted within our 120-day goal. Similarly, examination report processing time (*i.e.*, the time from when field work is complete to when the report is sent to the bank) has improved, with more than 92 percent of safety and soundness reports and more than 98 percent of consumer compliance and CRA reports processed within our 45-day goal.

We recently established a new Subcommittee on Supervision Modernization – which reports to our Community Bank Advisory Committee (CBAC) – to make recommendations for improving our supervisory activities. The Subcommittee, which is comprised of 15 bankers, technologists, former regulators, and legal experts, is tasked with considering how the FDIC can further leverage technology and refine its processes to improve the efficiency of the examination program, while managing and training a geographically dispersed workforce.

[7] *See* FDIC Transparency & Accountability, available at https://www.fdic.gov/transparency.

4. *De Novo* Application Process

Another key focus of our supervisory modernization effort has been the *de novo* application process. *De novo* banks are an important source of new capital, talent, and ideas, and many offer products and services to underserved communities and fill gaps in overlooked markets. The need for these institutions is underscored by the uneven distribution of banking offices across the country. As of June 30, 2019, 620 counties – or 20 percent of the counties across the nation – were served only by community banking offices, 127 counties had only one banking office, and 33 counties had no banking offices at all.[8]

In the decade immediately following the financial crisis, very few new banks opened due to the challenging economic environment and regulatory constraints. During my first year as Chairman, the FDIC emphasized the need for greater *de novo* activity, and the FDIC has taken several actions to support this objective, including:

- Revising our process for reviewing deposit insurance proposals to provide initial feedback to organizers on draft applications prior to submission;[9]
- Updating two manuals related to the deposit insurance application process;[10]
- Issuing a request for information to solicit additional ideas for improvement;[11] and
- Engaging with stakeholders at seven roundtables across the country.

Results we have seen thus far are encouraging. Organizers have expressed renewed interest in *de novo* charters, and we approved 14 *de novo* banks in 2018 – more than the total number of approvals in the eight previous years combined.[12] This momentum has continued throughout 2019, and we have approved eight *de novo* banks thus far.

5. Interagency Statement on Alternative Data

Earlier this week, the FDIC, FRB, Office of the Comptroller of the Currency (OCC), Consumer Financial Protection Bureau (CFPB), and National Credit Union Administration (NCUA) jointly issued a statement[13] encouraging the responsible use of alternative data (*i.e.*, data not typically found in the consumer's credit files of the nationwide consumer reporting agencies or customarily provided as part of applications for credit) for use in credit underwriting. The agencies recognize that the use of alternative data may improve the speed and accuracy of

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[8] *See* FDIC Summary of Deposits, available at https://www7.fdic.gov/SOD.
[9] *See* FDIC FIL-82-2018, *Review Process for Draft Deposit Insurance Proposals* (Dec. 6, 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18082.html.
[10] *See* FDIC FIL-83-2018, *FDIC Issues an Update to its Publication Entitled* Applying for Deposit Insurance – A Handbook for Organizers of De Novo Institutions, *Finalizes its Deposit Insurance Applications Procedures Manual, and Establishes a Designated Applications Mailbox* (Dec. 6, 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18083.html.
[11] *See* Request for Information on the FDIC's Deposit Insurance Application Process, 83 Fed. Reg. 63868 (Dec. 12, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-12-12/pdf/2018-26811.pdf.
[12] *See* FDIC Decisions on Bank Applications, available at https://www.fdic.gov/regulations/laws/bankdecisions/depins/index.html.
[13] *See* Federal Regulators issue joint statement on the use of alternative data in credit underwriting (Dec. 3, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19117.html.

credit decisions and may help firms evaluate the creditworthiness of consumers who currently may not obtain credit in the mainstream credit system. The statement also emphasizes that, if firms choose to use alternative data, they must comply with applicable consumer protection laws, including fair lending laws and the Fair Credit Reporting Act.

6. Federal Interest Rate Authority

Our push for modernization is not limited to supervision and examination programs, but also includes work to provide clarity on key legal issues. One specific example of this approach is an ongoing effort to address marketplace uncertainty regarding the enforceability of the interest rate terms of loan agreements following a bank's assignment of a loan to a nonbank. In 2015, the United States Court of Appeals for the Second Circuit issued a decision[14] that called into question such enforceability by holding that 12 U.S.C. § 85 – which authorizes national banks to charge interest at the rate permitted by the law of the state in which the bank is located, regardless of other states' interest rate restrictions – does not apply following assignment of a loan to a nonbank. Although this decision concerned a loan made by a national bank, the statutory provision governing state banks' authority with respect to interest rates is patterned after and interpreted in the same manner.[15]

Last month, we proposed a rule[16] that would clarify the law governing the interest rates state banks may charge. Among other things, the proposal would provide that whether interest on a loan is permissible under section 27 of the Federal Deposit Insurance Act (FDI Act) would be determined at the time the loan is made, and interest on a loan permissible under section 27 would not be affected by subsequent events, such as a change in state law, a change in the relevant commercial paper rate, or the sale, assignment, or other transfer of the loan.

7. Cooperation with State Regulators

In an effort to facilitate and increase dialogue between the FDIC and our state regulatory partners on a host of important regulatory issues, the FDIC approved the establishment of a new Advisory Committee of State Regulators (ACSR).[17] The committee will allow the FDIC and state regulators to discuss a variety of current and emerging issues that have potential implications for the regulation and supervision of state-chartered financial institutions. Once fully established, ACSR will facilitate discussions of: safety and soundness and consumer protection issues; the creation of new banks; the protection of our nation's financial system from risks such as cyberattacks or money laundering; and other timely issues.

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[14] *See Madden v. Midland Funding, LLC*, 786 F.3d 246 (2d Cir. 2015), *cert. denied*, 136 S. Ct. 2505 (2016).
[15] 12 U.S.C. §1831d.
[16] *See* FDIC Proposes New Rule Clarifying Federal Interest Rate Authority (Nov. 19, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19107.html.
[17] *See* FDIC Board Approves Establishment of Advisory Committee of State Regulators (Nov. 19, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19105.html.

B. Tailoring Regulations

As we continue to think about ways to strengthen the banking system, the appropriate calibration of our regulatory framework remains a top priority. Given the wide range of risk profiles across banking organizations, it is critical that regulators continuously evaluate whether our rules are being applied properly and not imposing unnecessary regulatory burdens that might impede safe and sound banking activities. As such, the FDIC has taken numerous actions to tailor our regulatory framework while maintaining safety and soundness, financial stability, and consumer protection.

1. Enhanced Prudential Standards

In May 2018, Congress enacted the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA),[18] which set forth specific legislative instructions for regulatory tailoring, including by raising the statutory asset threshold for the application of enhanced prudential standards to $250 billion (while giving the FRB the discretion to apply such standards to firms with assets between $100 billion and $250 billion). Last month, the FDIC, FRB, and OCC finalized a rule that implements a key part of EGRRCPA by establishing four risk-based categories for determining capital and liquidity requirements.[19] Under the rule, requirements for Category I firms (*i.e.*, U.S. global systemically important banks, or GSIBs) are unchanged, and these institutions remain subject to the most stringent standards. Requirements for Category II, Category III, and Category IV firms (*i.e.*, all other banking organizations with greater than $100 billion in assets) are tiered based on each bank's risk profile.

Beyond the tailoring rule, the FDIC has completed all of its EGRRCPA-mandated rules. Appendix A to this testimony contains a full list of these rules.

2. Company-Run Stress Testing

Just as EGRRCPA raised the asset threshold for the application of enhanced prudential standards from $50 billion to $250 billion, it raised the asset threshold for company-run stress testing requirements from $10 billion to $250 billion. We recently finalized a rule[20] to reflect this statutory change. We are also working on amendments to our interagency stress testing guidance[21] that would further tailor supervisory expectations. Specifically, we are considering raising the asset threshold under the guidance to $100 billion in assets, among other potential changes.

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[18] Pub. L. 115-174 (May 24, 2018), available at https://www.govinfo.gov/content/pkg/PLAW-115publ174/pdf/PLAW-115publ174.pdf.

[19] *See* Changes to Applicability Thresholders for Regulatory Capital and Liquidity Requirements, 84 Fed. Reg. 59230 (Nov. 1, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-01/pdf/2019-23800.pdf.

[20] *See* Company-Run Stress Testing Requirements for FDIC-Supervised State Nonmember Banks and State Savings Associations, 84 Fed. Reg. 56929 (Oct. 24, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-10-24/pdf/2019-23036.pdf.

[21] *See* Supervisory Guidance on Stress Testing for Banking Organizations With More Than $10 Billion in Total Consolidated Assets, 77 Fed. Reg. 29458 (May 17, 2012), available at https://www.govinfo.gov/content/pkg/FR-2012-05-17/pdf/2012-11989.pdf.

3. Resolution Planning

In 2011, the FDIC and FRB finalized a rule[22] establishing new resolution planning requirements. Over the past eight years, large firms have improved their resolution strategies and governance, refined their estimates of liquidity and capital needs in resolution, and simplified their legal structures. Consistent with the new statutory asset threshold under EGRRCPA and the agencies' experience with resolution planning, the FDIC and FRB recently issued a final rule[23] to improve the efficiency and effectiveness of the process and exempt smaller regional banks from the requirements. Under the rule, our underlying standards for reviewing resolution plans will not change. With respect to timing, the rule formalizes the agencies' existing practice of requiring U.S. GSIBs to submit resolution plans every two years and requiring other filers to submit plans every three years. The rule also introduces a new "targeted resolution plan" that will allow filers to submit a subset of information required by a full resolution plan. Such targeted plans will be submitted every other cycle.

4. Incentive-Based Compensation

In June 2010 – a month prior to the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act)[24] – the FDIC, FRB, and OCC issued guidance[25] to help ensure that incentive compensation policies at banking organizations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organization. In connection with the guidance, then-FRB Governor Daniel Tarullo noted that many large banking organizations had already implemented certain changes in their incentive compensation policies.[26] Section 956 of the Dodd-Frank Act subsequently directed the FDIC, FRB, OCC, NCUA, Securities and Exchange Commission (SEC), and Commodity Futures Trading Commission (CFTC) to jointly prescribe, within nine months of the enactment of the law, regulations or guidelines that prohibit any types of incentive-based pay arrangement that encourages inappropriate risks, based on the standards established in the FDI Act.[27] Proposals to implement this statute were issued in 2011[28] and 2016,[29] but neither was finalized. Although the banking agencies' 2010 guidance remains fully intact – and firms have made further changes to

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[22] *See* Resolution Plans Required, 76 Fed. Reg. 67323 (Nov. 1, 2011), available at https://www.govinfo.gov/content/pkg/FR-2011-11-01/pdf/2011-27377.pdf.
[23] *See* Resolution Plans Required, 84 Fed. Reg. 59194 (Nov. 1, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-01/pdf/2019-23967.pdf.
[24] Pub. L. 111-203 (July 21, 2010), available at https://www.govinfo.gov/content/pkg/PLAW-111publ203/pdf/PLAW-111publ203.pdf.
[25] *See* Guidance on Sound Incentive Compensation Policies, 75 Fed. Reg. 36395 (June 25, 2010), available at https://www.govinfo.gov/content/pkg/FR-2010-06-25/pdf/2010-15435.pdf.
[26] *See* Federal Reserve, OCC, OTS, FDIC Issue Final Guidance on Incentive Compensation (June 21, 2010), available at https://www.federalreserve.gov/newsevents/pressreleases/bcreg20100621a.htm.
[27] Section 956(c) of the Dodd-Frank Act specifically requires the regulators to "take into consideration standards described in section 39(c) of the FDI Act" (12 U.S.C. 2 1831p–1 and 12 U.S.C. 1831p– 9 1(c)).in establishing standards.
[28] *See* Incentive-Based Compensation Arrangements, 76 Fed. Reg. 21170 (Apr. 14, 2011), available at https://www.govinfo.gov/content/pkg/FR-2011-04-14/pdf/2011-7937.pdf.
[29] *See* Incentive-Based Compensation Arrangements, 81 Fed. Reg. 37670 (June 10, 2016), available at https://www.govinfo.gov/content/pkg/FR-2016-06-10/pdf/2016-11788.pdf.

their incentive compensation policies following this guidance – the agencies continue to engage in discussions regarding how best to implement the statute.

5. Volcker Rule

One of the most challenging post-crisis reforms for regulators and institutions to implement has been the Volcker Rule, which restricts banks from engaging in proprietary trading and from owning hedge funds and private equity funds. As written and originally implemented, the rule was so complex that it required regulators to issue 21 responses to frequently asked questions (FAQs) within three years of its adoption. This complexity has resulted in uncertainty and unnecessary burden, especially for smaller, less-complex institutions.

To address some of these concerns, EGRRCPA exempted from the Volcker Rule all banks below $10 billion in consolidated assets that do not engage in significant trading activity. Earlier this year, the five agencies responsible for implementing the Volcker Rule finalized a rule[30] to codify this exemption.

In addition, the agencies issued a larger set of revisions[31] to the Volcker Rule – sometimes referred to as "Volcker 2.0" – that tailor the rule's compliance requirements by establishing three tiers of banking entities based on level of trading activity for purposes of applying compliance requirements: (1) significant trading assets and liabilities, (2) moderate trading assets and liabilities, and (3) limited trading assets and liabilities.

Banking entities with significant trading assets and liabilities, which hold approximately 93 percent of total trading assets and liabilities across the U.S. banking system, will continue to be subject to the most stringent compliance standards. The revisions also provide greater clarity, certainty, and objectivity about what activities are prohibited under the Volcker Rule. These changes, which apply specifically to the Volcker Rule's proprietary trading prohibition, will improve compliance with the rule and reduce unnecessary burdens while maintaining the statutory prohibition on proprietary trading by covered banking entities.

Additionally, the agencies are currently working on a forthcoming proposal to address the overly broad restrictions associated with covered funds, which the agencies plan to issue for comment as soon as possible.

6. Appraisals

Last year, the FDIC, FRB, and OCC finalized a rule[32] that raised the appraisal threshold for federally related commercial real estate transactions from $250,000 – the threshold

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[30] *See* Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests In, and Relationships With, Hedge Funds and Private Equity Funds, 84 Fed. Reg. 35008 (July 22, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-07-22/pdf/2019-15019.pdf.

[31] *See* Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 84 Fed. Reg. 61974 (Nov. 14, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-14/pdf/2019-22695.pdf.

[32] *See* Real Estate Appraisals, 83 Fed. Reg. 15019 (Apr. 9, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-04-09/pdf/2018-06960.pdf.

established in 1994 – to $500,000. Earlier this year, the agencies finalized a related rule[33] that raised the appraisal threshold for federally related residential real estate transactions from $250,000 – also the threshold established in 1994 – to $400,000. These changes balance current market realities and price appreciation, including needs in rural communities where access to appraisal services can be limited, with the need to ensure the safety and soundness of our institutions.

C. Enhancing Resolution Preparedness

In addition to supervising small and medium-sized banks and appropriately tailoring regulations for banks of all sizes, one of the FDIC's most important responsibilities for strengthening the banking system is ensuring that, in the event of financial distress, large and complex banks are resolvable in a rapid and orderly manner under the Bankruptcy Code. In furtherance of this critical goal, we have taken several steps to enhance resolution preparedness.

1. New FDIC Division

Earlier this year, we announced the centralization of our supervision and resolution activities for the largest and most complex banks in a new Division of Complex Institution Supervision and Resolution (CISR).[34] This move is more than just an organizational realignment. Rather, combining these key functions will create a stronger, more coherent approach for bank resolution and supervision by enabling us to take a more holistic approach. On the supervision side, CISR is responsible for overseeing banks with more than $100 billion in assets for which the FDIC is not the primary federal regulator. On the resolution side, CISR is responsible for executing the FDIC's resolution planning mandates for these institutions. In conjunction with this new division, we established a new position – Deputy to the Chairman for Financial Stability – to focus on financial stability issues, including the resolvability of large banks.

2. Cross-Border Cooperation

Given the cross-border activities of the largest, most systemically important banks, we continue to work with our international counterparts on resolution preparedness. For example, earlier this year we hosted a series of exercises with senior officials in the United States, United Kingdom, and European Banking Union to strengthen coordination on cross-border resolution and enhance understanding of one another's resolution regimes for GSIBs.[35] In addition, we have established Crisis Management Groups that have brought together firms and home and host authorities to discuss resolution planning. We have developed information-sharing arrangements to support this work and engaged in a number of international operational exercises to test and improve our readiness.

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[33] *See* Real Estate Appraisals, 84 Fed. Reg. 53579 (Oct. 8, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-10-08/pdf/2019-21376.pdf.

[34] *See* FDIC to Centralize Key Aspects of Its Large, Complex Financial Institution Activities (June 27, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19056.html.

[35] *See* U.S., European Banking Union, and UK Officials Meet for Planned Coordination Exercise on Cross-Border Resolution Planning (Apr. 9, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19033.html.

D. Assessing New and Emerging Risks

The FDIC has a long tradition of identifying, analyzing, and addressing key risks in the economy, financial markets, and the banking industry. Through numerous publications, including an annual *Risk Review*, we advance the goal of strengthening the banking system by highlighting risks at a stage when policymakers, bankers, and the public can act to mitigate their scope and impact.

1. Cyber and Resiliency

The FDIC continues to actively monitor cybersecurity risks in the banking industry. FDIC examiners conduct examinations to ensure that financial institutions are appropriately managing their exposure to cybersecurity risk. Our examiners verify that bank management has considered how cyber events could disrupt their operations and has designed resilience into their operations.

Working with our regulatory partners through the Federal Financial Institutions Examination Council (FFIEC), we recently issued an updated *Business Continuity Management* booklet, which describes key principles and practices in this area.[36] The booklet also helps examiners to evaluate the adequacy of an entity's business continuity management program and to determine whether management adequately addresses risks related to the availability of critical financial products and services. The FDIC will continue to engage with other regulators and the private sector to monitor and respond to the risks posed by cyber threats.

2. Bank Secrecy Act/Anti-Money Laundering (BSA/AML)

BSA/AML laws and regulations are a vital component of U.S. efforts to prevent unlawful financial transactions that help fund criminals, terrorists, and other illicit actors. As these actors use increasingly sophisticated methods to conceal their transactions in an evolving financial, technological, and regulatory landscape, the FDIC continues to work with other regulators and the law enforcement and intelligence communities to help supervised institutions respond to these threats.

At the same time, BSA/AML laws and regulations impose significant compliance costs on the entire system and on the individual institutions that shoulder the reporting burdens. For example, although the information gathered by suspicious activity reports (SARs) can be useful, it can be burdensome for institutions – particularly community banks – to file SARs. Federal regulatory agencies are working to develop better ways to communicate the value of SARs to the bankers that incur the reporting cost. The government also must continue to examine the rules it imposes to ensure that the system is effective and the obligations imposed on institutions are not unduly burdensome. It is also essential that we support the use of technology to both prevent illicit activity and to strengthen the collaboration among banks, regulators, and the law enforcement and intelligence communities.

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[36] *See* FDIC FIL-71-2019, *Updated FFIEC IT Examination Handbook* – Business Continuity Management *Booklet* (Nov. 14, 2019), available at https://www.fdic.gov/news/news/financial/2019/fil19071.html.

To advance the parallel goals of cost effectiveness and greater system-wide efficiency, the FDIC, FRB, OCC, NCUA, and the U.S. Department of Treasury's Financial Crimes Enforcement Network (FinCEN) jointly issued a statement[37] to address instances in which banks may decide to enter into collaborative arrangements to share resources to manage their BSA/AML obligations more efficiently and effectively. For example, banks use such arrangements to pool human, technology, or other resources to reduce costs, increase operational efficiencies, and leverage specialized expertise. In addition, the FDIC, FRB, OCC, NCUA, and FinCEN issued a statement[38] to encourage banks to consider, evaluate, and, where appropriate, responsibly implement innovative approaches to meet their BSA/AML obligations. The agencies recognized that innovation has the potential to help banks address these risks.

3. Leveraged Lending and Corporate Debt

Nonfinancial corporate debt as a share of gross domestic product (GDP) has reached a record level of 49.6 percent.[39] The increase has been driven by corporate bonds and leveraged loans, which have grown faster than other types of corporate debt. Although banks do not hold a significant amount of corporate bonds, direct bank exposure to corporate debt is concentrated in leveraged loans, collateralized loan obligations (CLOs), commercial and industrial loans, and commercial mortgages. In addition, indirect exposures, such as those arising from loans to CLO arrangers, could transmit stress from the corporate sector into the banking system. The FDIC is carefully monitoring these risks. We recently published a paper[40] discussing the growth in corporate debt and examining bank exposure to the growth of leveraged loans and continue to engage with other regulatory agencies on this issue.

4. Growth in Nonbank Mortgage Origination and Servicing

As the FDIC remains vigilant to the risks facing banks, we also monitor the evolution of the financial system, including the migration of certain financial activities to nonbanks. Perhaps the most prominent example of this shift has been in mortgage origination and servicing. We recently published a paper[41] analyzing this dynamic and associated risks. Among other things, the paper finds that the growth of nonbanks in mortgage origination and servicing has largely been attributed to the rapid expansion by nonbanks, mortgage-focused business models and technological innovation of nonbanks, litigation regarding financial crisis-era legacy portfolios at the largest bank originators, large bank sales of legacy servicing portfolios, and changes to the capital treatment of mortgage servicing assets applicable to banks. As regulators and

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[37] *See* FDIC FIL-55-2018, *Bank Secrecy Act: Interagency Statement on Sharing Bank Secrecy Act Resources* (Oct. 3, 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18055.html.

[38] *See* FDIC FIL-79-2018, *Bank Secrecy Act: Interagency Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing* (Dec. 3, 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18079.html.

[39] *See* FDIC Annual Publication Examines Potential Credit and Market Risks (July 30, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19070.html.

[40] *See* Leveraged Lending and Corporate Borrowing: Increased Reliance on Capital Markets, With Important Bank Links, available at https://www.fdic.gov/bank/analytical/quarterly/2019-vol13-4/fdic-v13n4-3q2019-article2.pdf.

[41] *See* Trends in Mortgage Origination and Servicing: Nonbanks in the Post-Crisis Period, available at https://www.fdic.gov/bank/analytical/quarterly/2019-vol13-4/fdic-v13n4-3q2019-article3.pdf.

policymakers seek to better understand the implications of this migration, we must consider both the benefits and the risks.

E. Creating the Workforce of the Future

It goes without saying that the FDIC's ability to fulfill its mission depends on having an experienced, knowledgeable, and agile workforce. To this end, I am honored to work alongside 6,000 dedicated FDIC employees who come to work every day focused on protecting consumers and strengthening the banking system. As banks have evolved with the use of new technology and delivery channels, however, so should the FDIC's workforce. In order to maintain and reinforce the quality of our workforce – and improve its diversity – in this constantly changing environment, we have taken several steps I would like to highlight.

1. Retention

We are seeking to bolster retention by striving to reduce our examiners' travel time, which is one of the primary reasons examiners leave the agency. When I joined the FDIC, safety and soundness examiners spent an average of 89 nights per year away from home. We are striving to reduce that number, and our supervision modernization efforts will help. Employing better technology provides our team the flexibility to perform significant portions of the examination off-site, whether at home while teleworking or in a local field office. Using enhanced technology will help us strike the right balance between on-site and off-site supervision activities, thereby providing better work-life balance for employees and reducing the supervisory burden for institutions.

2. Recruiting

To support our supervision modernization efforts, we looked at how to build the workforce of the future. Our goal is to attract, retain, and promote a diverse and engaged workforce with the knowledge, skills, and abilities to effectively execute the mission of the FDIC, keeping pace with industry changes. Examiners represent about one-third of our workforce and are tasked with performing the core business function of the agency.

Until recently, we typically hired generalists into a commissioned examiner training program. That program did not meet our business needs; attrition outpaced our commissioning process, the protracted speed-to-commissioning time resulted in significant attrition, and we were challenged to get our work done.

This year, we pulled together a team of executives to conduct a review of our entry-level examiner hiring and corporate perspective training to recommend changes to improve efficiency and effectiveness. We changed the way we recruit, hire, and train to meet the needs of a changing industry and workforce and to speed the time to commission by up to one year.

3. Specialists

Earlier this year, the FDIC established a new office of innovation, the FDIC Tech Lab (FDiTech), with a focus on how to best utilize technology to meet consumer demands while maintaining safety, soundness, and consumer protection. The success of this office will depend on the caliber of its personnel. We are seeking a wide range of technologists to join the agency, including a Chief Innovation Officer, data scientists, process engineers, software developers, and network security experts who can reshape our supervisory approach in a rapidly evolving digital world.

We are also supplementing our examiner cadre with specialists and analysts in both information technology and loan review. These individuals will complement our workforce by providing assistance on critical areas of the examination. Although they will never replace commissioned examiners as our primary hiring target, they will contribute significantly to our supervision program.

4. Diversity

My personal and professional experiences have underscored the importance of a workplace that is free from discrimination and that supports diversity and inclusion. In furtherance of the FDIC's longstanding commitment to diversity and inclusion, we have created an executive-level taskforce on diversity. The taskforce will help to ensure our recruiting resources, hiring decisions, interviewing processes, retention efforts, and advancement pools reflect a purposeful and intentional effort to leverage diversity to maintain a high-performing examination workforce.

The racial, ethnic, and gender diversity of the FDIC workforce continues a steady increase since 2010 with minority representation at nearly 30 percent and with women comprising nearly 45 percent of permanent employees. We have also continued our efforts to promote the participation of Minority and Women-Owned Businesses in FDIC contracting actions. We will work to consistently improve the representation of women and minorities at all levels of the agency and seamlessly integrate veterans and people with disabilities. We will continue to foster an environment without barriers in which all employees feel welcomed, valued, respected, and engaged.

5. New Compensation Agreement and New Benefits

Earlier this year, the FDIC and the National Treasury Employees Union (NTEU) reached a new compensation agreement that includes two significant new benefits to enhance work-life balance for employees.

First, the FDIC will provide six weeks of paid parental leave for the birth, adoption, or foster care of a child.[42] This benefit, which will be in addition to any leave entitlement under the Family and Medical Leave Act, will enable growing families to thrive and help to ensure that no

[42] *See* FDIC Announces New Paid Parental Leave Benefit for Employees (Oct. 9, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19089.html.

FDIC employee feels forced to choose between work and family. I am proud that the FDIC is a leader in this space as one of the first federal government agencies to offer this benefit.

Second, the agreement calls for a Pilot Student Loan Repayment Program, which will target commissioned examiner employees over a three-year period. During these three years, up to 100 employees each year will be eligible to have their student loans paid directly, up to $500 per month for a total of up to $18,000 per employee. The pilot is designed to provide meaningful financial assistance to employees and contribute to FDIC retention goals. If successful, the FDIC will consider expansion of the program to other categories of positions with recruitment or retention challenges.

In addition to these work-life benefits, the agreement includes compensation increases for the next three years and shifts a portion of an employee's annual pay increase to a bonus component, which will help the FDIC reward its highest performers in a sustainable and fiscally responsible manner. To improve performance management and support the new bonus component of pay, the agreement also provides for a simplified, two-level performance management system, which will replace the current five-level rating system. The new system will be designed to enhance communication between employees and their supervisors, and it will also help identify and reward outstanding performance under the new bonus structure.

III. Ensuring That FDIC-Supervised Institutions Can Meet the Needs of Consumers and Businesses

Economic growth across the nation is predicated on the ability of banks to provide safe and secure financial products and services to consumers and businesses. Although modernizing our supervisory and enforcement programs and tailoring regulations based on an institution's risk profile are matters of good government and steps toward a stronger banking system, there are certain areas in which the needs of consumers and businesses must be addressed by more comprehensive reforms.

I have embarked on a 50-state listening tour to hear from banks directly about their challenges and to learn about the needs of the consumers and businesses that banks serve. At the outset of this effort, I emphasized the need to reverse the trend of having those affected by our regulations come to Washington to have their voices heard, but instead to meet them on their home turf. With 26 state visits, I am now more than halfway through this listening tour, which has provided valuable feedback and has underscored the importance of seeking perspectives outside of the "beltway." The following issues represent an attempt to address some of the concerns that have been brought to our attention.

A. Brokered Deposits and Interest Rate Caps

The FDIC is undertaking a comprehensive review of our longstanding regulatory approach to brokered deposits and the interest rate caps applicable to banks that are less than well capitalized. Since the statutory brokered deposit and rate restrictions applicable to less than well capitalized banks were put in place in 1989 (and amended in 1991), the financial services industry has seen significant changes in technology, business models, and products. In February,

we issued an advance notice of proposed rulemaking (ANPR)[43] to seek public comment on all aspects of these regulations.

After considering feedback from the ANPR, we expedited the interest rate cap component of this review and proposed a rule[44] that would amend the methodology for calculating the national rate and national rate cap for specific deposit products. Under the proposal, the national rate cap for particular products would be set at the higher of the 95th percentile of rates paid by insured depository institutions (IDIs) weighted by each institution's share of total domestic deposits, or the proposed national rate plus 75 basis points. The proposed rule would also greatly simplify the current local rate cap calculation and process by allowing less than well capitalized institutions to offer up to 90 percent of the highest rate paid on a particular deposit product in the institution's local market area.

We have also been working to propose a rule regarding our brokered deposits framework. We are preparing an updated framework with several goals in mind, including encouraging innovation to allow banks to reach customers using emerging technology and through new channels, minimizing risk to the DIF, consistency with the statute, and establishing a transparent, consistent process. We expect to issue that proposal later this month.

B. CRA Regulations

The regulations implementing the CRA have not been updated in 20 years. During this period, the banking industry has undergone transformative changes. As the industry continues to evolve, many stakeholders believe that the current regulations implementing the CRA do not fully achieve their statutory purpose (*i.e.*, encouraging banks to help meet the credit needs of the communities they serve, including low- and moderate-income areas). As part of an effort to update these regulations, the OCC issued an ANPR[45] last year seeking feedback on how the CRA could be modernized to improve the effectiveness of the law and provide much needed clarity to financial institutions on what activities receive CRA "credit." The banking agencies have reviewed the comment letters received by the OCC, and the FDIC is currently engaged with the OCC and FRB on how to revise the regulatory framework that can help meet these dual goals.

C. Small-Dollar Lending

According to a recent FRB study, nearly four in 10 households cannot cover a $400 emergency expense with cash.[46] Moreover, according to our unbanked and underbanked study,

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[43] *See* Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions, 84 Fed. Reg. 2366 (Feb. 6, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-02-06/pdf/2018-28273.pdf.
[44] *See* Interest Rate Restrictions on Institutions That Are Less Than Well Capitalized, 84 Fed. Reg. 46470 (Sep. 4, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-09-04/pdf/2019-18360.pdf.
[45] *See* Reforming the Community Reinvestment Act Regulatory Framework, 83 Fed. Reg. 45053 (Sept. 5, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-09-05/pdf/2018-19169.pdf.
[46] *See* Federal Reserve Board Report on the Economic Well-Being of U.S. Households in 2017 (May 2018), available at https://www.federalreserve.gov/publications/files/2017-report-economic-well-being-us-households-201805.pdf.

over 20 million households in America are underbanked and over 8 million are unbanked.[47] While some banks offer small-dollar lending to help those in need, many banks have chosen not to offer such products, in part, due to regulatory uncertainty.[48] As a result, many families rely on nonbank providers to cover these emergency expenses, or their needs go unmet. To solicit feedback on these products and consumer needs, the FDIC issued a request for information[49] last year to learn more about small-dollar credit needs and concerns. We have reviewed more than 60 comments and are reviewing our existing guidance and policies to ensure that they do not impose impediments to banks considering the extension of responsible small-dollar credit to consumers.

D. Initial Margin

In the aftermath of the financial crisis, Congress mandated that regulators establish capital and margin requirements for non-cleared swaps. In 2015, the banking agencies adopted regulations implementing these requirements.[50] In addition to requiring the exchange of initial and variation margin with unaffiliated counterparties, the rule requires that IDIs collect initial and variation margin from affiliates. After carefully reviewing these regulations, the agencies issued a proposal[51] to repeal the requirement that IDIs collect initial margin from affiliates while retaining the requirement that IDIs exchange variation margin with affiliates. The proposal, which would harmonize the banking agencies' framework with the rules finalized by international regulators, the SEC, and the CFTC, does not change the margin requirements for transactions with unaffiliated counterparties, but covers only transactions between an IDI and its affiliates. The removal of the inter-affiliate initial margin requirement would provide banking organizations with additional flexibility for internal allocation of collateral. We believe that such risk management practices often improve the safety and soundness of a covered swap entity.

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[47] *See* 2017 FDIC National Survey of Unbanked and Underbanked Households, available at https://www.fdic.gov/householdsurvey/2017/2017report.pdf. A household is classified as unbanked if no one in the household has a checking or savings account. A household is classified as underbanked if it has a checking or savings account and used one of the following products or services from an alternative financial services provider in the past 12 months: money orders, check cashing, international remittances, payday loans, refund anticipation services, rent-to-own services, pawn shop loans, or auto title loans.

[48] The FDIC, FRB, and OCC have taken separate approaches to small-dollar lending at the institutions they regulate. *See* FDIC Issues Final Guidance Regarding Deposit Advance Products (Nov. 21, 2013), available at https://www.fdic.gov/news/news/press/2013/pr13105.html; FDIC FIL-50-2007, *Affordable Small-Dollar Loan Guidelines* (June 19, 2007), available at: https://www.fdic.gov/news/news/financial/2007/fil07050.pdf; OCC Bulletin 2018-14, *Core Lending Principles for Short-Term, Small-Dollar, Installment Lending* (May 23, 2018), available at: https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-14.html; *Federal Reserve Statement on Deposit Advance Products* (April 25, 2013), available at: https://www.federalreserve.gov/supervisionreg/caletters/caltr1307.htm.

[49] *See* Request for Information on Small-Dollar Lending, 83 Fed. Reg. 58566 (Nov. 20, 2018), available at https://www.govinfo.gov/content/pkg/FR-2018-11-20/pdf/2018-25257.pdf.

[50] *See* Margin and Capital Requirements for Covered Swap Entities, 80 Fed. Reg. 74840 (Nov. 30, 2015), available at https://www.govinfo.gov/content/pkg/FR-2015-11-30/pdf/2015-28671.pdf.

[51] *See* Margin and Capital Requirements for Covered Swap Entities, 84 Fed. Reg. 59970 (Nov. 7, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-07/pdf/2019-23541.pdf.

E. Minority Depository Institutions

Preserving and protecting minority depository institutions (MDIs) remains a priority for the FDIC, and we have undertaken a number of initiatives to support MDIs, with a specific emphasis on partnerships. In June, we hosted a roundtable in Washington with 10 large banks and seven minority banks.[52] Each participant outlined in advance the types of partnerships they were seeking and, during the roundtable, MDIs and large banks met one-on-one to explore partnership opportunities. Following the roundtable, several large banks expressed appreciation for the opportunity to find mutually beneficial partnerships and eagerness to begin working with MDIs to help them have a greater impact on their communities. One of the large banks drafted a proposal to expand its partnerships beyond the seven MDIs at the roundtable, and one of the MDIs reported that it had partnered with three larger banks from the event on a variety of technical assistance efforts. This is exactly the type of outcome we were hoping for, and the FDIC stands ready to serve as a resource for any MDI that wants to partner with large banks – or any other bank that wants to partner with MDIs – and has questions about next steps. Based on the success of the June event, the FDIC held similar roundtables in Atlanta and Chicago this year and plans to host additional events in the Midwest and on the West Coast next year.

In addition, the FDIC appointed additional minority bankers to our CBAC and established a new MDI Subcommittee to the CBAC to highlight MDI efforts in their communities and to provide a platform for MDIs to exchange best practices.[53]

Like many other community banks, MDIs face challenges from the evolving financial services landscape. The boards and management of institutions must successfully navigate economic, technological, competitive, and regulatory circumstances to be profitable and serve their communities. For many MDIs, these challenges can be amplified if they serve economically distressed communities that do not fully recover during economic growth cycles. As the supervisor of nearly 100 MDIs – two-thirds of all MDIs nationwide – the FDIC is committed to promoting and sustaining the vibrant role these banks play in their communities. Increasing our engagement with MDIs enables us to understand their unique needs and provide tools and resources so they can help create jobs, grow small business, and build wealth in their communities.

IV. Fostering Technology Solutions and Encouraging Innovation at Community Banks

While the modernization efforts I have discussed are critical, perhaps no issue is more important – or more central to the future of banking – than innovation. Technology is transforming the business of banking, both in the way consumers interact with their bank and the way banks do business. I recently discussed several important ways technology could further transform banking, including digitization, data access and open banking, machine learning and

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[52] *See* FDIC Hosts Roundtable on Collaborations with Minority Depository Institutions (June 27, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19057.html.

[53] *See* FDIC Hosts Interagency Conference Focusing on Minority Depository Institutions (June 25, 2019), available at https://www.fdic.gov/news/news/press/2019/pr19054.html.

artificial intelligence, and personalization.[54] Given these and other developments, regulators cannot play "catch up," but must be proactive in engaging with all stakeholders, including banks, consumer groups, trade associations, and technology companies to understand and help foster the safe adoption of technology across the banking system, especially at community banks.

A. Encouraging Innovation and Partnerships

Banks know that if they do not innovate, they will lose in the long run. At the FDIC, we have asked, if banks know that they must innovate, why more community banks are not developing or utilizing new technologies.

We have received two principal explanations: (1) cost and (2) regulatory uncertainty. In many cases, the cost to innovation is prohibitively high for community banks, which often lack the expertise, information technology, and research and development budgets to independent develop and deploy their own technology. As a result, partnerships with financial technology companies, or fintechs, that have already developed, tested, and rolled out new technology are often critical for these banks and their communities. Yet, if our regulatory framework does not evolve with technological advances in a manner that enables partnerships between banks and fintechs, such innovation may not occur at community banks.

Regulatory modernization is not optional for the FDIC. We must lay this foundation because the survival of our community banks depends on it. These banks face challenges from industry consolidation, economies of scale, and competition from their community bank peers, larger banks, credit unions, fintechs, and nonbanks lenders. My goal is for the FDIC to lay the foundation for the next chapter of banking by encouraging innovation and partnerships, allowing banks and their communities to benefit from new products and services that improve people's lives.

With this goal in mind, FDiTech, the FDIC's new office of innovation, will collaborate with community banks on how to deploy technology in delivery channels and back office operations to better serve customers. Many of the institutions we supervise are already innovating, but a broader adoption of new technologies will allow community banks to stay relevant in the increasingly competitive marketplace.

We have identified three key ways in which FDiTech can work to encourage innovation and partnerships at community banks. First, through engagement and technical assistance we can help eliminate the regulatory uncertainty that prevents some banks from adopting new technologies. Second, through tech sprints – which are designed to challenge innovators to develop technological solutions to address specific challenges – we can help encourage the market to develop technology that improves the operations of financial institutions and how the FDIC functions as a regulatory agency. Third, through pilot programs we can work with developers to pilot products and services for truly innovative technologies. Over the coming months, the FDIC will play a convening role to encourage community bank consideration of how technological developments could impact their businesses and to ensure community bank

[54] *See* FDIC Chairman Jelena McWilliams, "The Future of Banking," speech before the Federal Reserve Bank of St. Louis (Oct. 1, 2019), available at https://www.fdic.gov/news/news/speeches/spoct0119.html.

perspectives are considered in industry-led efforts to establish standards. We will also host a series of community bank-focused stakeholder roundtables on digitization, data access and ownership, machine learning and artificial intelligence, and personalization of the banking experience.

B. Reducing Regulatory Burden

As we consider these medium- to long-term ways to encourage innovation and partnerships, we have simultaneously taken important short-term steps to reduce the regulatory burden at community banks. These changes should enable innovation at community banks by allowing them to spend less time navigating complex regulatory issues and more time managing their businesses.

Last month, the FDIC, FRB, and OCC finalized a rule[55] that implements EGRRCPA by establishing a simple leverage ratio for qualifying community banks. Under the rule, qualifying banks that elect to maintain a leverage ratio of greater than 9 percent will be considered to have satisfied the generally applicable risk-based and leverage capital requirements in the agencies' capital rules and, if applicable, will be considered to have met the well-capitalized ratio requirements for purposes of section 38 of the FDI Act. Notably, the agencies estimate that over 80 percent of community banks will qualify to use the community bank leverage ratio. The rule provides meaningful regulatory compliance burden relief by allowing these banks to avoid complex risk-based capital calculations and reporting.

Earlier this year, the FDIC, FRB, and OCC finalized a separate rule[56] that implements EGRRCPA by simplifying the Call Report for community banks for the first and third calendar quarters and expanding the eligibility to file the most streamlined Call Report to include most IDIs with less than $5 billion in total assets.

V. Conclusion

Since 1933, the FDIC has played a vital role in maintaining stability and public confidence in the nation's financial system. This mission remains as critical today as it was more than 86 years ago, but if we are to achieve our mission in the modern financial environment, while still allowing the industry to evolve and innovate, the agency cannot be stagnant.

Thank you again for the opportunity to testify today, and I look forward to answering your questions.

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[55] *See* Regulatory Capital Rule: Capital Simplification for Qualifying Community Banking Organizations, 84 Fed. Reg. 61776 (Nov. 13, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-13/pdf/2019-23472.pdf.
[56] *See* Reduced Reporting for Covered Depository Institutions, 84 Fed. Reg. 29039 (June 21, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-06-21/pdf/2019-12985.pdf.

Appendix A

Status of Rulemakings under the Economic Growth, Regulatory Relief, and Consumer Protection Act

SECTION	DESCRIPTION	STATUS
103	**Appraisals** Amends the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 to exempt certain real property mortgage transactions from appraisal requirements	Final Rule published October 8, 2019
201	**Community Bank Leverage Ratio** Exempts banks with less than $10 billion in assets and that meet other requirements — including limits on off-balance sheet exposures, trading assets and liabilities, total notional derivatives exposures, and other factors — from existing risk-based capital ratio and leverage ratio requirements provided they exceed a community bank leverage ratio	Final Rule published November 13, 2019
202	**Reciprocal Deposits** Amends Section 29 of the Federal Deposit Insurance Act to except a capped amount of certain reciprocal deposits from treatment as brokered deposits for qualifying institutions	Final Rule published February 4, 2019
203, 204	**Volcker Rule** Exempts banks with less than $10 billion in assets and total trading assets and liabilities of no more than 5 percent of total consolidated assets from the Volcker Rule	Final Rule published July 22, 2019
205	**Short Form Call Reports** Requires regulations that allow reduced call reporting for the first and third quarters for certain banks with less than $5 billion in assets	Final Rule published June 21, 2019

SECTION	DESCRIPTION	STATUS
210	**Examination Cycle** Increases the size threshold for well-capitalized banks to be eligible for an 18-month examination cycle from $1 billion to $3 billion in total assets, and authorizes the banking agencies to make corresponding changes for 2-rated institutions	Final Rule published December 28, 2018
214	**HVCRE/ADC** States that the appropriate federal banking agencies may assign heightened risk weights for high-volatility commercial real estate (HVCRE) loans only to those loans that meet a statutory definition of HVCRE	Final Rule approved by FDIC Board November 19, 2019; awaiting publication in *Federal Register*
401	**Tailoring Capital and Liquidity Rules for Large Domestic and Foreign Banking Organizations** Raises the threshold for application of enhanced prudential standards to bank holding companies, including capital and liquidity rules, from $50 billion to $250 billion in total consolidated assets and allows the FRB to apply enhanced prudential standards to any bank holding company with between $100 billion and $250 billion in total consolidated assets under certain circumstances	Final Rule published November 1, 2019
401	**Resolution Plans** Raises the threshold for application of enhanced prudential standards to bank holding companies, including the requirement to file section 165(d) resolution plans, from $50 billion to $250 billion in total consolidated assets and allows the FRB to apply enhanced prudential standards to any bank holding company with between $100 billion and $250 billion in total consolidated assets under certain circumstances	Final Rule published November 1, 2019

SECTION	DESCRIPTION	STATUS
401	**Company-Run Stress Tests** Amends the requirements for company-run stress tests by: raising the threshold from $10 billion to $250 billion in assets; making the stress tests periodic rather than annual; and removing the adverse scenario (leaving intact the baseline and severely adverse sets of stress test conditions)	Final Rule published October 24, 2019
402	**Supplementary Leverage Ratio for Custodial Banks** Requires the appropriate federal banking agencies to amend their capital regulations to exempt funds of a custodial bank held at certain central banks when calculating the supplementary leverage ratio	Final Rule approved by FDIC Board November 19, 2019; awaiting publication in *Federal Register*
403	**High-Quality Liquid Assets (HQLA)** Requires the federal banking agencies to amend their liquidity coverage ratio regulations to treat municipal obligations that are "investment grade" and "liquid and readily marketable" as level 2B liquid assets not later than 90 days after enactment	Final Rule published June 5, 2019

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Statement by

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Vice Chair for Supervision

Board of Governors of the Federal Reserve System

before the

Committee on Financial Services

U.S. House of Representatives

December 4, 2019

Chairwoman Waters, Ranking Member McHenry, members of the committee, thank you for the opportunity to appear today, alongside my colleagues from the regulatory community. We join you on the cusp of a significant and shared milestone: the full and faithful implementation of Congress's efforts to improve financial regulation, in the form of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA).[1] Today, I will briefly review the steps we have taken toward this milestone; share information on the state of the banking system, from the report that accompanies my testimony; and discuss the continuing need to ensure our regulatory framework is both coherent and effective.[2]

Roughly 18 months ago, Congress passed legislation to consolidate a decade of work on financial reform, and to better tailor financial regulation and supervision to the risks of the institutions being regulated. The EGRRCPA was a specific, targeted response to the conditions facing today's banking organizations and their customers. It was also rooted, however, in long-standing congressional practice: of reviewing the work done in the immediate aftermath of a crisis; of addressing any gaps; and of ensuring that public and private resources go toward their best, most efficient use. This approach informed the Banking Acts of 1933 and 1935, on issues from shareholder liability to deposit insurance.[3] It informed the bills passed after the savings-and-loan crisis, requiring "prompt corrective action" at struggling firms and reducing the

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[1] EGRRCPA, Pub. L. No. 115-174, 132 Stat. 1296 (2018).
[2] Board of Governors of the Federal Reserve System, "Supervision and Regulation Report," November 26, 2019, https://www.federalreserve.gov/publications/files/201911-supervision-and-regulation-report.pdf.
[3] See Gary Richardson, Alejandro Komai, and Michael Gou, "Banking Act of 1935," Federal Reserve History (website), Federal Reserve Bank of Richmond, November 22, 2013, https://www.federalreservehistory.org/essays/banking_act_of_1935.

examination burden at strong ones.[4] And it continues to inform our efforts now, from the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act to today.[5]

The Board's latest *Supervision and Regulation Report*, which we published last week, confirms the current health of the banking system.

- It depicts a stable, healthy, and resilient banking sector, with robust capital and liquidity positions.
- It details stable loan performance and strong loan growth, particularly among regional banks, whose share of overall bank lending continues to grow.
- It describes steady improvements in safety and soundness, with a gradual decline in outstanding supervisory actions at both the largest and smallest organizations.
- And it identifies areas of continued supervisory focus, including operational resiliency and cyber-related risks, which are among our top priorities for the year to come.

The banking system is substantially better prepared to manage unexpected shocks today than it was before the financial crisis. Now, when the waters are relatively calm, is the right time to step back and examine the efficiency and effectiveness of our protection against future storms. With the EGRRCPA, Congress made a significant down payment on that task. In less than 18 months after the act's passage, we implemented all of its major provisions.

Earlier this year, we completed a cornerstone of the legislation to tailor our rules for regional banks, which was entirely consistent with a principle at the heart of our existing work: firms that pose greater risks should meet higher standards and receive more scrutiny. Our

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[4] See Noelle Richards, "Federal Deposit Insurance Corporation Improvement Act of 1991," Federal Reserve History (website), Federal Reserve Bank of Richmond, November 22, 2013, https://www.federalreservehistory.org/essays/fdicia.

[5] Dodd-Frank Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

previous framework relied heavily on a firm's total assets as a proxy for these risks and for the costs the financial system would incur if a firm failed. This simple asset proxy was clear and critical, rough and ready, but neither risk-sensitive nor complete. Our new rules employ a broader set of indicators, like short-term wholesale funding and off-balance-sheet exposures, to assess the need for greater supervisory scrutiny.[6] They maintain the most stringent requirements and strictest oversight for the largest, most complex organizations—the collapse of which would do the most harm.

We and our interagency colleagues also have worked on a range of measures addressed to smaller banks, with particular attention to better capturing and reflecting the characteristics of the community bank business model. These include elements of last year's legislation, and other steps we have taken in the same spirit, intended to help community banking organizations survive and thrive:

- We adjusted the scope of our supervisory assessments, our stress-testing requirements, our appraisal regulations, and the Volcker rule—all aimed at the activities of large, complex institutions, not small local banks.[7]

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[6] Board of Governors of the Federal Reserve System, "Federal Reserve Board Finalizes Rules That Tailor Its Regulations for Domestic and Foreign Banks to More Closely Match Their Risk Profiles," news release, October 10, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20191010a.htm.

[7] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies Issue Final Rule to Exempt Residential Real Estate Transactions of $400,000 or Less from Appraisal Requirements," news release, September 27, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190927a.htm; Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and Securities and Exchange Commission, "Agencies Finalize Changes to Simplify Volcker Rule," news release, October 8, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20191008a.htm; Board of Governors of the Federal Reserve System, "Federal Reserve Board Finalizes Rules That Tailor Its Regulations for Domestic and Foreign Banks to More Closely Match Their Risk Profiles," news release, October 10, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20191010a.htm; Board of Governors of the Federal Reserve System, "Federal Reserve Board Invites Public Comment on Proposal That Would Modify Company-Run Stress Testing Requirements to Conform with Economic Growth, Regulatory Relief, and Consumer Protection Act," news release, January 8, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190108a.htm; and Board of Governors of the Federal Reserve System, "Federal Reserve Board Issues Statement Describing How, Consistent with Recently Enacted EGRRCPA, the Board Will No Longer Subject Primarily Smaller, Less Complex

- We clarified our capital treatment of commercial real estate loans, which are central to the credit books of many community banks.
- We detailed our approach to anti-money-laundering exams, and our goal of prioritizing high-risk activities over routine matters.[8]
- We expanded eligibility for our small bank holding company policy statement, opening the door to simpler funding requirements for a broader range of small banking firms.[9] We also increased the scope of banks eligible for longer examination cycles.[10]
- We revised a management-interlock rule for the first time since 1996, removing a governance barrier for more small banks and their holding companies.[11]
- We made our short-form call report shorter, removing items that were often ancillary to filers' core lending activities.

Banking Organizations to Certain Board Regulations," news release, July 6, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180706b.htm.

[8] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies Propose Rule Regarding the Treatment of High Volatility Commercial Real Estate," news release, September 18, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180918a.htm; and Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Financial Crimes Enforcement Network, National Credit Union Administration, and Office of the Comptroller of the Currency, "Federal Bank Regulatory Agencies and FinCEN Improve Transparency of Risk-Focused BSA/AML Supervision," news release, July 22, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190722a.htm.

[9] Board of Governors of the Federal Reserve System, "Federal Reserve Board Issues Interim Final Rule Expanding the Applicability of the Board's Small Bank Holding Company Policy Statement," news release, August 28, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180828a.htm.

[10] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies Issue Final Rules Expanding Examination Cycles for Qualifying Small Banks and U.S. Branches and Agencies of Foreign Banks," news release, December 21, 2018, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20181221c.htm.

[11] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Agencies Issue Final Rule to Update Management Interlock Rules," news release, October 2, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20191002a.htm.

- And we finalized a new community bank leverage ratio, giving small, strong banking organizations a much simpler way to meet their capital requirements.[12]

Our goal, through this period of intense regulatory activity, has been to faithfully implement Congress's instructions. However, those instructions also speak to a broader need, and one central to our ongoing work: to ensure our regulatory regime is not only simple, efficient, and transparent, but also coherent and effective.[13]

Financial regulation, like any area of policy, is a product of history. Each component dates from a particular time and place, and it was designed, debated, and enacted to address a particular set of needs. No rule can be truly evergreen; gaps and areas for improvement will always reveal themselves over time. Our responsibility—among the most challenging and essential we have—is to address those gaps without creating new ones; to understand fully the interaction among regulations; to reduce complexity where possible, before it becomes its own source of risk; and to ensure our *entire* rulebook supports the safety, stability, and strength of the financial system.

Looking ahead, my colleagues and I are paying particular attention to coherence in our capital regime. We are reviewing public input into proposed changes to the stress capital buffer, which would simplify our regime by integrating our stress-test and point-in-time capital requirements and maintain our current strong levels of capital.[14] As we move forward, we also

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[12] Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, and Office of the Comptroller of the Currency, "Federal Bank Regulatory Agencies Issue Final Rule to Simplify Capital Calculation for Community Banks," news release, October 29, 2019, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20191029a.htm.

[13] Randal K. Quarles, "Early Observations on Improving the Effectiveness of Post-Crisis Regulation" (speech at the American Bar Association Banking Law Committee Annual Meeting, Washington, D.C., January 19, 2018), https://www.federalreserve.gov/newsevents/speech/quarles20180119a.htm.

[14] Randal K. Quarles, "Refining the Stress Capital Buffer" (speech at the Program on International Financial Systems Conference, Frankfurt, Germany, September 5, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190905a.htm; and Randal K. Quarles, "Stress Testing: A Decade of Continuity and Change" (speech at the "Stress Testing: A Discussion and Review" research conference

understand the need to thoughtfully finalize implementation of Basel III, in a way that preserves aggregate capital and liquidity levels at large banking organizations, avoids additional burden at smaller ones, and upholds our standards for transparency and due process.

We also understand the need to ensure a smooth transition away from LIBOR, and other legacy benchmark rates, so institutions can manage risks comprehensively and effectively.[15] And we understand the need for clear, consistent supervisory communication on these and other matters, which invites dialogue, reflects and reinforces our regulations and laws, and gives banks necessary transparency into supervisory views on safety and soundness.[16]

We also understand the need to thoughtfully address new financial products and technologies. Innovation has the potential to improve access to financial services, lower costs, and support the competitive health of the banking sector. Its promise, however, inevitably comes with risk—and as the financial crisis showed, risks that lie outside the banking system can have consequences within it. Our approach to innovation should be both open and careful, engaging thoughtfully with both the public and private sectors, to understand the benefits and costs that such fundamental changes can bring.

Finally, we understand the need for coherence across borders. Over the last decade, working with supervisors around the world, we have built a common understanding of the crisis, its causes, and its consequences. Now, as the full set of post-crisis reforms comes into effect, we should renew our focus on assessing their implementation and their overall impact. The

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sponsored by the Federal Reserve Bank of Boston, July 9, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190709a.htm.

[15] Randal K. Quarles, "The Next Stage in the LIBOR Transition" (speech at the Alternative Reference Rates Committee Roundtable, cohosted by the Alternative Reference Rates Committee and the New York University Stern School of Business and Its Salomon Center for the Study of Financial Institutions, New York, June 3, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190603a.htm.

[16] Randal K. Quarles, "Law and Macroeconomics: The Global Evolution of Macroprudential Regulation" (speech at the "Law and Macroeconomics" conference at Georgetown University Law Center, Washington, D.C., September 27, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190927a.htm.

financial system is truly global, and the structures and incentives that govern it are critical to its stability and resilience.[17] The regulatory community has started significant work to examine those structures and incentives as a whole, from their effect on "too-big-to-fail" subsidies to their impact on market fragmentation.[18] We are participating actively in that work, as a way to ensure the global financial system supports, rather than inhibits, American growth.

I appreciate the chance to discuss this work with you, and I look forward to answering your questions. Thank you.

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[17] Randal K. Quarles, "Government of Union: Achieving Certainty in Cross-Border Finance" (speech at the Financial Stability Board Workshop on Pre-Positioning, Ring-Fencing, and Market Fragmentation, Philadelphia, September 26, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20190926a.htm.

[18] Randal K. Quarles, "The Financial Stability Board at 10 Years—Looking Back and Looking Ahead" (speech at the European Banking Federation's European Banking Summit, Brussels, Belgium, October 3, 2019), https://www.federalreserve.gov/newsevents/speech/quarles20191003a.htm; see also, Financial Stability Board, "FSB Launches Evaluation of Too-Big-to-Fail Reforms and Invites Feedback from Stakeholders," news release, May 23, 2019, https://www.fsb.org/2019/05/fsb-launches-evaluation-of-too-big-to-fail-reforms-and-invites-feedback-from-stakeholders/; and Financial Stability Board, "FSB Publishes Report on Market Fragmentation," news release, June 4, 2019, https://www.fsb.org/2019/06/fsb-publishes-report-on-market-fragmentation/.

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National Association of Federally-Insured Credit Unions

December 3, 2019

The Honorable Maxine Waters
Chairwoman
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
United States House of Representatives
Washington, DC 20515

RE: Tomorrow's Hearing on Oversight of Prudential Regulators

Dear Chairwoman Waters and Ranking Member McHenry:

I am writing on behalf of the National Association of Federally-Insured Credit Unions (NAFCU) to share our thoughts ahead of tomorrow's hearing entitled "Oversight of Prudential Regulators: Ensuring the Safety, Soundness, Diversity, and Accountability of Depository Institutions?." NAFCU advocates for all federally-insured not-for-profit credit unions that, in turn, serve over 118 million consumers with personal and small business financial service products. NAFCU and our members welcome the Committee's oversight of financial regulators.

Since the financial crisis, the credit union industry has lost over 1,500 institutions. This dramatic consolidation is due, in large part, to increased regulatory compliance requirements. We urge you to continue to work to create a regulatory environment where credit unions can grow and thrive. As we have previously communicated to you, NAFCU supports the following five tenets of a healthy regulatory environment:

- **NAFCU supports a regulatory environment that allows credit unions to grow.** NAFCU believes that there must be a regulatory environment that neither stifles innovation, nor discourages credit unions from providing consumers and small businesses with access to credit. Promoting growth-friendly regulation includes protecting the current tax status of credit unions. It also includes the ability of credit unions to establish healthy fields of membership that are not limited by outdated laws or regulatory red tape. All credit unions should have the ability to add underserved areas to their fields of membership. Revised regulations may also be necessary to address structural barriers to growth. For example, credit unions need modernized capital standards that reflect the realities of the 21st century financial marketplace, such as the ability to issue supplemental capital. Additionally, there must be a housing finance system that works for credit unions.

- **NAFCU supports appropriate, tailored regulation for credit unions and relief from growing regulatory burdens.** Credit unions are swamped by unabated regulatory burden from the Consumer Financial Protection Bureau (CFPB) and other regulatory entities, often from rules that are targeting bad actors and not community institutions. NAFCU supports the adoption of cost-benefit analysis in the rulemaking process to ensure that positive regulations may be easily implemented and negative ones may be quickly eliminated. NAFCU also believes that enforcement orders from regulators should not take the place of regulation or agency guidance to provide clear rules of the road. This NAFCU priority includes seeking regulatory relief and reform that allows credit unions to better serve their members. This includes changes to modernize the Federal Credit Union Act, such as giving the National Credit Union Administration (NCUA) authority and flexibility to set longer loan maturity limits, improving credit union investment options, and updating outdated statutory credit union governance provisions found in the Act, including the ability for credit unions to deal with threats to the institution in a timely manner.

- **NAFCU supports a fair playing field.** NAFCU believes that credit unions should have as many opportunities as banks and non-regulated entities to provide provident credit to our nations' consumers. NAFCU wants to ensure that all similarly situated depositories and lenders follow the same rules of the road

and unregulated entities, such as predatory payday lenders, do not escape oversight. We also believe that there should be a federal regulatory structure for non-bank financial services market players that do not have a prudential regulator, including emerging fintech companies. Additionally, retailers and others who handle personal financial information should be held responsible for protecting that information. Retailers should also pay their share for costs associated with data breaches and for access to a reliable and secure national payments system.

- **NAFCU supports government transparency and accountability.** NAFCU believes that regulators need to be transparent in their actions, with the opportunity for public input, and should respect possible different viewpoints. We believe a bipartisan commission is the best form of regulatory governance structure for independent agencies, and all stakeholders should be able to provide feedback in the regulatory process.

- **NAFCU supports a strong, independent NCUA as the primary regulator for credit unions.** NAFCU believes that the NCUA is the sole regulator equipped with the requisite knowledge and expertise to regulate credit unions due to their unique nature. The current structure of the NCUA, including a three-person board, has a track record of success. The NCUA should be the sole regulator for credit unions and continue to work with other regulators on joint rulemaking and other initiatives when appropriate. Congress should make sure that the NCUA has the tools and powers that it needs to effectively regulate credit unions. However, NAFCU does not support the NCUA expanding its regulatory and examination authority beyond credit unions. We believe the NCUA should focus its resources on regulating and examining credit unions, rather than non-credit union third parties where it may not have the expertise or where there may be duplicative regulatory efforts.

In addition to these five tenets of a healthy regulatory environment, NAFCU would like to emphasize several challenging regulatory issues that we hope Chairman Hood and the NCUA Board will address:

- **Exam Modernization:** NAFCU generally supports the NCUA's commitment to modernizing its examination process so long as it reduces burdens on credit unions. Considering that credit unions continue to struggle with procedural inconsistencies and other exam-related issues, NAFCU advocates that the NCUA should prioritize its examination modernization initiatives to standardize examinations and relieve burdens, including the Flexible Examination Pilot Program (FLEX) or offsite examination procedures and the Virtual Examination Program. In particular, NAFCU urges the NCUA to use its authority to expand eligibility for an extended 18-month exam cycle for all well-run, low-risk credit unions. Banks already have increased access to extended exam cycles as authorized by Congress through the Economic Growth, Regulatory Relief, and Consumer Protection Act last year. NAFCU is pleased to see advancements in the implementation of the Enterprise Solution Modernization (ESM) program, which includes the replacement of the Automated Integrated Regulatory Examination System (AIRES) with the new Modern Examination and Risk Identification Tool (MERIT) system. Successful deployment of this new platform could provide cost savings for both credit unions and examiners. NAFCU supports the modernization of the agency's legacy AIRES system with a new platform capable of sharing data in real-time. This new platform could provide substantial efficiencies and help to facilitate more virtual examinations. However, NAFCU asks the NCUA to balance enhanced monitoring with respect for credit union autonomy – increased communication between examiners and credit union management to support virtual supervision should not interfere with day-to-day operations. We hope to see the agency leverage advancements in technology to reduce the length of exams, improve consistency, and reduce the overall burden on credit unions.

- **Risk-Based Capital (RBC) Rule:** NAFCU and its member credit unions support a fair capital system for all federally-insured credit unions that both provides true risk-based capital and access to supplemental capital. In October 2015, the NCUA adopted the RBC rule for federally insured, natural-person credit unions to create a two-tier risk-based capital system. The rule made significant changes to the NCUA's capital adequacy rules

and was to take effect on January 1, 2019. In October 2018, the NCUA finalized a rule amending its 2015 RBC rule to delay the implementation date by one year to January 1, 2020 and increase the threshold level for coverage under the RBC requirements from $100 million to $500 million by amending the definition of a "complex" credit union. In June 2019, the NCUA proposed to delay the effective date of both the 2015 and 2018 final rules until January 1, 2022 to allow the agency more time to consider whether to: (1) develop regulatory and supervisory standards to address asset securitization; (2) propose and finalize a rule to allow certain forms of subordinated debt to qualify as capital for RBC purposes; and (3) integrate the equivalent of a community bank leverage ratio (CBLR) into the NCUA's capital standards. NAFCU urges the NCUA to finalize this delay and to permanently grandfather "excluded goodwill" and "excluded other intangible assets" in the RBC calculation. In summary, in any RBC regime, NAFCU has one key tenet that needs to exist: capital must be sufficient to protect the institution, but not so restrictive as to provide a competitive disadvantage or curtail lending.

- **Current Expected Credit Loss (CECL) Standard:** The Financial Accounting Standards Board's (FASB) CECL standard remains a major concern for credit unions. The CECL standard is the most significant change in accounting rules to hit the financial services industry in decades. NAFCU believes that there is a fundamental misalignment between FASB's objectives in developing the CECL standard and the credit union industry. As not-for-profit member-owned cooperatives, credit unions stand to be severely disadvantaged by this new standard and could be forced to curtail certain types of lending because of this standard. NAFCU has urged FASB to reconsider its approach to this proposal and provide an exemption for credit unions because the credit union industry was not responsible for the market conditions that caused the financial crisis. NAFCU appreciates FASB delaying implementation of the standard until 2023 for not-for-profits, including credit unions, but a delay is not enough. We ask the Committee to work with regulators such as the NCUA to come up with solution so that credit unions and their 118 million members are not harmed by, and have the resources necessary to understand, this new standard.

Finally, NAFCU asks the Committee to support several bipartisan pieces of legislation that are consistent with NAFCU's five tenets of a healthy regulatory environment and would help credit unions to better serve American consumers:

- **H.R. 1661, legislation to provide the NCUA Board flexibility to increase loan maturities.** The Federal Credit Union Act has a general statutory limit on federal credit union loans of 15 years, with a limited number of exceptions, such as mortgage loans for a primary residence. However, the Act does not have as much explicit flexibility for other types of loans and the NCUA's ability to address this through regulation may be limited. For example, many military members may purchase a home to move to when their service ends, but because it is not their current primary residence, they may be unable to obtain a loan with a term longer than 15 years. The current 15-year limit is outdated and does not conform to maturities that are commonly accepted in the market today. Language to raise the credit union general loan maturity limit from 12 to 15 years and to provide the NCUA greater flexibility to address loan maturity limits passed the House in 2006, as part of the efforts that led to P.L. 109-351, the Financial Services Regulatory Relief Act of 2006. However, the final version of the legislation only raised the limit to 15 years and did not include the language providing greater flexibility for the NCUA Board. In a rising interest rate environment, it is important that consumers have options for longer maturity products. Representatives Lee Zeldin (R-NY) and Vincente Gonzalez (D-TX) introduced H.R. 1661 on March 8, 2019, which mirrors the additional language that passed the House in 2006, and would clarify the NCUA Board's ability to establish longer maturities for other types of loans. The language does not extend any maturity limits on its own, rather just gives the NCUA Board the ability to do so if it deems necessary.

- **H.R. 2305, Veterans Members Business Loan Act.** Under the Federal Credit Union Act, a credit union's aggregate member business lending (MBL) is effectively capped at 12.25% of assets. Although credit unions

have the capital to help small businesses thrive, credit unions' ability to help stimulate the economy is frustrated by the outdated MBL cap. This bipartisan bill offered by Representatives Vicente Gonzalez (D-TX), Paul Cook (R-CA), Tulsi Gabbard (D-HI) and Don Young (R-AK) would exclude loans made to veterans from the statutory credit union MBL cap, thus improving veterans' access to necessary capital by removing regulatory barriers that hinder credit unions' ability to meet the financial needs of our nation's veterans.

- **Legislation to allow all credit unions to add underserved areas to their fields of membership.** Currently, only credit unions with multiple-group charters are able to add underserved areas to their fields of membership. NAFCU supports legislation that would allow other types of credit unions to seek the NCUA Board's approval to add such areas. Although this legislation has yet to be introduced this Congress, it was introduced last Congress as H.R. 4665, the Financial Services for the Underserved Act, by Representatives Gwen Moore (D-WI) and Paul Cook (R-CA).

In conclusion, we thank you for your leadership and ongoing oversight of prudential regulators. NAFCU is pleased to see the Committee examining ways to continue regular oversight. We urge you to also continue to consider additional measures that will help credit unions to better serve their members. We appreciate the opportunity to share our input and look forward to continuing to work with the Committee to balance minimizing regulatory burden with enhancing the safety and soundness of the credit union system. Should you have any questions or require any additional information, please contact me or Sarah Jacobs, NAFCU's Associate Director of Legislative Affairs, at 703-842-2231.

Sincerely,

Brad Thaler

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the House Financial Services Committee

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December 3, 2019

The Honorable Maxine Waters
Chairwoman
House Committee on Financial Services

The Honorable Patrick McHenry
Ranking Member
House Committee on Financial Services

Dear Chairwoman Waters and Ranking Member McHenry,

I am writing to you on behalf of the National Association of Industrial Bankers (NAIB) regarding draft legislation, the "Close the ILC Loophole Act," being proposed by Congressman Chuy Garcia (IL).

The NAIB represents most of America's state- chartered industrial loan corporations (ILCs), also known as industrial banks (IBs). Our members provide a broad array of products and services to customers and small businesses nationwide, including some of the most underserved segments of the U.S. economy.

NAIB strongly opposes the "Close the ILC Loophole Act." This bill is a misguided attempt to eliminate the strongest and safest banks in the nation (as documented by FDIC call reports). Even the title of this legislation is misleading and disparages highly regulated financial institutions that provide high-quality services to millions of Americans. The industrial bank charter is not a "loophole." Congress has explicitly authorized the industrial bank charter and has repeatedly chosen to continue its legal status, most recently during the Dodd-Frank Act deliberations. In 2012, the GAO completed an in-depth report on Industrial Banks and made no recommendations to change the law.

This legislation would not only prohibit future applications for an industrial bank charter but would also require most existing IBs to end their operations.

States have been chartering these financial institutions for more than 100 years, and Congress declared them eligible for deposit insurance over 40 years ago. Industrial banks pose no risk to the banking system. Industrial banks are subject to all of the laws, regulations and standards applicable to other banks, along with additional requirements and a prohibition on commercial checking accounts. These banks are independently managed and isolated from risks or problems that may develop from their parent company. State and federal regulators have extensive authority to regulate bank relationships with parent companies, affiliates and other "institution affiliated parties."

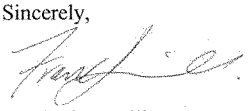
Perhaps the most important difference between an industrial bank and other banks is that a typical industrial bank owner has other businesses and assets that can support the bank. In an industry where "capital is king," most industrial banks have ready access to capital when needed, while other banks struggle to raise and seek capital in a crisis. More than 530 community and regional banks failed in the U.S. between 2008 and 2015. Almost all had a holding company regulated by the Federal Reserve that was unable to prevent the bank's failure. Only four industrial bank holding companies (IBHCs) have filed for bankruptcy in the past 40 years. In two cases the bank lost its source of business and self-liquidated at no cost to the FDIC. In one case the parent reorganized, and the bank continued operating normally. Only once did both the holding company and bank fail. By every metric relevant to safe and sound banking, industrial banks demonstrate a stronger model than banks owned by holding companies regulated by the Federal Reserve.

The so-called threat of IBs mixing banking and commerce is also an unfounded concern. Congress enacted laws to prevent conflicts of interest that prohibit an industrial bank from lending to or financing an affiliate and ensure that all transactions with affiliates are fair to the bank. The bogeyman of "big tech" is equally specious. Large technology companies do not want to be subject to holding company regulation as executed by the Federal Reserve or the FDIC. Nor do industrial banks compete with community banks, as almost all of them are specialized branchless lenders to a national market, not taking retail deposits. Industrial banks serve a niche role in the banking ecosystem by offering financing to customers, making the transaction more convenient and efficient.

The dynamics of the 21st century continue, regardless of well-meaning efforts to preserve outdated methods of credit extension. The future of banking depends on the ability to innovate, an essential feature of industrial banks. A typical industrial bank broadens and diversifies financial services in a carefully regulated way. They broaden the role of banks in the economy, a critical component of continued American vitality.

The "Close the ILC Loophole Act" would cripple the safest and most innovative financial institutions in the country while harming millions of American consumers. We respectfully ask that you oppose this legislation.

Sincerely,



Frank Pignanelli
National Association of Industrial
Bankers Executive Director

CC: The Honorable Chuy Garcia, IL-4

National Credit Union Administration

United States House Committee on Financial Services
Responses from Chairman Rodney E. Hood
Questions for the Record from Full Committee Hearing:
"Oversight of Prudential Regulators: Ensuring the Safety, Soundness and Accountability of Megabanks and Other Depository Institutions"
December 4, 2019

QFR Responses

Questions for The Honorable Rodney E. Hood, Chairman, National Credit Union Administration, from Chairwoman Maxine Waters:

NCUA Consumer Compliance

27. Chairman Hood: *What steps will the NCUA take to create and implement a dedicated consumer compliance process for the largest credit unions?*

Response:

For the very largest credit unions—those with assets of $10 billion or more—the Dodd-Frank Act granted the Consumer Financial Protection Bureau (CFPB) consumer protection authority. Currently, CFPB has this responsibility over the 10 largest credit unions.

For credit unions that the NCUA has the authority to monitor with regards to consumer compliance, the agency takes a similar risk-focused approach to consumer compliance regulation and supervision as the Federal Deposit Insurance Corporation (FDIC), Federal Reserve Board, Office of the Comptroller of the Currency (OCC), and CFPB. The risk-focused approach provides flexibility to respond to areas of greater risk or need. The agency examines consumer complaints to determine whether credit unions may be deficient in a specific area. Examiners review compliance with new laws or changes to regulations, and they are free to expand their exam scope as necessary when they detect potential non-compliance.

The agency performs separate fair lending examinations and supervision contacts and incorporates consumer compliance examination procedures within the safety and soundness examinations at every federal credit union. In addition to annually targeting specific consumer compliance concerns, we review credit unions' compliance management systems to ensure they are appropriate and sufficient to protect their members. The NCUA uses the same interagency criteria as the other federal regulators for those reviews. The NCUA assigns an overall Compliance Risk rating of low, medium, or high and incorporates the quality of the compliance management systems into its assessment of a credit union's management team and overall CAMEL rating.

Diversity and Inclusion

29. Chairman McWilliams, Vice Chairman Quarles, and Chairman Hood: *What new steps can regulators and Congress take to promote diversity and inclusion in banking?*

Response:

Promoting greater diversity and inclusion, in all respects, is fundamental to the credit union mission, the goals of this agency, and my own vision. I see this as both a moral obligation and an example of sound regulation; when we expand the population we reach with affordable financial services, we help create greater financial security for credit union members and their families as well as strengthen local economies. For credit unions, it is quite clearly a good business practice that will help them expand their reach and tailor products and services to the dynamics of their markets.

In the largest sense, we promote greater diversity and inclusion by practicing it, by bringing more people into the effort, and by making more information available to credit union leadership. For example:

- On March 3 and March 4, 2020, NCUA held two events for Minority Depository Institutions, the Freedman's Bank Forum and the National Credit Union Administration's Minority Depository Institution Forum;
- Later this year, the NCUA will host its second annual Diversity, Equity, and Inclusion Summit. The first Summit, held in November 2019, was well-attended and participant feedback was overwhelmingly positive;
- The NCUA's Office of Minority and Women Inclusion (OMWI) will participate in more financial industry events to discuss diversity, equity, and inclusion and to promote the use of the credit union diversity self-assessment; and
- OMWI will continue its practice of publishing guidebooks on diversity and inclusion topics.

The industry has also made strides in these areas. As of September 30, 2019, seven of the largest 25 credit unions (all over $6 billion in assets), or 28 percent, have a female as CEO or manager and female CEOs or managers lead forty-one, or 12.8 percent of the 319 credit unions with assets in excess of $1 billion.

Ex-Offenders with Minor Offenses Seeking Employment

30. Chairman Hood and Chairman McWilliams: *What steps can Congress take to give ex-offenders who have minor offenses a second chance and get a job in the banking or credit union industry?*

Response:

The NCUA's interpretive ruling and policy statement on offering second chances to people with minor offenses on their records was approved by the Board at its November 2019 meeting. The statement added a new *de minimis* exception for single convictions of simple misdemeanor drug possession, which we believe poses minimal risk to insured credit unions. Providing an exception to allow persons with a minor drug possession conviction to work in credit unions without the need to apply for the NCUA Board's approval should afford significant relief to certain covered individuals with drug convictions, while maintaining appropriate safeguards to ensure the new exception does not present undue safety and soundness risks to federally insured credit unions.

Congress may wish to consider whether more can be done to give former offenders with minor, nonviolent drug convictions a meaningful path to re-entry into civilian life.

The NCUA's final Interpretive Ruling and Policy Statement (IRPS) is consistent with the statutory mandate under Section 205(d) for insured credit unions to make a reasonable inquiry regarding the history of every job applicant and to take appropriate steps to avoid hiring or permitting the participation of convicted persons.

Regulatory Gaps and Big Tech

33. Vice Chair Quarles, Chairman McWilliams and Chairman Hood, *what is the current status of any review under way by your agencies regarding Facebook's Libra project, both as an individual agency and as a member of FSOC? Do you have the authority to prohibit banks and credit unions from accepting Libra as a form of deposit or payment?*

Response:
Through the NCUA's Cryptocurrency/Digital Asset Working Group, the agency is closely monitoring the implications of such technologies on credit unions and the financial industry.

Currently, credit unions are not allowed to accept or trade in digital currencies. The NCUA has the authority to prohibit credit unions from accepting Libra, or any other commodity, as a form of deposit or payment for safety and soundness reasons.

Rent-a-Bank Schemes and Payday Loans

37. Chairman Hood, *how do you respond to Board Member Harper's concerns? Is it fair for credit union borrowers to pay triple-digit rates for these loans when they might be able to, for example, take out a credit card and pay far less in financing costs?*

Response:
The NCUA adopted two Payday Alternative Loan (PALs) rules designed to encourage credit unions to offer credit services to underbanked segments of society. The consumer protections for PALs II loans are, in fact, stronger than those for PALs I loans. The PALs II rule provides the same consumer protections that exist for PALs I loans, with the added protection to prohibit fees for overdrafts and insufficient funds.

Credit unions cannot charge an interest rate higher than 28 percent on an annualized basis for any PALs loan product. The only fee credit unions can charge in connection with making a PALs II loan is an application fee in the amount of the actual cost to process an application, not to exceed $20. By definition, under Regulation Z, an application fee is not a finance charge included in the APR[2] calculation.

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[2] A federal credit union can also charge late fees for payments a member fails to pay on time. Like application fees, late charges are not a finance charge or included in the APR.

While the PALs I and PALs II loan requirements do not prescribe a full underwriting regimen, both rules require credit unions that make PALs loans to implement "appropriate written underwriting guidelines to minimize risk, such as, requiring a borrower to verify employment by providing at least two recent pay stubs." The PALs II rule contains guidance on creating successful PALs programs that recommends adopting procedures and features designed to help each member repay these loans and restore a strong financial footing. First and foremost, the credit union should consider how the PALs loan will benefit a member's financial well-being. The rule also suggests including a savings component, financial education, and reporting repayment performance to consumer reporting agencies.

PALs II is a reflection of our experience overseeing the original PALs program and of working with consumer focused leaders such as the Pew Charitable Trusts to craft financial solutions that make a difference to millions of Americans with low-incomes. PALs is a program of prudent lending that directly helps households who have, to date, been relegated to the high interest rate, subprime payday lending industry. PALs loans are more affordable than pernicious payday loans. The NCUA is committed to building on our experience in this area and adjusting this program in a way that helps credit unions maximize sustainable and affordable service to their members.

NCUA staff will review small-dollar lending, including PALs programs, during all safety and soundness examinations performed in 2020. The reviews will include ensuring compliance with all PALs requirements and determining whether a credit union's program meets the annual percentage rate cap.

De-Risking

***38. All Witnesses**: What are your agencies doing to address this de-risking impact? What steps can examiners take to reverse this trend while still enforcing our laws to promote national security?*

Response:
Generally, credit unions have not engaged in de-risking. However, the NCUA stands ready to collaborate with the federal banking agencies and Financial Crimes Enforcement Network (FinCEN) to enhance knowledge in BSA/AML supervision as it pertains to money transmitters and, more specifically, de-risking.

Use of Alternative Data in Credit Underwriting

***39. All Witnesses:** in the use of alternative data, how do policymakers ensure consumer's permission to access this data is not abused? For example, how do we ensure that the data is not used for a purpose the consumer never intended such as targeted marketing after providing an initial, general consent to the company?*

Response:
The NCUA's approach is consistent with all other instances where a consumer may provide personal data to credit unions. That is, the agency ensures credit unions comply with the

provisions of the Fair Credit Reporting Act (FCRA) and the Gramm-Leach-Bliley Act. Those two laws represent Congress' determination of how creditors can use personal consumer financial data and the ability of a consumer to opt out of certain sharing of information. As the regulator for federal credit unions, the agency reviews compliance with those laws and takes appropriate action if a credit union is improperly sharing personal information or otherwise failing to comply with applicable laws.

***40. All Witnesses**: The interagency statement states that, "Based on that analysis, data that present greater consumer protection risks warrant more robust compliance management." What kind of alternative data, or uses of that data, are your agencies referring to that has "greater consumer protection risks"?*

Response:
As your question indicates, the NCUA and the other federal regulators did not specify types of data that may, in itself, create greater consumer protection or fair lending risks. There are several factors to consider when determining whether using specific data creates risk. For example, the agency may consider whether there is a correlation between the data relied upon and the creditworthiness of a borrower. Although certain types of data may reflect some characteristics of a person, it may not necessarily measure a person's ability or likelihood to repay. The agency would consider whether the data is trustworthy or reliable for all people and in what context it is used.

***41. All Witnesses:** the statement does not discuss racial or gender disparities that may exist in alternative data, especially when combined with artificial intelligence and machine learning. What steps will your agencies take to prevent the use of opaque algorithms or AI that may result in discriminatory outcomes in credit underwriting and other uses of alternative data?*

Response:
The joint statement focuses on the consumer protection implications of the use of alternative data in credit underwriting. The agencies clarify that institutions using alternative data must ensure compliance with applicable consumer protection laws, specifically fair lending laws. The NCUA expects credit unions to institute effective vendor management. This includes management of vendors that utilize alternative data.

The NCUA conducts fair lending examinations and supervision contacts in credit unions to ensure their practices do not result in discriminatory treatment, even when using third-party service providers.

Mobilizing Finance Against Slavery and Human Trafficking

***42. All Witnesses**: What is your agency doing to encourage the development of these analytical tools and investments in data innovations, with a specific emphasis on identifying activity related to human trafficking?*

Response:
In December 2018, the NCUA, along with the other federal banking agencies and the (FinCEN), issued a *Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing.* This statement encouraged credit unions and banks to consider, evaluate, and, where appropriate, responsibly implement innovative approaches to meet their BSA/AML compliance obligations in order to further strengthen the financial system against illicit financial activity.

The NCUA has enhanced its coordination and communication with law enforcement agencies by meeting with them on a regular basis. One of the goals of these meetings is to identify how credit unions can improve their suspicious activity reporting and anti-money laundering approaches while incorporating law enforcement agency priorities.

Additionally, NCUA intends to convene a BSA/AML credit union summit in order to continue to educate credit unions on their compliance with these laws and regulations.

***43. All Witnesses:** What is your agency doing to support better identification of risks relating to human trafficking within the financial sector and the steps needed to mitigate these risks?*

Response:
The NCUA works collaboratively with the other FFIEC members to develop training for examination staff. Human trafficking has consistently been included in the curriculum in the Financial Crimes Seminars and Advanced BSA/AML Specialists Conferences.

Housing Counseling

***44. All Witnesses:** Given the effectiveness of housing counseling in helping low- and moderate-income households to help themselves to responsibly become homeowners, what are you doing as a regulator to promote the use of housing counseling for potential customers of your regulated entities?*

Response:
Credit unions currently play a critical role in facilitating affordable homeownership. In the first three quarters of 2019, the annualized pace of real estate lending for federally insured credit unions exceeded $190 billion. In many cases, mortgage rates for credit union loans are significantly below rates charged by other financial institutions. The NCUA's Chief Economist estimates that in metro areas, credit unions issue mortgages with interest rates 12 basis points lower than those of noncredit unions. This gap widens to 14 basis points in rural areas. While this difference appears small, it can have a meaningful impact on borrowers. A 14 basis-point

discount in the median rate spread could save a borrower $5,000 over the life of a $175,000 30-year loan.[1]

In terms of sustainability, I would stress that credit union mortgages traditionally have had significantly low default rates relative to other loans. Although NCUA always will remain vigilant in ensuring that underwriting standards are safe and sound, the strong historical loan performance indicates that mortgage sustainability has been a critical industry value.

I have been a strong proponent of ensuring that regulation is effective, but not excessive. That principle has played a critical role—and will continue to do so—in facilitating affordable homeownership among credit union members. Last year, for instance, the NCUA proposed to increase the appraisal threshold for residential mortgages originated by credit unions. This threshold parallels similar increases from the FDIC. This effort will decrease loan origination costs for a significant number of borrowers in the years ahead.

In addition, the NCUA regards financial literacy promotion as fundamental to the credit union mission. Many credit unions across the country offer housing and general financial counseling services, voluntarily and often free of charge, to their members. We at the NCUA encourage the industry to find new ways to offer financial capability counseling to help low- and moderate-income families improve their financial position. Last summer, I visited a credit union in Maryland, and that opportunity launched a new partnership to offer in-branch financial counseling services.

The NCUA's Community Development Revolving Loan Fund (CDRLF), which relies on Congressional appropriations, supports technical assistance grants for low-income-designated credit unions. In 2019, for the first time, the NCUA offered grant funding for counselor certification to help credit union staff obtain a certificate in financial and housing counseling to members. The NCUA awarded 35 such grants last year.

Grants were distributed as follows:

Initiative	**Sum of Total Awards**	**Number of Awards**
Counselor Certification	$161,925	35
Digital Services & Security	$550,613	73
MDI Mentoring	$74,875	3
Training	$222,369	47
Underserved Outreach	$972,742	11
Grand Total	**$1,982,524**	**169**

One of the credit union industry's distinguishing features is personalized service to its members. Financial counseling is very much part of this. As such, credit unions generally tend to know

[1] This assumes an interest rate reduction from 3.74 percent to 3.60 percent

more about their members than other financial institutions and are able to tailor their financial products accordingly. This relationship supports more careful underwriting in the case of home loans. That has led to relatively strong loan performance. In fact, credit union mortgage loan delinquency rates tend to be significantly lower than other mortgage originators. I am proud of the fact that the ethos of the credit union industry – expanded economic opportunity and shared prosperity – also leads to good business outcomes.

Appraisals

***45. All Witnesses**: Did any of your agencies take any supervisory or enforcement actions during or after the financial crisis that related to appraisal and underwriting deficiencies? If yes, does this not suggest there were safety and soundness concerns relating to appraisals in the lead up to the financial crisis a decade ago?*

Response:
While the NCUA did take some supervisory actions against individual credit unions related to appraisal and underwriting issues during and after the financial crisis, these actions do not suggest any systemic or material problems related to appraisals and poor underwriting in the credit union system. Instead, many of these actions helped to ensure that credit unions had appropriate lending policies with respect to appraisals and adhered to them. No credit union was liquidated or conserved because of appraisal deficiencies.

Following the financial crisis, the Dodd-Frank Act provided a series of reforms and consumer protections to the financial system, including amending Title XI to require the CFPB to engage in applicable rulemakings and amendments to the Truth in Lending Act (TILA) and Equal Credit Opportunity Act (ECOA). The NCUA has worked with other regulators to implement these reforms to provide legitimacy, independence, and oversight of appraisals and evaluations. For example, the NCUA issued the Interagency Appraisal and Evaluation Guidelines in 2010 to address collateral valuation and an Interagency Statement on Supervisory Approach for Qualified and Non-Qualified Mortgage Loans in 2013 to address prudent underwriting of residential mortgage loans.

In addition, the NCUA periodically reviews its real estate appraisal regulations to determine that the threshold levels do not pose a threat to the safety and soundness of federally insured credit unions. The 2019 proposed increase to the residential threshold raises it for credit unions to the same level as banks and sets the proportion of loans requiring an appraisal to approximately the same level it was in 2002 when we last increased the threshold. The 2002 threshold increase did not result in a material increase in risk to safety and soundness even through the Great Recession where losses in credit unions were elevated but well below national averages. Credit unions' residential mortgage loans have performed well with relatively low delinquencies and net charge-off rates both before and after the increase. The net charge-off rate for residential real estate transactions also did not increase after the NCUA's increase in the appraisal threshold from $50,000 to $100,000 in 1995.

In addition, based on supervisory experience and analysis of Material Loss Reviews (losses to the Share Insurance Fund of more than $25 million and more than 10 percent of total assets)

conducted by the NCUA's Inspector General since 2008, appraisals are not a substantial factor in the failure of credit unions. Of the 27 Material Loss Reviews, 14 were residential-real-estate–related; however, none of the failures resulted from a lack of appraisals. Losses were all driven by either specialty concentration—such as investments in RMBS and structured finance products—fraud at the institution, or governance lapses.

***46. All Witnesses**: Please provide aggregate year-by-year data on examiner findings regarding appraisals and evaluations since enactment of Title XI of FIRREA.*

Response:
The NCUA defines "findings" as problems that management must address but can do so in the normal course of business, since these problems do not threaten the viability of the credit union, represent an undue risk to the Share Insurance Fund, or reflect willful or egregious violations. A Document of Resolution is a problem that must be addressed immediately and is similar to Matters Requiring Board Attention issued by the federal banking agencies.

The NCUA does not have a searchable database to accurately identify examiner findings regarding appraisals and evaluations. However, the NCUA maintains a searchable database of violation reports related to compliance regulations from the examination process. The NCUA started tracking this data in 2000, and this system tracks the type of violation and the examiner's corresponding resolution to the violation. Management reviews these reports periodically as part of the monitoring process.

From 2000 to 2018, there were two violations relating to appraisals (12 CFR Part 722) and evaluations, out of 86,274 total violations in the database. These violations related to a credit union not obtaining required appraisals and a credit union not having board-approved real estate appraisal policies and procedures. The credit unions both agreed to correct the violations and the NCUA has resolved both violations.

***47. All Witnesses**: With respect to oversight of individuals conducting evaluations, what recourse does a consumer have who may have issues arising from an evaluation product, which currently has no regulatory oversight?*

Response:
The NCUA has long required evaluations in lieu of appraisals for many transactions, including certain transactions exempted by an appraisal threshold. The recently amended regulation Part 722 requires that an evaluation be performed by an individual who is independent of the loan production and collection processes; has no direct, indirect, or prospective interest, financial or otherwise, in the property or the transaction; and is qualified and experienced to perform such estimates of value for the type and amount of credit being considered. Evaluations prepared according to these standards provide an important level of consumer protection.

Under the Dodd-Frank Wall Act, consumers have certain recourses for evaluations. The Interim Final Rule on Valuation Independence, which implements Section 1472 of the Dodd-Frank Act,

requires that evaluations meet independence standards that carry civil liability penalties for covered consumer transactions. The Dodd-Frank Act amended the ECOA to require creditors to provide applicants free copies of appraisals and other types of valuations prepared in connection with first-lien transactions secured by a dwelling, which include evaluations. In addition, borrowers may make a complaint about appraisals or evaluations to the CFPB consumer complaint database or directly to the NCUA. Finally, through the supervision process, NCUA examiners may identify issues with policies and implementation of the evaluation process and issue enforcement actions as necessary to ensure adherence to the regulation and protection for the consumer.

Questions for Mr. Hood
Chairman, National Credit Union Administration Questions from Representative Ocasio-Cortez

1) *During your testimony before the Committee on December 4th when asked about considering principal reduction for owner-drivers you stated this would be difficult given your statutory requirements to protect the National Credit Union Administration's share insurance.*

    a) *Can you specify what particular statute prohibits you from using your discretion to provide principal reduction?*

Response:
Thank you for the opportunity to clarify my response during the hearing. While there is no specific statute prohibiting the use of principal reduction in individual cases, and indeed the agency has provided principal reduction on a case-by-case basis, Federal Credit Union Act provisions express a principal purpose to resolve problems with insured credit unions at the "least possible long-term loss to the Fund."[2] Furthermore, the Federal Credit Union Act specifies a number of specific actions the Board is required to take as liquidating agent in winding down an insolvent institution, some within a specified period, including, making determinations to repudiate contracts, immediately paying insurance claims incurred by the institution, distributing an institution's assets, paying all valid obligations of the credit union, and, in the case of a federal credit union, cancelling its charter.[3][4][5][6][7] The Federal Credit Union Act creates a clear distinction between the Board's conservatorship and liquidation authorities, evidencing intent for the Board to wind down operations in liquidation.

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[2] 12 U.S.C. 1790d. *See also*, 12 U.S.C. 1790d(l)(3)(C), with respect to federally insured state-chartered credit unions, which requires the agency to consider the risk that the Share Insurance Fund would incur a loss with respect to the credit union or any loss that the Fund is expected to incur with respect to the credit union.
[3] 12 U.S.C. 1787(c)(2).
[4] 12 U.S.C. 1787(d)(1).
[5] 12 U.S.C. 1787(b)(11).
[6] 12 U.S.C. 1787(b)(2)(F).
[7] 12 U.S.C. 1766(b)(5).

Where the agency does have discretion in its role as liquidating agent is in taking actions which the Board determines are in the best interests of the credit union, its account holders, or the Board.[8] In this context, the Board must consider the interests of more than 120 million credit union members and more than 5,200 federally insured credit unions nationwide to prudently manage the Fund, which they pay into and are required to replenish, as needed, to ensure the Fund's equity ratio remains sound.

Any principal forgiveness granted by the NCUA, as liquidating agent, to taxi credit unions' members with business loans, while appropriate and needed in certain cases, comes at the expense not only of other claimants, members, and creditors of the particular liquidated institution, but the credit union system at large, which must pay for Share Insurance Fund losses.

b) What is the rationale behind not considering principal reduction for owner-drivers that have been driven to financial ruin or suicide due after being victims of this predatory lending scheme?

Response:
We have not concluded the loans were granted in a predatory manner. Some credit unions had deficiencies in their underwriting standards and ignored repeated warnings from this agency, including guidance on the dangers of holding a large concentration of assets in any one asset class or related asset classes. Those credit unions with an excessive concentration of medallion loans have either been liquidated or merged. We continue to believe the primary cause for borrower hardship was the rapid run-up in values driven by Taxi and Limousine Commission auctions and the dislocation of the taxi industry caused by the introduction of rideshare companies to the New York City transportation-for-hire marketplace.

The NCUA has granted some principal reduction on a case-by-case basis to borrowers when circumstances support this course of action. This typically has come in the form of discounted payoffs or other settlement arrangements. Programmatically, however, our primary focus has been to work with borrowers to ease their burden through favorable modifications to interest rates, payments, and terms where borrowers are willing to engage with us and provide updated financial statements. Since each case is different, we believe offering wholesale forgiveness without evaluating individual circumstances would be counter to our statutory duties.

While evaluating its ultimate resolution strategy, the NCUA determined that offering programmatic debt forgiveness would limit the options and potential recoveries on the asset management estates of failed credit unions, and thus was contrary to the agency's statutory mandates.

2. According to a report from the NCUA Office of the Inspector General on the taxicab medallion crisis, NCUA inspectors published reports in 2012, 2013, and 2014

[8] 12 U.S.C. 1787(b)(2)(J).

documenting the unsafe and unsound lending practices on taxicab medallion lending by credit unions that eventually failed.

a) *Why did NCUA allow credit unions to lend in this market at inflated values even though the NCUA was aware that unsafe and unsound lending practices was occurring?*

Response:
The not-for-profit credit unions that served this industry provided stable and secure business loans to member taxi drivers and owners in New York City for more than 80 years. They were not speculative entrants making risky bets. They were founded in the 1920s and 1930s to provide low-interest loans on a type of collateral that gave many taxi drivers the opportunity to enter the middle class. Those who were able to purchase their own medallions at affordable prices secured better lives for themselves and their families as the price of their medallions increased over the years. Many used the equity generated by rising medallion values to become homeowners, finance college educations, and save for retirement. The concentration of credit union lending to this market created a specialization that worked well for decades until the disruption caused by the sudden emergence of ridesharing services devastated the incomes of many taxi drivers at the time when their medallions had risen beyond a sustainable value.

In the NCUA' supervision of these credit unions, the agency identified some with deficient underwriting standards. However, the NCUA's data show that, in 2015, the average outstanding loan balance per taxi medallion was less than $350,000 at a time when taxi medallions were being sold for almost $1 million. The ratios of outstanding loan balance to collateral value at that time were relatively conservative: averaging less than 40 percent with more than nine out of 10 loans having a ratio of less than 65 percent. Many of the credit unions that made these loans no longer exist. In their efforts to continue serving members as they had done prudently for decades, these credit unions were exposed to the risks of an asset bubble and adverse changes in the market from new sources of competition.

b) *Did NCUA share these reports with the Taxi & Limousine Commission or any other City/State agency?*

Response:
The NCUA's examiners issue examination reports at the end of each examination. Examination reports are supervisory records between a credit union and the NCUA and, in the case of federally insured, state-chartered credit unions, the State Supervisory Authority. These reports generally are not disclosed to external third parties.

5. *I, along with my colleagues in the New York delegation, have called for the establishment of an entity to buy and restructure the loans and reduce the principal to make sure owner drivers benefit from the discounted rates at which loans are being sold to debt collectors.*

a) If a city or private entity created a fund to buy-back these loans, what role could the NCUA play?

Response:
Prior to selling the majority of our taxi related assets, and at my direction, senior staff from the NCUA met with New York City officials and representatives from the New York City Taxi Taskforce. Regrettably, the senior staff determined that no party had committed funds to purchase the agency's taxi medallion loan portfolio. Additionally, they entered into the bidding process for the medallion portfolio without a definitive offer.

While the task force's proposal was not conceived in time to bid on this transaction, NCUA's decision to sell does not restrict the city or any other private entity from negotiating with the new owners or other owners who own the majority of the loans secured by New York taxi medallions.

As noted above, the NCUA has a statutory obligation to prudently manage and protect the National Credit Union Share Insurance Fund.[9] Any delay could have caused the Fund to incur further losses.

As to loans not managed by the NCUA, the agency is not able to dictate how credit unions holding taxi medallion loans manage their portfolios as long as they are in compliance with applicable laws, regulations, and safety and soundness principles.

b) Could the NCUA coordinate bulk buy-backs of loans of specific lenders?

Response:
The NCUA does not have the authority to coordinate loan sales by or for credit unions that are not under its direct control.

c) Does NCUA keep data on cost of loan to debt collector versus outstanding balance owed by borrower?

Response:
The NCUA does not collect this data.

7. Media reports have shed light on the tragic number of suicides by taxi drivers in New York City due to the overwhelming debt and financial plight of medallion owners, which includes taxicab medallion foreclosures.

a) Does the NCUA receive notification before a foreclosure is acted upon?

Response:

[9] 12 U.S.C. 1790d.

The NCUA does not receive notification of foreclosures initiated by credit unions. For assets managed by the NCUA as liquidating agent, the agency does receive notification.

b) Has the NCUA investigated foreclosures and the use of confessions of judgment?

Response:
The agency has not conducted a formal investigation.

c) What can NCUA do to put a hold on the current trend of foreclosures while efforts are being made to address the debt and stabilize the industry?

Response:
The foreclosure process is typically governed by state law, which both credit unions and the agency comply with when foreclosing on collateral. For credit union loan portfolios that are not under the direct control of the NCUA, the agency is unable to dictate or prohibit foreclosure procedures, as long as the credit union complies with applicable laws, regulations, and safety and soundness principles. Foreclosure is always the last resort.

Prior to the loan sale, the agency's focus was on working with borrowers to modify loans, where possible, to address the ever increasing debt and help stabilize the market. We worked with borrowers in good faith. For example: the Liquidating Agent modified 600 loans, reducing payments by 21 percent on over 70 percent of loan modifications.

9. Vulture investors, including hedge funds that specialize in buying distressed assets, have now been looking to purchase delinquent and foreclosed taxicab medallions.

a) Does the NCUA intend to put out an RFP for debt collector to purchase all the loans?

Response:
The NCUA evaluated its options for resolving the asset management estates of failed taxi medallion credit unions for the past two years. As noted above, NCUA has a statutory obligation to prudently manage and protect the National Credit Union Share Insurance Fund.[10] The agency, as liquidating agent, worked to achieve the best value for the asset management estates while taking steps to identify a buyer of the troubled assets that would act in good faith. Through its financial advisor, the agency issued a Request for Qualifications (RFQ) to prospective investors and thoroughly vetted all bidders before making a decision to sell. This included contracting with a respected, independent third party to complete due diligence on all prospective bidders. Our review of that due diligence indicated we were dealing with reputable firms.

[10] 12 U.S.C. 1790d.

b) What guarantees has the NCUA been offered that if they do sell to hedge funds or other entities that these loan purchasing entities will work with borrowers for sustainable and affordable loan modifications?

Response:
Normally in a bulk asset sale, it has been the practice of the NCUA, and other governmental entities, to resolve assets based on the highest bid. With respect to the taxi medallion loans and related assets, the NCUA took additional, self-imposed extraordinary measures to ensure that qualified bidders would be reputable and responsible counterparties, and would work with borrowers in a good faith manner.

The NCUA worked through a thorough process of vetting bidders to make sure we only considered bids from reputable and experienced firms dedicated to working in a good-faith manner with borrowers. In consultation with our financial advisor, the NCUA reached out to 23 qualified firms with experience in handling distressed commercial assets, and six of those submitted bids. After an extensive review, the NCUA allowed two firms go through to the final due diligence bid round and received two independent offers. Some firms were turned away because the NCUA was not confident the firms would treat borrowers in a fair way.

I've said previously that behind every taxi medallion loan is a family. I firmly believe this sale will help holders and their families because it will provide them with greater certainty over the management of their loans. We believe our process has accomplished these additional standards.

c) Will these loan purchasing entities have loan modification specialists?

Response:
Yes. The winning bidder has a full loan servicing operation and a history of working with taxi medallion borrowers to achieve loan modifications.

d) Will they have loan purchasing entities have clear and transparent policies and practices for loan modification terms, interest rate reductions, and principal rate reductions that will be reviewable by the public?

Response:
Parties responding to the RFQ indicated they would clearly communicate loss mitigation policies and procedures to borrowers, including plans for principal forgiveness, where appropriate.

e) Will a thorough review of business practices of these loan purchasing entities be conducted prior to selling off loans?

Response:

Yes. In addition to the attestations in the RFQ process described above, the NCUA independently and thoroughly researched the backgrounds of prospective bidders, their key investors, their named asset managers, and key employees for any unscrupulous or illegal business practices.

U.S House Committee on Financial Services
"Oversight of Prudential Regulators: Ensuring the Safety, Soundness, Diversity, and Accountability of Depository Institutions?"
December 4, 2019

Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Community Reinvestment Act

Question 1: We discussed the importance of the Community Reinvestment Act (CRA) and its implementation during the hearing. Shortly following the hearing, the OCC and the FDIC issued a notice of proposed rulemaking (NPR),[1] which FDIC Board Member Martin Gruenberg characterized as, "a deeply misconceived proposal that would fundamentally undermine and weaken the Community Reinvestment Act."[2] Furthermore, the Federal Reserve does not support the proposal and despite a request being made by stakeholders and a number of Members of Congress that any proposal should not be rushed and allow for, at a minimum, at least 120 days for the public to review and comment on the proposal, this proposal provides only 60 days for public comment.

Vice Chair Quarles and Chairman McWilliams, if regulators finalized different regulations to implement the Community Reinvestment Act, could this lead to regulatory arbitrage in the marketplace? Leading up to the last financial crisis, when the Office of Thrift Supervision lowered standards for thrifts compared to other banks, was that kind of regulatory arbitrage helpful or did it lead to a race to the bottom? Should consistent application of the CRA be one of the highest priorities regarding any changes to its implementing regulations?

Response:

On December 12, 2019, the FDIC and OCC approved a notice of proposed rulemaking[3] to modernize the regulations implementing the Community Reinvestment Act (CRA), which had not been substantively updated for nearly 25 years. The proposed rule was intended to increase bank activity in low- and moderate-income (LMI) communities where there is significant need for credit, encourage more responsible lending, and promote improvements to critical infrastructure. On May 20, 2020, the OCC adopted a final rule implementing the proposed changes to the CRA regulations. The FDIC strongly supports the efforts to make the CRA rules clearer, more transparent, and less subjective. However, the agency was not prepared to finalize the CRA proposal at that time, and FDIC-regulated banks continue to comply with the same CRA framework as they did before the proposal.[4]

On March 19, 2020, the FDIC, FRB, and OCC issued a joint statement to encourage financial institutions to work with affected customers and communities, particularly LMI customers and communities, and clarified that the agencies will provide favorable consideration of certain retail

[1] https://www.occ.treas.gov/news-issuances/news-releases/2019/nr-ia-2019-147.html.
[2] https://www.fdic.gov/news/news/speeches/spdec1219d.pdf.
[3] *See* Community Reinvestment Act Regulations, 85 Fed. Reg. 1204 (Jan. 9, 2020), available at https://www.govinfo.gov/content/pkg/FR-2020-01-09/pdf/2019-27940.pdf.
[4] *See* Statement by FDIC Chairman Jelena McWilliams on the CRA Joint Proposed Rulemaking (May 20, 2020), available at https://www.fdic.gov/news/news/speeches/spmay2020.html.

banking services, retail lending activities, and community development activities related to the COVID-19 national emergency pursuant to the CRA.[5]

[5] *See* FDIC FIL-19-2020, *Joint Statement on CRA Consideration for Activities in Response to the COVID-19* (Mar. 19, 2020), available at https://www.fdic.gov/news/news/financial/2020/fil20019.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 2: Chairman McWilliams, is there an arbitrary deadline that you are rushing to meet with respect to updating CRA regulations? Why did the NPR only allow for 60 days for public comment? How do you compare these CRA efforts to other statutory mandates the FDIC has failed to complete, such as issuing a final rule on incentive-based compensation arrangements under Section 956 of Dodd-Frank?

Response:

The notice of proposed rulemaking on CRA modernization was approved by the FDIC Board of Directors in a public meeting on December 12, 2019 and published in the *Federal Register* on January 9, 2020. In response to requests from members of Congress and other commenters, the FDIC and OCC extended the comment deadline from March 9, 2020 to April 8, 2020, nearly four months after the proposal was approved and issued by the FDIC Board. This public comment period was consistent with FDIC practice and the requirements established by Congress under the Administrative Procedure Act. After receiving thousands of comment letters on the proposal, including from members of Congress, the OCC adopted a rule finalizing the proposed changes to the CRA regulations. The FDIC strongly supports the efforts to make the CRA rules clearer, more transparent, and less subjective. However, the agency was not prepared to finalize the CRA proposal at that time, and FDIC-regulated banks continue to comply with the same CRA framework as they did before the proposal.[6]

With respect to incentive-based compensation, the FDIC, FRB, and OCC issued guidance in June 2010 – one month prior to the enactment of the Dodd-Frank Act – to help ensure that incentive compensation policies at banking organizations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organization.[7]

Section 956 of the Dodd-Frank Act subsequently directed the FDIC, FRB, OCC, NCUA, SEC, and FHFA ("six agencies") to jointly prescribe, within nine months of the enactment of the law, regulations or guidelines that prohibit incentive-based pay arrangements that the six agencies determine encourage inappropriate risks. Section 956 mandates that the six agencies ensure that the standards are "comparable" to the standards established under section 39 of the FDI Act and specifically take into consideration the compensation standards described in section 39(c). Under section 39(c), the federal banking agencies are required to prohibit compensation arrangements that provide excessive compensation or could lead to material financial loss to an insured depository institution (IDI). Section 39(c) was promulgated by Congress in 1991 and has been in effect for IDIs since then.

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[6] *See* Statement by FDIC Chairman Jelena McWilliams on the CRA Joint Proposed Rulemaking (May 20, 2020), available at https://www.fdic.gov/news/news/speeches/spmay2020.html.
[7] *See* Federal Reserve, OCC, OTS, FDIC Issue Final Guidance on Incentive Compensation (June 21, 2010), available at https://www.federalreserve.gov/newsevents/pressreleases/bcreg20100621a.htm.

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While the banking agencies' 2010 guidance remains fully intact, the six agencies continue to engage in discussions regarding how best to implement the statute. In the meantime, the FDIC continues to review compensation policies and practices of supervised institutions in accordance with the FDI Act and the 2010 guidance to ensure that institutions have appropriate risk management frameworks in place, including appropriate oversight and governance by the board of directors and sound operational controls.

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Question 3: The OCC's initial Advance Notice of Proposed Rulemaking (ANPR) regarding modernizing CRA regulations issued in August 2018 asked whether CRA credit "…[should] be limited to loans to LMI borrowers and loans in LMI or other identified areas…."[8] The architects of CRA sought to combat redlining. While tax credits and other federal programs might encourage investments in infrastructure – roads, bridges and hospitals – and projects that benefit a community more broadly, CRA has historically and should remain targeted on access to credit and financial services for LMI borrowers and communities traditionally underserved by the nation's financial system.

Vice Chair Quarles and Chairman McWilliams, do you agree that CRA regulations should remain narrowly targeted on providing banks credit for lending and investing activities to LMI individuals and LMI areas? Should roads and bridges and other general community-building activities, as a general matter receive more CRA credit than they get today? How does infrastructure expenditures combat redlining and promote access to credit?

Response:

The notice of proposed rulemaking encouraged banks to increase lending and financial services provided to or benefitting LMI individuals, including by no longer providing CRA credit for mortgage loans to high-income individuals living in low-income census tracts. The proposal would have also provided CRA credit for investments in essential infrastructure that benefits or serves LMI individuals, LMI census tracts, or other targeted areas such as Indian Country. Essential infrastructure projects would include roads, mass transit, or water supply and distribution. The addition of the essential infrastructure criterion would acknowledge the importance of these types of projects to LMI communities.

[8] https://www.occ.gov/news-issuances/news-releases/2018/nr-occ-2018-87.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 4: FDIC Board Member Gruenberg raised another concern with the OCC and FDIC's NPR to modernize CRA, specifically that, "[T]his proposal would allow a bank to achieve a less than satisfactory rating in nearly half of its assessment areas and still receive a satisfactory or even outstanding rating. Banks would have the flexibility to focus their stronger community reinvestment-qualifying efforts on as few as half of their assessment areas while minimizing their efforts elsewhere."

Chairman McWilliams, why should banks that achieve a less than satisfactory rating in nearly half of its assessment areas be able to receive a satisfactory or outstanding rating overall, as they would under the NPR?

Response:

Under the existing framework, a bank can receive a less than satisfactory rating in some of its assessment areas and still qualify for an overall rating of satisfactory or outstanding. The notice of proposed rulemaking provided that the ratings for a bank evaluated under the general performance standards would be based on a combination of approaches. To receive a satisfactory or outstanding rating at the assessment area level, a bank would have been required to meet the minimum thresholds for performance on the applicable retail lending distribution tests in that assessment area for each major retail lending product line with at least 20 loans in that assessment area. In addition, the average of a bank's CRA evaluation measures for an evaluation period would have to meet the associated empirical benchmark. Notably, the proposal sought public comment on whether a threshold of 50 percent or 80 percent should be used to determine a significant portion of a bank's assessment areas.

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Question 5: Since 2016, banks have negotiated $86 billion in community benefit agreements (CBAs) with local stakeholders because of CRA and its community input provisions during mergers/acquisitions, resulting in banks providing more mortgages, small business and community development loans and investments in LMI communities around the country. OCC Comptroller Otting has admitted that part of his CRA reform plan is to make it harder for community groups to "hold [bankers] hostage" when bank merger and expansion deals are up for regulatory approval.

Vice Chair Quarles and Chairman McWilliams, do you agree that a bank's CRA rating should remain a key consideration in whether a bank is allowed to merge? Under what circumstances, do you believe it is important to have a public hearing in the case of a bank merger?

Response:

The Bank Merger Act (BMA) prohibits an insured depository institution (IDI) from merging with another IDI without the prior approval of the responsible agency. Among other things, the BMA requires the responsible agency to consider specific statutory factors related to financial and managerial resources and future prospects, the convenience and needs of the community, financial stability, and the anti-money laundering records of the banks involved. The CRA requires that, when evaluating an IDI's application under the BMA, the responsible agency take into account an IDI's record of meeting the credit needs of its community, including LMI neighborhoods. Under the notice of proposed rulemaking, the agencies would continue to consider a bank's CRA rating as part of its statutory analysis under the BMA. The FDIC holds public hearings when it believes such hearings would be helpful or necessary to obtain additional views or information that are not otherwise provided through the comment process.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Deregulating Megabanks

Question 6: Vice Chair Quarles and Chairman McWilliams, over the past 18 months, your agencies have proposed rules to reduce leverage capital requirements for the biggest systemically significant banks, slashed liquidity requirements for all but the nation's largest banks, cut back on resolution planning requirements for large banks, weakened stress testing by removing key leverage ratio requirements, cut back on effective capital requirements for large bank derivatives dealers, drastically reduced Volcker Rule protections against proprietary trading, and just recently you have proposed to eliminate key margin requirements for large international banks engaged in derivatives transactions.

Chairman McWilliams: Do you believe that big banks were excessively regulated before this Administration took office? Given that bank lending and bank profits were growing rapidly at the time this Administration took office, why do you believe that?

Response:

The FDIC continues to fulfill its mission to maintain stability and public confidence in the nation's financial system by insuring deposits, examining and supervising financial institutions for safety and soundness and consumer protection, making large and complex financial institutions resolvable, and managing receiverships. The FDIC has taken steps to appropriately tailor its supervision and regulation to take into account the size, complexity, risk profile, and business model of financial institutions, while still ensuring safety and soundness.

The FDIC has also maintained the most rigorous and most critical regulatory requirements on the largest banks. The largest banks are subject to standardized and advanced risk-based capital standards, market-risk capital standards, capital surcharges, leverage ratios, supplementary leverage ratios, enhanced supplementary leverage ratios, liquidity coverage ratios, long-term debt requirements, stress testing, and mandatory clearing and margin requirements for derivatives. These banks are also subject to the FRB's Comprehensive Capital Analysis and Review (CCAR) exercise.

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Question 7: Chairman McWilliams: Following our hearing in May, you responded to questions for the record, and you wrote, "Resolution plans have been a valuable tool for improving resolvability through bankruptcy. The planning process has helped ensure that firms can better project resource availability and needs in resolution, understand and simplify their legal structures, work through their internal governance processes, and address core obstacles to resolution in bankruptcy. Firms have made significant progress in this regard." I agree, but if living wills have helped large banks become better organized, why is the FDIC now dialing back these requirements? As we saw in the last crisis, over the course of 2005, 2006, 2007 and 2008, a lot can change in a few months let alone a few years. So why should megabanks like Wells Fargo only have to update their *complete* living will once every four years?

Response:

Over the past eight years, large firms have improved their resolution strategies and governance, refined their estimates of liquidity and capital needs in resolution, and simplified their legal structures. Consistent with the new statutory asset threshold under the Economic Growth, Regulatory Relief, and Consumer Protection Act and the agencies' experience with resolution planning, the FDIC and FRB issued a final rule[9] to improve the efficiency and effectiveness of the process and exempt smaller regional banks from the requirements. Under the rule, our underlying standards for reviewing resolution plans will not change and will remain rigorous.

With respect to timing, the rule formalizes the agencies' existing practice of requiring U.S. global systemically important banks (GSIBs) to submit resolution plans every two years and requiring other filers to submit plans every three years. The rule also introduces a new "targeted resolution plan" that will allow filers to submit a subset of information required by a full resolution plan. Such targeted plans will be submitted every other cycle and will still require the core elements most critical to resolution plans. The targeted plans also must include any material changes since the prior plan. After several rounds of resolution plan submissions, firm-specific feedback, and general guidance, the U.S. GSIBs' resolution plans have matured over time.

Under the final rule, the agencies retain the ability to obtain key information between resolution plan submissions, including by requiring interim updates and receiving notices of extraordinary events, which will allow the agencies to remain informed of material developments affecting resolvability. The agencies also have the authority to require a full resolution plan instead of a targeted resolution plan and to move a resolution plan submission date.

[9] *See* Resolution Plans Required, 84 Fed. Reg. 59194 (Nov. 1, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-01/pdf/2019-23967.pdf.

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Question 8: According to data from the Federal Reserve Bank of New York, Tier 1 leverage ratios at the largest banks have dropped steadily in recent years -- over 60 basis points since their peak in 2016. Stakeholders contend this represents losing over one-quarter of the gains in bank leverage capital since 2008. As you know, leverage ratios are the broadest metric of the capital banks have available to absorb losses over their entire asset base.

Chairman McWilliams, in his farewell speech, former Fed Governor Tarullo said, "[O]ur researchers, like those at some other official-sector entities, have been using more formal economic analysis to estimate the level of capital requirements that best balances the benefits associated with reduced risk of financial crisis with the costs of banks funding with capital rather than debt. A recent study by three Federal Reserve Board researchers concludes that the tier 1 capital requirement that best achieves this balance is somewhere in the range of 13 percent to 26 percent, depending on reasonable choices made on some key assumptions. By this assessment, current requirements for the largest U.S. firms are toward the lower end of this range, even when one takes account of the de facto capital buffers imposed on most firms in connection with the stress test."[10] For U.S. G-SIBs, what is their current level of tier 1 capital, and based on the Federal Reserve's research referenced by Mr. Tarullo, do you agree that these standards should be increased, at least for the G-SIBs?

Response:

Strengthening capital requirements at our nation's largest, most systemically important banks was an essential post-crisis response, as strongly capitalized banks are better able to withstand financial and economic headwinds. The stringency of these standards should be appropriately tailored to firm's size, risk profile, and systemic importance. As noted above, the U.S. GSIBs continue to be subject to the most rigorous standards, including standardized and advanced risk-based capital standards, market-risk capital standards, capital surcharges, leverage ratios, supplementary leverage ratios, enhanced supplementary leverage ratios, liquidity coverage ratios, long-term debt requirements, stress testing, and mandatory clearing and margin requirements for derivatives. These banks are also subject to the FRB's CCAR exercise.

In addition to the minimum capital requirements, the FDIC expects every institution to maintain capital levels commensurate with the level and nature of all risks to which the institution is exposed. Firms must have a framework for assessing and governing their overall capital adequacy in relation to their risk profile and a comprehensive strategy for maintaining an appropriate level of capital.

[10] https://www.federalreserve.gov/newsevents/speech/tarullo20170404a.htm. The study referenced is Simon Firestone, Amy Lorenc and Ben Ranish (2017), "An Empirical Economic Assessment of the Costs and Benefits of Bank Capital in the U.S. (PDF)," Finance and Economic Discussion Series 2017-034 (Washington: Board of Governors of the Federal Reserve System).

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Question 9: Chairman McWilliams, as the manager of the Deposit Insurance Fund and the agency that must resolve failed depository banks, the FDIC has traditionally been a key advocate for protection of the publicly insured depository bank from the Wall Street trading risks taken in large mega-bank holding companies. But unfortunately, I am concerned the FDIC may be moving away from this commitment.

Chairman McWilliams, the FDIC recently joined other prudential regulators in proposing to allow the global mega-banks that dominate U.S derivatives dealing to move their derivatives transactions from non-bank subsidiaries into the public insured depository, without setting aside any additional margin to protect taxpayers from the associated risk. Would such a move not create new threats to the Deposit Insurance Fund?

Response:

In the aftermath of the financial crisis, Congress mandated that regulators establish capital and margin requirements for non-cleared swaps. In 2015, the banking agencies adopted regulations implementing these requirements. In addition to requiring the exchange of initial and variation margin with unaffiliated counterparties, the rule requires that IDIs collect initial and variation margin from affiliates to protect the IDI from losses exacerbated by an affiliate's failure. Since that time, the largest firms have made significant progress implementing a single point of entry resolution strategy designed to recapitalize subsidiaries and protect against the type of affiliate failures envisioned under the rule. After carefully reviewing these regulations, the agencies issued a proposal to repeal the requirement that IDIs collect initial margin from affiliates while retaining important safeguards to protect the safety and soundness of the IDI and the Deposit Insurance Fund, including the requirement that IDIs exchange variation margin with affiliates.[11] Recently, the agencies have undertaken a number of regulatory actions in the midst of significantly changing economic conditions. While considering the impact of these actions, the agencies continue to discuss the swap margin rule as we endeavor to craft a policy that promotes the efficient allocation of resources, fosters orderly resolution, and protects the Deposit Insurance Fund.

[11] *See* Margin and Capital Requirements for Covered Swap Entities, 84 Fed. Reg. 59970 (Nov. 7, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-07/pdf/2019-23541.pdf.

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Question 10: Chairman McWilliams, the FDIC joined other regulators in weakening the Volcker Rule – specifically, permitting banks to engage in high-risk proprietary trading using so-called "available for sale" securities. Concretely speaking, that exempts over $500 billion in assets, or over half of the securities held by depository banks, from Volcker Rule restrictions. Aren't you worried that by permitting this kind of trading for so many assets at depository banks, the FDIC will improperly subsidize high-risk trading with insured deposits, and increase risks to the Deposit Insurance Fund?

Response:

The Volcker Rule has been one of the most challenging post-crisis reforms for regulators and institutions to implement. As written and originally implemented, the rule was so complex that it required regulators to issue 21 sets of responses to frequently asked questions (FAQs) within three years of its adoption. This complexity has resulted in uncertainty and unnecessary burden, especially for smaller, less-complex institutions.

To address some of these concerns, the agencies issued a set of revisions[12] to the Volcker Rule that tailor the rule's compliance requirements by establishing three tiers of banking entities based on level of trading activity for purposes of applying compliance requirements: (1) significant trading assets and liabilities, (2) moderate trading assets and liabilities, and (3) limited trading assets and liabilities. Banking entities with significant trading assets and liabilities, which hold approximately 93 percent of total trading assets and liabilities across the U.S. banking system, will continue to be subject to the most stringent compliance standards. The revisions also provide greater clarity, certainty, and objectivity about what activities are prohibited under the Volcker Rule. These changes, which apply specifically to the Volcker Rule's proprietary trading prohibition, will improve compliance with the rule and reduce unnecessary burdens while maintaining the statutory prohibition on proprietary trading by covered banking entities.

[12] *See* Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 84 Fed. Reg. 61974 (Nov. 14, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-11-14/pdf/2019-22695.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Diversity and Inclusion

Question 11: Based on feedback from the nation's largest banks to an inquiry led by myself and Rep. Beatty, the Committee found that while the U.S. population is over 50% women and 40% minorities: the boards of directors of the largest banks are comprised of only 29% women and 17% minorities; there is no U.S. global significantly important bank (G-SIB) with a female or minority CEO at the helm; chief diversity officers do not report directly to the CEO at any G-SIB; only 4 out of 8 megabanks spent more than $1 billion on diverse suppliers in 2018; and, while $1.4 billion is the average spent by U.S. G-SIBs on supplier diversity, less than 1% of megabank spending is devoted to diverse asset managers and suppliers, and only 4% of externally managed assets go to diverse-owned firms.[13]

Chairman McWilliams, your agency provides deposit insurance for the megabanks, meaning that all taxpayers provide a backstop to these megabanks, correct? And yet, these institutions, and especially their leadership, do not look like the communities they serve. What steps can the FDIC and other bank regulators take to change these statistics? Is there any reason why every federally-insured bank should not have an internal policy to promote diversity and inclusion, in their hiring practices, in their contracting practices, and so on?

Response:

The FDIC's mission, as an independent agency created by the Congress, is to maintain stability and public confidence in the nation's financial system by insuring deposits, examining and supervising financial institutions for safety and soundness and consumer protection, making large and complex financial institutions resolvable, and managing receiverships.

The FDIC has taken proactive steps to host outreach events and use other methods to aid with awareness of and increase maturity in FDIC-regulated institutions' diversity and inclusion practices. These technical assistance and outreach efforts focus on the value of these institutions conducting voluntary diversity self-assessments and annually submitting assessment results to the FDIC's Office of Office of Minority and Women Inclusion (OMWI). As a result of these efforts, the FDIC will continue to advance the visibility and adoption of diversity and inclusion practices in the financial industry. The FDIC does not have legal authority by law or regulations to require, audit, or examine the hiring or supplier diversity practices of its regulated entities. Examples of the FDIC's outreach activities include the following:

- The FDIC's OMWI engages with FDIC-regulated financial institutions to encourage these institutions to assess their diversity policies and practices. Together with other financial regulators, we have held two annual "Financial Regulatory Agencies' Diversity

[13] FSC Press Release, "Committee Finds More Work is Needed to Improve Diversity at Megabanks," Aug. 13, 2019.

and Inclusion Summits" that bring together organizations in the financial industry to highlight industry best practices involving diversity and inclusion in employment and procurement practices. In the last three years, the FDIC has annually surveyed financial institutions with more than 100 employees for a self-assessment of their diversity policies and practices. The majority of respondents reported that diversity and inclusion is considered in internal workforce matters. The assessments provide insight into exemplary practices that financial institutions implement as a part of their workforce diversity and inclusion practices. The FDIC provided a series of leading practices for these institutions to consider in the future.

- The FDIC has implemented multiple outreach methods to communicate and promote financial institution diversity. This includes a dedicated web page for the financial institution diversity program,[14] participation in multiple banking industry events, and coordination with the American Bankers Association (ABA).

- On November 20, 2019, the FDIC's OMWI participated with the FRB and OCC in a webinar for bankers hosted by the ABA about the joint standards for assessing diversity and inclusion policies and practices, titled "Diversity: What Bankers Need to Know about the Diversity Self-Assessment." The webinar was developed for institutions of all sizes to learn about leading practices and gain a useful understanding about the agencies' collection and reporting of the voluntary submissions of diversity self-assessments received.

- In May 2019, the FDIC's OMWI prepared a video[15] in which the FDIC's OMWI Director describes the FDIC's Financial Institution Diversity Program and encourages FDIC-regulated financial institutions having 100 or more employees to conduct annual self-assessments of their diversity policies and practices as outlined in the Policy Statement.

The FDIC has received voluntary diversity self-assessment submissions from regulated financial institutions for the last three reporting years. The average response rate for institutions responding to the standard for organizational commitment to diversity and inclusion was 88 percent for 2018. Ninety-two percent reported that their financial institution includes diversity and inclusion considerations in both employment and contracting as an important part of its strategic plan for recruiting, hiring, retention, and promotion. Eighty-eight percent reported having a diversity and inclusion policy that is approved and supported by senior leadership, including senior management and the board of directors. The diversity self-assessments completed by the FDIC's regulated financial institutions demonstrate their commitment to diversity and inclusion within their organizations.

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[14] *See* FDIC, Financial Institution Diversity, available at https://www.fdic.gov/about/diversity/dibanking.html.
[15] *See* FDIC FIL-26-2019, *Financial Institution Diversity Video* (May 20, 2019), available at https://www.fdic.gov/news/news/financial/2019/fil19026.html.

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The FDIC recognizes the unique characteristics and size of individual financial institutions' impact on diversity and inclusion efforts. As of September 30, 2019, there were 5,256 FDIC-insured institutions, only 784 (15 percent) of which had more than 100 employees. It is our belief that small financial institutions struggle to compete for the highly qualified diverse candidates due to their location and/or limited resources. Financial institutions that are located in rural or small town areas often face challenges in recruiting a diverse workforce. Those rural and small town banks that are successful at recruiting diverse candidates from other localities often find it difficult to retain these employees.

As of the 2018 reporting period, the FDIC's OMWI has collected three years of data from the self-assessment. Our analysis provides insight into the diversity practices of our regulated financial institutions that we previously did not have. The diversity self-assessment process has been instructive and informative, as many of these institutions do not make available information on their diversity and inclusion policies and practices online. Although the data is not fully representative of the financial services industry, it does provide the FDIC with information we can leverage as we further engage with regulated institutions.

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Question 12: Chairman McWilliams, Vice Chairman Quarles, and Chairman Hood: What new steps can regulators and Congress take to promote diversity and inclusion in banking?

Response:

In its early years, the FDIC's OMWI focused much of its efforts on the implementation of the provisions of the Dodd-Frank Act. This legislation initially required the agencies to establish the infrastructure, programs, and processes to ensure compliance with diversity and inclusion requirements.

As these programs and processes mature, the FDIC's OMWI is beginning to shift its focus beyond compliance with the Dodd-Frank Act into additional ways to promote diversity and inclusion among financial institutions, both in terms of workforce diversity and supplier diversity. The FDIC's OMWI aims to increase outreach, technical assistance, and communication with regulated financial institutions to promote diversity and inclusion as a strategic objective. In addition, for those institutions that continue to experience challenges, the FDIC will explore opportunities to provide tools to support their efforts.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Ex-Offenders with Minor Offenses Seeking Employment

Question 13: In November 2019, the FDIC issued a proposal seeking public comment to codify its Statement of Policy related to Section 19 of the Federal Deposit Insurance Act, which provides criteria for individuals seeking employment in the banking industry with certain minor criminal offenses. In addition, the NCUA Board approved a final interpretive ruling and policy statement allowing people convicted of certain minor offenses to return to work in the credit union industry without applying for the Board's approval.

Chairman Hood and Chairman McWilliams: What steps can Congress take to give ex-offenders who have minor offenses a second chance and get a job in the banking or credit union industry?

Response:

Section 19 of the Federal Deposit Insurance Act generally prohibits an insured depository institution from hiring a person who has been convicted of a crime involving "dishonesty or a breach of trust or money laundering" without prior written consent of the FDIC. This statute has served as a barrier or impediment for individuals who have committed minor crimes from serving in the banking industry.

On November 19, 2019, the FDIC Board unanimously approved a notice of proposed rulemaking[16] to seek public comment on ways the FDIC could expand the scope of minor offenses excluded from the application of Section 19.

If Congress decides to amend Section 19 to further exclude individuals who have committed minor offenses, the FDIC stands ready to provide technical assistance if requested.

Section 19 should not be a barrier to entry for individuals who have committed minor crimes in the past, paid their debt to society, reformed their conduct, and are now seeking to gain employment with a financial institution. Since joining the FDIC, I have heard a number of stories about individuals that committed minor criminal violations when they were young and have been barred from banking.

We look forward to continuing to engage with members of Congress, civil rights organizations, financial institutions, civic organizations, and other stakeholders on Section 19 reform, as well as broader efforts to ensure that our regulations do not pose a barrier to entry for certain individuals who have committed minor crimes.

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[16] *See* Incorporation of Existing Statement of Policy Regarding Requests for Participation in the Affairs of an Insured Depository Institution by Convicted Individuals, 84 Fed. Reg. 68353 (Dec. 16, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-12-16/pdf/2019-26351.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Regulatory Gaps and Big Tech

Question 14: A growing number of concerns have been raised about the impact technology is generally having in the banking space, including questions about its impact on the traditional separation of banking and commerce. For example, this Committee continues to be focused on Facebook's plan to establish a new currency, Libra, and potentially creating a bank with more than 2 billion account holders with little to no regulatory oversight. In response to an application for an Industrial Loan Company (ILC) charter by a Japanese online retailer, the American Bankers Association and Bank Policy Institute expressed concerns with the application, writing, "The public and the FDIC would benefit from thorough public input and analysis, as the Application threatens to undermine two long-standing pillars of U.S. bank regulation—the separation of banking and non-financial businesses, and the value of consolidated supervision of banking organizations."

Vice Chair Quarles and Chairman McWilliams, do you believe there should be a separation of banking and commerce in the United States? Why or why not? If you do, what actions can regulators and Congress take to maintain or enhance the separation of banking and commerce?

Response:

Industrial loan companies (ILCs) and Industrial Banks are state-chartered, FDIC-supervised financial institutions that can be owned by financial or commercial firms.[17] Congress authorized federal deposit insurance for ILCs and Industrial Banks in 1982,[18] and exempted ILCs and Industrial Banks from the definition of "bank" under the Bank Holding Company Act (BHCA) in 1987.[19] As of December 31, 2019, there were 23 ILCs and Industrial Banks with approximately $141 billion in aggregate total assets. These ILCs and Industrial Banks are subject to the same statutory standards as other insured depository institutions (IDIs) for which the FDIC is the primary supervisor.

In determining whether to grant deposit insurance to an ILC or Industrial Bank, the FDIC must consider the same statutory factors under section 6 of the Federal Deposit Insurance Act (FDI Act)[20] that it considers for all other applications for deposit insurance, including traditional banks: (1) the financial history and condition of the depository institution; (2) the adequacy of its capital structure; (3) future earnings prospects; (4) the general character and fitness of management; (5) the risk presented by such depository institution to the DIF; (6) the convenience and needs of the community to be served by the depository institution; and (7) whether the

[17] *See* FDIC Supervisory Insights, *Supervision of Industrial Loan Companies* (Summer 2004), available at https://www.fdic.gov/regulations/examinations/supervisory/insights/sisum04/sisum04.pdf.
[18] *See* Garn-St Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469 (1982).
[19] *See* Competitive Equality Banking Act of 1987, Pub. L. No. 100–86, 101 Stat. 552 (Aug. 10, 1987).
[20] 12 U.S.C. § 1816.

depository institution's corporate powers are consistent with the purposes of the FDI Act. The FDIC must also consider whether the parent company can serve as a source of strength to the IDI, as required by Section 616 of the Dodd-Frank Act.

Although a financial or commercial firm that owns an ILC or Industrial Bank is not subject to regulation or supervision by the Federal Reserve Board at the parent holding company level because of the exemption from the BHCA, an ILC or Industrial Bank is required to enter into legally enforceable commitments with the FDIC as a required condition of approval for an ILC or Industrial Bank and their parent companies. Beginning in 2000, the FDIC has required ILCs or Industrial Banks and their parent companies to enter into Capital and Liquidity Maintenance Agreements (CALMAs) and Parent Company Agreements (PAs), which have proven to be useful as part of a comprehensive supervisory strategy to protect the IDI and address potential risks to the DIF.

CALMAs are designed to ensure that the parent financially supports the IDI and serves as a source of strength in terms of capital and/or liquidity. CALMAs require that capital contributions be made in the form of cash unless other assets are approved. Liquidity provisions in a CALMA require financial support to meet any ongoing liquidity obligations, and may require the top-tier parent company to establish a line of credit on which the IDI can draw. As a general matter, ILCs and Industrial Banks have higher capital and liquidity requirements than traditional de novo community banks.

PAs are designed to address a variety of circumstances regarding corporate governance and control exercised over the IDI and include consent of the non-bank parent to agree to examination by the FDIC. Among other items, PAs help ensure that the IDI's board and executive officers are independent of the parent company and any affiliates, that the IDI operates under a separate and distinct business plan, and that the IDI maintains separate books and records. The PAs also require the ILC or Industrial Bank to abide by the limitations on transactions with affiliates under Section 23A and 23B of the Federal Reserve Act and Regulation W. Further, the FDIC requires the ILC or Industrial Bank to adhere to the anti-tying requirements under the BHCA, insider lending limitations under Regulation O, and restrictions on conflicts of interest.

In addition to the requirements under the PA and CALMA, FDIC examiners conduct supervisory examinations of both the ILC or Industrial Bank focusing on safety and soundness, Bank Secrecy Act and Anti-Money Laundering (BSA/AML) compliance, information technology (including cybersecurity), and consumer protection. With regard to consumer protection, all ILCs and Industrial Banks are subject to the same consumer protection laws the FDIC supervises and enforces compliance with for all FDIC state non-member banks.

For example, ILCs and Industrial Banks are subject to Section 5 of the Federal Trade Commission Act (FTC Act), which provides that unfair and deceptive acts and practices

(UDAPs) affecting commerce are illegal.[21] Under Federal Trade Commission (FTC) and FDIC precedent, supervisory enforcement actions require companies to take reasonable and appropriate measures to protect consumers' personal data. The FTC and FDIC actions have focused on consumer deception either through false representations of data security or misappropriations of private data and failure to properly protect consumer data from data breaches. Further, the Gramm-Leach-Bliley Act (GLBA) applies to all companies that provide financial services, so if it is any type of financial service provider (which is broadly defined), it is subject to federal privacy and data security standards. Additionally, ILCs and Industrial Banks are subject to fair lending laws, including fair credit reporting, truth in lending, and the Community Reinvestment Act (CRA).

On March 17, 2020, the FDIC Board unanimously approved a proposed rule[22] that would impose these required conditions on all future ILC applicants.

[21] *See* 15 USC § 45(a) (Section 5 FTC Act).
[22] *See* Parent Companies of Industrial Banks and Industrial Loan Companies, 85 Fed. Reg. 17771 (Mar. 31, 2020), available at https://www.govinfo.gov/content/pkg/FR-2020-03-31/pdf/2020-06153.pdf.

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Question 15: Vice Chair Quarles, Chairman McWilliams and Chairman Hood, what is the current status of any review under way by your agencies regarding Facebook's Libra project, both as an individual agency and as a member of FSOC? Do you have the authority to prohibit banks and credit unions from accepting Libra as a form of deposit or payment?

Response:

U.S. regulatory agencies, including the FDIC, are monitoring innovation in digital assets and payments by banks and non-banks, including the use of digital currencies. At FSOC, the digital assets and distributed ledger technology working group has been monitoring this issue. In addition, the FSOC's *2019 Annual Report*[23] includes a discussion of the issue and notes that stablecoins (i.e., digital assets designed to maintain a stable value relative to another asset or a basket of assets) grew in market capitalization in 2019. At the international level, the Financial Stability Board (FSB) is also reviewing the impact of global "stablecoins"[24] and issued a public consultation[25] on regulatory issues related to stablecoins in April 2020.

[23] *See* FSOC, *2019 Annual Report*, available at https://home.treasury.gov/system/files/261/FSOC2019AnnualReport.pdf.
[24] *See* FSB, *Regulatory issues of stablecoins* (Oct. 18, 2019), available at https://www.fsb.org/wp-content/uploads/P181019.pdf.
[25] *See* FSB, *Addressing the regulatory, supervisory and oversight challenges raised by "global stablecoin" arrangements* (Apr. 14, 2020), available at https://www.fsb.org/wp-content/uploads/P140420-1.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Rent-a-Bank Schemes and Payday Loans

Question 16: Last month, the FDIC and OCC issued a proposed rulemaking to clarify that when a loan that is non-usurious when originated by a bank, it remains non-usurious if the loan is sold, assigned, or otherwise transferred to a non-bank. In 2015, the Second Circuit held in *Madden v. Midland Funding*, that non-bank debt collectors that had purchased debt originated by a national bank could not benefit from the bank's exportation power. The OCC stated the proposal is intended to "address confusion resulting from" the Madden decision. Consumer groups and legal experts have raised serious concerns that the proposal will encourage predatory rent-a-bank schemes that are designed to evade state usury caps.

Chairman McWilliams: What is the FDIC's intentions with this proposed regulation? Is it intended, in any way, to administratively override the Second Circuit decision in the *Madden* case? Is it okay for banks to effectively rent out their charter to third-parties hoping to evade state usury limits, and if not, what will stop them from doing that under your proposed regulation? If the FDIC does permit a bank to rent out the charter, is the FDIC going to supervise the payday lender to ensure that it is in compliance with FDIC regulations and applicable US laws?

Response:

On December 6, 2019, the FDIC published a notice of proposed rulemaking that would clarify the law governing the interest rates state banks may charge,[26] which Congress put in place for FDIC-regulated institutions in 1980.[27] This provision of the FDI Act has been interpreted in two published opinions of the FDIC's General Counsel in 1998.[28] The proposed rule would codify the guidance provided in those published opinions that has been in effect for over 20 years. The proposal would provide that whether interest on a loan is permissible under section 27 of the FDI

[26] *See* Federal Interest Rate Authority, 84 Fed. Reg. 66845 (Dec. 6, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-12-06/pdf/2019-25689.pdf.
[27] *See* Section 2[27(b)] of the Act of September 21, 1950 (Pub. L. No. 797), effective September 21, 1950, as added by section 521 of title V of the Act of March 31, 1980 (Pub. L. No. 96–221; 94 Stat. 164), effective March 31, 1980, provides that "[i]n order to prevent discrimination against State-chartered insured depository institutions, including insured savings banks, or insured branches of foreign banks with respect to interest rates, if the applicable rate prescribed in this subsection exceeds the rate such State bank or insured branch of a foreign bank would be permitted to charge in the absence of this subsection, such State bank or such insured branch of a foreign bank may, notwithstanding any State constitution or statute which is hereby preempted for the purposes of this section, take, receive, reserve, and charge on any loan or discount made, or upon any note, bill of exchange, or other evidence of debt, interest at a rate of not more than 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal Reserve bank in the Federal Reserve district where such State bank or such insured branch of a foreign bank is located or at the rate allowed by the laws of the State, territory, or district where the bank is located, whichever may be greater."
[28] *See* FDIC General Counsel's Opinion No. 10, 63 Fed. Reg. 19258 (Apr. 17, 1998); FDIC General Counsel's Opinion No. 11, 63 Fed. Reg. 27282 (May 18, 1998).

Act would be determined at the time the loan is made, and interest on a loan permissible under section 27 would not be affected by subsequent events, such as a change in state law, a change in the relevant commercial paper rate, or the sale, assignment, or other transfer of the loan. In addition, the proposed rule is consistent with the common law "valid when made" doctrine (i.e., usury must exist at the inception of the loan for a loan to be deemed usurious), which the Supreme Court has recognized for nearly 200 years.[29]

The preamble explained that an important benefit of the proposed rule is to uphold longstanding principles regarding the ability of banks to sell loans, an ability that has significant safety and soundness implications, and included an extensive discussion of the FDIC's legal reasoning. Further, one way the FDIC fulfills its mission to maintain stability and public confidence in the nation's financial system is by carrying out all of the tasks triggered by the closure of an FDIC-insured institution. This includes attempting to find a purchaser for the institution and the liquidation of the assets held by the failed banks.

The proposed rule affirms that the FDIC views unfavorably entities that partner with a state bank with the sole goal of evading a lower interest rate established under the law of the entity's licensing state(s). Although I am unable to address any confidential supervisory information or provide institution-specific information, I would note that the FDIC issued a public enforcement action[30] in October 2018 against Republic Bank & Trust Company for failing to clearly and conspicuously disclose required information related to the bank's Elastic line of credit product offered pursuant to a contract with Elevate@Work, L.L.C. The FDIC will continue to examine supervised institutions for compliance with all applicable laws and regulations.

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[29] *See Nichols* v. *Fearson,* 32 U.S. (7. Pet.) 103, 109 (1833) ("a contract, which in its inception, is unaffected by usury, can never be invalidated by any subsequent usurious transaction"); *see also Gaither* v. *Farmers & Merchants Bank of Georgetown,* 26 U.S. 37, 43 (1828) ("[T]he rule cannot be doubted, that if the note free from usury, in its origin, no subsequent usurious transactions respecting it, can affect it with the taint of usury.").

[30] https://orders.fdic.gov/sfc/servlet.shepherd/document/download/069t00000037a32AAA?operationContext=S1.

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Question 17: Chairman McWilliams, the FDIC joined with the OCC to file an amicus brief in support of a lender that used a Wisconsin bank to camouflage an illegal $550,000 loan that charged 120% to a business in Colorado in violation of Colorado state law. Why is the FDIC supporting what appears to be a predatory non-bank lender? And why is the agency advancing policies that could allow predatory payday lenders to evade reasonable restrictions my state of California has implemented to protect our state residents?

Response:

On September 10, 2019, the FDIC and OCC filed an amicus brief in support of a Colorado bankruptcy court's decision recognizing the validity and enforceability of the interest rate on a loan made by a Wisconsin state-chartered bank. The amicus brief is consistent with the common law "valid when made" doctrine (i.e., usury must exist at the inception of the loan for a loan to be deemed usurious), which the Supreme Court has recognized for nearly 200 years[31] and is necessary to give full effect to the exportation authority contained in section 27 of the FDI Act, which was enacted in 1980.

[31] *See Nichols* v. *Fearson,* 32 U.S. (7. Pet.) 103, 109 (1833) ("a contract, which in its inception, is unaffected by usury, can never be invalidated by any subsequent usurious transaction"); *see also Gaither* v. *Farmers & Merchants Bank of Georgetown,* 26 U.S. 37, 43 (1828) ("[T]he rule cannot be doubted, that if the note free from usury, in its origin, no subsequent usurious transactions respecting it, can affect it with the taint of usury.").

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Derisking

Question 18: Over the last decade, institutions and even whole nations and regions have lost access to financial services, including cross-border payment facilitation. This appears to be the unintended outcome of the increased focus on risk-based compliance, especially with respect to Bank Secrecy Act/Anti-Money Laundering (BSA/AML) enforcement. Unquestionably, the execution and enforcement of these laws and regulations are essential for our national and economic security. The effects of so-called "de-risking," however, have been devastating for those cut or priced out of the system, negatively affecting small and local businesses, national economies, trade relations, and even regional stability. For example, in the Caribbean, nations like Antigua and Barbuda and Saint Lucia have seen significant reductions in access to the correspondent banking services that are critical to their globally connected economies.

All Witnesses: What are your agencies doing to address this de-risking impact? What steps can examiners take to reverse this trend while still enforcing our laws to promote national security?

Response:

The FDIC encourages IDIs to serve their communities while operating in a safe and sound manner and consistent with their complexity, size, and risk profile. The FDIC has taken several actions to provide guidance to banks regarding the services offered to individual customers or particular industries. For example, in 2015 the FDIC issued a statement[32] encouraging banks to take a risk-based approach to assessing *individual* customer relationships rather than declining to provide banking services to entire categories of customers, without regard to the risks presented by an individual customer or the financial institution's ability to manage the risk. As part of that statement, the FDIC expressly states that financial institutions that can properly manage customer relationships and effectively mitigate risks are neither prohibited nor discouraged from providing services to any category of customer accounts or individual customers operating in compliance with applicable state and federal law. Recently, we have made additional efforts to ensure that this message is effectively conveyed to the institutions we supervise by ensuring that our examiner workforce is trained on these policies.

[32] *See* FDIC FIL-5-2015, *Statement on Providing Banking Services* (January 28, 2015), available at https://www.fdic.gov/news/news/financial/2015/fil15005.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Use of Alternative Data in Credit Underwriting

Question 19: Financial regulators recently issued a joint statement on the use of alternative data in credit underwriting by banks, credit unions, and non-bank financial firms.[33]

All Witnesses: in the use of alternative data, how do policymakers ensure consumer's permission to access this data is not abused? For example, how do we ensure that the data is not used for a purpose the consumer never intended such as targeted marketing after providing an initial, general consent to the company?

Response:

Consumer-permissioned access to data is an important issue. The FDIC is encouraged by the potential benefits open banking can provide in terms of innovation and competition. At the same time, we are continuing to explore how to balance these benefits with potential impacts on safety and soundness, consumer protection, and other risk considerations.

The FDIC, along with the other agencies, has been engaged with stakeholders (including banks, aggregators, fintechs, and consumer groups) on this issue for a number of years. Key issues that frequently arise in stakeholder discussions include, for example, consumer privacy, consumers' control of how their data is used, and data minimization, among others.

The U.S. approach to consumer-permissioned data access to-date has been primarily focused on market-driven initiatives, with ongoing regulatory engagement. During 2019, there were a number of significant marketplace developments related to account aggregation. For example, the Financial Data Exchange (FDX), which launched in late 2018, has made significant progress in developing and promoting a common standard for a Durable Data Application Programming Interface (the FDX API), and a number of new bilateral agreements between banks and data aggregators were finalized in 2019. To facilitate more such arrangements, in November 2019, The Clearing House developed a model agreement to help financial institutions and fintech companies establish legal terms for the sharing of bank-held consumer data. Despite progress, challenges remain, and as market-driven approaches have evolved, the FDIC has continued to engage in collaborative discussions with relevant financial regulators and industry stakeholders.

The FDIC has participated in a number of interagency meetings with industry stakeholders, including representatives of financial institutions, data aggregators, fintechs, and trade associations. The FDIC also participated in international efforts on this subject, including, for example, through the Basel Committee on Banking Supervision's Taskforce on Financial

[33] https://www.consumerfinance.gov/about-us/newsroom/federal-regulators-issue-joint-statement-use-alternative-data-credit-underwriting.

Technology, which published a report on open banking and application programming interfaces in November 2019.[34] The report discusses open banking trends observed in Basel Committee member jurisdictions and discusses the implications of these developments on banks and banking supervision.

The FDIC continues to monitor the account aggregation marketplace, engage in collaborative discussions, evaluate marketplace developments, and take appropriate actions based on our statutorily defined roles and responsibilities.

[34] *See* Basel Committee on Banking Supervision, "Report on open banking and application programming interfaces" (Nov. 19, 2019), available at https://www.bis.org/bcbs/publ/d486.htm.

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Question 20: All Witnesses: the interagency statement states that, "Based on that analysis, data that present greater consumer protection risks warrant more robust compliance management." What kind of alternative data, or uses of that data, are your agencies referring to that has "greater consumer protection risks"?

Response:

The interagency statement states that, in the context of an effective compliance management program, data that present greater consumer protection risks warrant more robust compliance management. The statement was not referring to any specific kind of alternative data, but rather stating that data that present greater consumer protection risks warrant more robust compliance management. The statement emphasizes that an effective compliance management program for firms considering using alternative data includes performing a thorough analysis that considers opportunities, risks, and compliance requirements. This analysis, in turn, can be used by firms to make their own determinations of the consumer protection risks associated with using particular types of data or particular use cases.

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Question 21: All Witnesses: the statement does not discuss racial or gender disparities that may exist in alternative data, especially when combined with artificial intelligence and machine learning. What steps will your agencies take to prevent the use of opaque algorithms or AI that may result in discriminatory outcomes in credit underwriting and other uses of alternative data?

Response:

The FDIC's supervisory program includes fair lending reviews as a component of every consumer compliance examination performed to assess whether supervised institutions are meeting their responsibilities to comply with the Fair Housing Act (FHA) and, for institutions with assets of $10 billion or less, the Equal Credit Opportunity Act (ECOA). When conducting a fair lending review, FDIC examiners use the Interagency Fair Lending Examination (IFLE) Procedures to evaluate compliance with the ECOA and FHA, detect any fair lending risks in an institution's operations, and consider any factors that may mitigate the risks.

The IFLE Procedures call for evaluating credit scoring systems and risk-based pricing models, among other information. The Appendix to the IFLE Procedures discusses how examiners develop and support fair lending conclusions in situations that involve automated underwriting or credit scoring. These procedures call for consideration of critical information regarding credit scoring models and scorecards, such as the developer of each scorecard and the development population used, the types and frequency of monitoring reports generated, the policies applied to the use of credit scoring, action taken to revalidate or recalibrate any model or scorecard, the variables used, and the values the variables may take. In addition, the IFLE Procedures direct examiners to consider such issues as whether third parties are involved in a credit decision and how responsibility is allocated among the institution and any third parties.

Through a risk-focused review of an institution's lending activities and any third-party relationships, the FDIC addresses any violations of federal fair lending laws. The FDIC's fair lending program is designed to identify such violations whether they occur based on the use of algorithms or otherwise. As the financial technology landscape continues to evolve and expand rapidly, the FDIC will continue to monitor and analyze the results of fair lending reviews in order to detect trends in the credit practices of supervised IDIs, including trends related to financial technology developments.

In addition, the FDIC reviews published research to monitor any observable trends from the use of algorithms and other modeling techniques on credit availability and pricing. Last year, the FDIC held a conference, "Fintech and the Future of Banking," to bring together researchers and other stakeholders to explore the impact of technology and fintech firms on the banking industry. The FDIC plans to continue to convene stakeholders to gain a deeper understanding of technological developments and their impacts on relevant stakeholders, including consumers.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Mobilizing Finance Against Slavery and Human Trafficking

Question 22: One area of interest for this Committee is how the financial sector can better combat the crime of human trafficking. A recent report— "A Blueprint for Mobilizing Finance Against Slavery and Trafficking," prepared by the Financial Sector Commission on Modern Slavery and Human Trafficking— identified the need to strengthen AML tools in relation to addressing modern slavery and human trafficking. In particular, the report highlighted the importance of developing transaction analysis tools to better "identify proceeds of modern slavery and human trafficking in all areas of financial sector activity", especially as it relates to more difficult cases which often involve labor trafficking, debt bondage and forms of modern slavery and human trafficking occurring in the developing world. Furthermore, the report stated, in the case of financing involving sectors with known higher risks of forced labor, anti-slavery and anti-trafficking measures could be developed as part of the loan conditions.

All Witnesses: What is your agency doing to encourage the development of these analytical tools and investments in data innovations, with a specific emphasis on identifying activity related to human trafficking?

Response:

The FDIC, along with the other federal banking agencies and FinCEN, issued a joint statement[35] on December 3, 2018 to encourage depository institutions to consider, evaluate, and, where appropriate, responsibly implement innovative approaches to meet their BSA/AML compliance obligations in order to strengthen the financial system against illicit financial activity. The agencies recognize that private sector innovation, including new ways of using existing tools or adopting new technologies, can help banks identify and report money laundering, terrorist financing, and other illicit financial activity by enhancing the effectiveness and efficiency of their BSA/AML compliance programs. The FDIC is open to engaging with bank management to discuss pilot programs for innovative BSA/AML approaches.

Currently, the FDIC is working closely with the financial services industry through the auspices of the Bank Secrecy Act Advisory Group (BSAAG) on multiple AML initiatives that address effectiveness, including by transmitting useful and timely information to law enforcement. An issue under consideration is more timely identification of financing associated with crimes such as human trafficking. In that context, multiple BSAAG initiatives are aimed at more quickly adapting to and identifying financial transactions and customer behavior that is suspicious and possibly indicative of activities such as human trafficking. That is a challenging problem that has been raised and highlighted by many financial institutions and law enforcement. The FDIC

[35] *See* FDIC FIL-79-2018, *Bank Secrecy Act: Interagency Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing* (Dec. 3, 2018), available at https://www.fdic.gov/news/news/financial/2018/fil18079.html.

is an engaged partner in evaluating innovative and technological solutions for meeting suspicious activity reporting requirements.

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Question 23: All Witnesses: What is your agency doing to support better identification of risks relating to human trafficking within the financial sector and the steps needed to mitigate these risks?

Response:

FinCEN issued an advisory in 2014 to help financial institutions detect and report suspicious activity that could be related to human smuggling or human trafficking. Issues relating to human trafficking detection and prevention are regularly addressed in bank examiner training events and conferences. Specifically, the FFIEC Advanced BSA/AML Specialists Conference included presentations on human trafficking detection and prevention in 2016, 2017, and 2019. This conference is an annual event designed to provide continuing education to examiners with specialized BSA experience within the financial institution regulatory agencies. The emphasis is on advanced BSA/AML topics and emerging supervisory issues related to institutions with greater complexity in terms of products, services, customers, and geographical locations.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Housing Counseling

Question 24: HUD-approved housing counseling agencies work primarily with low and moderate income households, preparing homebuyers for responsible homeownership and helping financially challenged homeowners work with their mortgage servicer to get a loan workout or other solution. Recent studies have shown very positive outcomes that are achieved by families who receive housing counseling, including significantly lower default rates and more successful loan modifications. However, due to shrinking funding, housing counseling agency capacity has been shrinking rather than growing to meet the need.

All Witnesses: Given the effectiveness of housing counseling in helping low- and moderate-income households to help themselves to responsibly become homeowners, what are you doing as a regulator to promote the use of housing counseling for potential customers of your regulated entities?

Response:

The FDIC has a long history of promoting housing counseling for consumers and regulated entities through community events, collaboration with industry and agency partners, and financial education resources. Every year, the Community Affairs branch of the FDIC collaborates with numerous housing counseling agencies on community-related programs, including affordable housing roundtables and financial education events. In 2019, the FDIC facilitated 50 events nationwide focused on affordable housing drawing about 800 intermediaries, and convened over 25,000 attendees at 227 events focused on financial education. Local housing counseling agencies were frequently a partner and participant in these efforts.

The FDIC also promotes housing counseling by offering CRA credit to banks that support housing counseling efforts. Housing counseling is a community development activity under the CRA, and FDIC examiners provide consideration to banks that support housing counseling during their CRA Evaluations. Community Affairs complements the work of FDIC bank examiners by helping banks identify potential collaboration opportunities related to housing counseling.

The FDIC also provides information on housing counseling through various outlets. The FDIC's Affordable Mortgage Lending Center[36] features information on homeownership education and includes links to housing counseling resources provided by the Department of Housing and Urban Development (HUD) and the Consumer Financial Protection Bureau. The FDIC also

[36] *See* FDIC, Community Affairs – Affordable Mortgage Lending Center, available at https://www.fdic.gov/consumers/community/mortgagelending/index.html.

partners with HUD to conduct training webinars that promote Money Smart,[37] the FDIC's free financial education curriculum for HUD-approved housing counseling agencies. Other FDIC resources to educate consumers on housing counseling are provided through Consumer News publications, which feature articles on home buying and counseling resources. Examples of the FDIC's efforts to promote housing counseling include the following:

- The FDIC Dallas Regional Office conducted a CRA Banker Roundtable in Lubbock, Texas, regarding challenges to homeownership. As a result, participants agreed to bank collaborations with Certified Development Financial Institutions to deliver homebuyer and credit counseling assistance.

- The FDIC New York Regional Office and the Federal Reserve Bank of Richmond convened a Housing Counselor Connection Forum in Columbia, Maryland, focused on providing housing and financial counselors training on homebuyer education, foreclosure intervention, financial coaching, and counseling.

- The FDIC Chicago Regional Office and Office of the Comptroller of the Currency hosted a community development listening session with stakeholders serving low- to moderate-income communities in Columbus, Ohio. Participants identified foreclosure prevention education and housing counseling opportunities as a potential solution to address community needs.

[37] *See* FDIC, Money Smart – A Financial Educational Program, available at https://www.fdic.gov/consumers/consumer/moneysmart/index.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Appraisals

Question 25: Banking regulators have recently determined that raising appraisal thresholds would not be in the public's interest. Specifically, in 2017, after a multiyear review that included several public hearings and open comment requests, banking regulators submitted a "Joint Report to Congress on the Economic Growth and Regulatory Paperwork Reduction."[38] The Joint Report stated:

> "The agencies also considered safety and soundness and consumer protection concerns that could result from a threshold increase for residential transactions. The last financial crisis showed that, like other asset classes, imprudent residential mortgage lending can pose significant risks to financial institutions. In addition, the agencies recognize that appraisals can provide protection to consumers by helping to assure the residential purchaser that the value of the property supports the mortgage amount assumed. Overall, the agencies believe that the interests of consumers are better served when appraisal regulations are coordinated among government agencies."

Yet, in September, the federal banking agencies' issued a final rule to increase the residential appraisal threshold from $250,000 to $400,000, which was approved with the CFPB's concurrence. Under the rule, 72%, or nearly 3 out of 4, home mortgage transactions in the U.S. are now exempt from appraisal requirements, putting taxpayers at serious risk for any future calamity related to the housing market. Furthermore, over 500 comments were received on the proposed rule with a majority in strong opposition to increasing threshold amounts, including 38 consumer and public interest organizations. Many of these organizations requested a public hearing to discuss this issue, but their suggestion was dismissed.

In addition, the NCUA recently issued a similar proposed rule which would align its appraisal requirements with the federal banking agencies as well as approved a final rule which increases the non-residential appraisal threshold level to $1 million, a move that contradicts the final rule that increased the commercial real estate appraisal threshold level to $500,000 for federally regulated banks. I understand this is the first time in history that the NCUA has stepped ahead of the banking agencies on appraisal requirements.

As we attempt to reconcile apparent inconsistencies between the Joint Report to Congress and your recent regulatory actions to increase appraisal thresholds, please respond to the following:

All Witnesses: Did any of your agencies take any supervisory or enforcement actions during or after the financial crisis that related to appraisal and underwriting deficiencies? If yes, does this

[38] https://www.ffiec.gov/pdf/2017_FFIEC_EGRPRA_Joint-Report_to_Congress.pdf.

not suggest there were safety and soundness concerns relating to appraisals in the lead up to the financial crisis a decade ago?

Response:

The Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) amended the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) to exempt from appraisal requirements certain federally related, rural real estate transactions below $400,000 if no certified appraiser is available. The agencies reviewed our appraisal requirements after the enactment of EGRRCPA, including the threshold for all federally related real estate transactions (i.e., not just transactions in rural areas), which had not been raised or adjusted since 1994 even though home prices increased in the 25 intervening years. After adjusting for inflation, the $250,000 threshold set in 1994 would be over $429,000 as measured by the Consumer Price Index (CPI), a measure of the average change over time in the prices paid by urban customers for a market basket of goods and services.[39] While undertaking this analysis, the agencies relied on the 2017 report to Congress, additional stakeholder outreach, and public comments to determine whether to increase the threshold for all federally related real estate transactions pursuant to Title XI of FIRREA.

The proportion of transactions covered by the exemption at $400,000, excluding mortgages guaranteed or insured by the federal government or sold to the government-sponsored enterprises, is less than half what it was after the threshold was raised in 1994. Meanwhile, the additional exempted transactions would have amounted to just 3 percent of total originations in 2017.

The FDIC did take supervisory and enforcement actions during and after the 2008 financial crisis that related to deficiencies in institutions' property valuation processes, including with respect to both evaluations and appraisals, and underwriting deficiencies. It should be noted that the FDIC Office of Inspector General in its *Comprehensive Study on the Impact of the Failure of Insured Depository Institutions*[40] did not list concerns with appraisals or evaluations as a common contributing cause of material loss failures.

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[39] *See* Real Estate Appraisals, 84 Fed. Reg. 53579 (Oct. 8, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-10-08/pdf/2019-21376.pdf.

[40] *See* FDIC Office of Inspector General, Report to the Congress, Comprehensive Study on the Impact of the Failure of Insured Depository Institutions (Jan. 2013), available at https://www.fdicoig.gov/sites/default/files/publications/13-002EV.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 26: Vice Chair Quarles and Chairman McWilliams: Appraisal problems was a contributing factor to the last financial crisis identified by the FDIC's Inspector General report entitled, "Comprehensive Study on the Impact of the Failure of Insured Depository Institutions." In fact, the word "appraisal" is used 345 times in the report. Did the banking agencies review this report or related Material Loss Review reports examining bank failures during the financial crisis in determining there are no safety and soundness concerns relating to appraisals? If not, why not?

Response:

The FDIC reviewed the Comprehensive Study and considered various Material Loss Review (MLR) reports during its analyses. The FDIC's review of MLRs reflected that appraisals were not a significant factor in the failures. These findings are consistent with those of the FDIC OIG in that the Comprehensive Study did not list concerns with appraisals or evaluations as a common contributing cause of material loss failures, as reflected in Table 6 on page 50 of the Comprehensive Study below.

Most Common Contributing Causes of Material Loss Failures	FDIC	OCC	FRB
High ADC or CRE Concentrations	95%	86%	100%
Rapid Asset Growth	69%	82%	82%
Relying on Volatile Funding Sources to Support Growth	55%	27%	14%
Inadequate Loan Underwriting	70%	50%	23%
Inadequate Credit Administration Practices	71%	55%	27%
Inadequate Credit Risk Management	76%	77%	73%

Source: OIG analysis of 131 MLR reports for 142 institutions that failed from January 2007 through September 2011.

The FDIC OIG's findings reflect that the FDIC was identifying and addressing appraisal-related safety and soundness concerns during its supervisory process. The FDIC OIG's findings also reflect that while some financial institutions had appraisal-related safety and soundness concerns, such concerns were not a significant contributing cause of material loss failures during the 2008 financial crisis.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 27: Vice Chair Quarles and Chairman McWilliams: Why were the dates of January 2017-December 2018 chosen to review Reports of Examination, given 2018 was the first year since 2006 without a bank failure?

Response:

Last year, the federal financial institution regulators issued a final rule[41] to increase the threshold level for residential real estate transactions. The rule notes that "[a]s part of the agencies' consideration of the safety and soundness implications of the proposed threshold increased, the agencies reviewed safety and soundness Reports of Examination. Regarding examination experience, the agencies reviewed Reports of Examination of their respective supervised institutions from January 2017 to December 2018 for examiner findings regarding appraisals and evaluations. Both appraisals and evaluations were cited in examiner findings, however, the overall amount and nature of valuation-related examination findings support a conclusion that the proposed threshold increase would not threaten the safety and soundness of financial institutions."

There are two primary reasons for the decision to conduct a review of the 900 safety and soundness Reports of Examination from January 2017 through December 2018 that detailed any type of valuation-related issues. First, the agencies sought a better understanding of more recent valuation-related concerns. Second, this timeframe provided a sufficient period after the implementation of the Qualified Mortgage Rule in 2014 for that rule to have had an impact on residential mortgage lending.

[41] *See* Real Estate Appraisals, 84 Fed. Reg. 53579 (Oct. 8, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-10-08/pdf/2019-21376.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 28: All Witnesses: Please provide aggregate year-by-year data on examiner findings regarding appraisals and evaluations since enactment of Title XI of FIRREA.

Response:

The FDIC conducts thousands of safety and soundness examinations each year. A review of valuation programs, including a review of individual appraisals and evaluations, is a standard part of the examination process for real estate credits. The FDIC does not maintain aggregate year-by-year data on examiner findings regarding appraisals and evaluations.

While FDIC-supervised financial institutions generally engage in residential and commercial real estate transactions in a manner that complies with regulatory requirements for appraisals and evaluations, FDIC staff will cite apparent violations of Part 323, which covers appraisals and evaluations, when deemed appropriate and seek management commitments for corrective action. The FDIC reserves the right to require an appraisal under Part 323 whenever the agency believes it is necessary to address safety and soundness concerns.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Chairwoman Maxine Waters:

Question 29: All Witnesses: With respect to oversight of individuals conducting evaluations, what recourse does a consumer have who may have issues arising from an evaluation product, which currently has no regulatory oversight?

Response:

Financial institutions' use of evaluations is subject to review by their primary federal regulator during the supervisory process. The 2019 final rule notes that "[t]he agencies have implemented examination procedures to frame their review of an institution's valuation practices and the sufficiency of the supporting information in evaluations, as appropriate for the size and nature of the institution's residential real estate lending activities. The agencies have used these procedures to assess the use of evaluations and ensure that they are prepared according to safety and soundness principles and will continue to examine institutions' evaluation policies and practices."

Consumers may raise issues with an evaluation product directly to the lender, which can address specific issues with the individual who prepared the evaluation, or choose to obtain another valuation product, such as an appraisal. Consumers also can submit a complaint regarding an evaluation with a financial institution's primary federal regulator[42] or contact the Office of the Ombudsman of the primary federal regulator if the consumer prefers to remain anonymous.[43] In addition, consumers can file a complaint with the appropriate state agency in states with laws requiring the licensing of individuals who perform evaluations.

[42] *See* Interagency Appraisal Complaint Form, available at https://ask.fdic.gov/FDICInteragencyForm.
[43] *See* FDIC Comment Form, available at https://ask.fdic.gov/fdiccommentform.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Benjamin McAdams:

Question 1: In general, we want to promote and encourage the long-term growth of companies. Such growth can help companies innovate and create new jobs – but such growth is often dependent on a variety of sources of capital, including directly from banks. I support the policy behind the Volcker Rule to prevent banks from engaging in short-term proprietary trading directly. However, it is my understanding that some provisions of the rule, specifically aspects of the covered funds provisions, may prohibit long-term investments if such investment is made using a fund structure. Chairman Powell has previously testified that a bank's long-term investments in covered funds is not an activity that typically threatens safety and soundness.

In the 2019 final rule related to the Volcker Rule, the agencies stated that they "continue to consider comments received and intend to address additional aspects of the covered funds provisions in the future covered funds proposal."

In this forthcoming rulemaking, do you expect to provide additional certainty to banks through an exclusion for investments in long-term investment vehicles in order to allow additional sources of capital for growing companies?

Response:

On January 30, 2020, the FDIC Board approved a proposed rule[44] that would amend the regulations implementing Section 619 of the Dodd-Frank Act (the Volcker Rule) by modifying and clarifying the "covered fund" provisions. Among other things, the proposal would establish a new exclusion from the covered fund definition for venture capital funds, which would allow banking entities to acquire or retain an ownership interest in, or sponsor, certain venture capital funds to the extent the banking entity is permitted to engage in such activities under otherwise applicable law. This proposed exclusion would help ensure that banking entities can fully engage in this important type of development and investment activity, which may facilitate capital formation and provide important financing for small businesses, particularly in areas where such financing may not be readily available.

[44] *See* Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds, 85 Fed. Reg. 12120 (Feb. 29, 2020), available at https://www.govinfo.gov/content/pkg/FR-2020-02-28/pdf/2020-02707.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Alexandria Ocasio-Cortez:

Community Reinvestment Act

Question 1: Nearly half of NYC renters live in rent-stabilized multifamily apartment buildings. This stock of housing remains one of the most important sources of private, more affordable housing in New York City, particularly for constituents like mine in Queens and the Bronx. Rent-stabilized tenants are more likely to be Hispanic than non-regulated tenants and less likely to have a college degree. Rent-stabilized tenants are more likely to be low-income and on some form of public assistance. Rent-stabilized housing also provides tenants with critical protections, including the right to renew a lease, limited rent increases, and the right to organize.

In the past 23 years, NYC has seen a net loss of over 147,500 units of rent-stabilized housing. Historically, predatory equity landlords have routinely used loopholes in the law and in some cases flagrantly flouted the law to raise the rents and harass and displace tenants, disproportionately impacting low-income people, people of color, and immigrants. They use all sorts of tactics to displace tenants, deregulate apartments, and raise rents, including outright harassment and intimidation, failure to make repairs, threatening to call ICE, and dangerous construction leading to lead contamination in children. The list goes on and on. Even with some loopholes recently closed in New York, landlords can continue to raise rents through other means, cut back on expenses, and find other ways to skirt regulation. And outside of NYC, these protections barely exist.

Landlords can't do this without financing, which comes from investors and lenders, many of which are CRA-regulated banks. When lenders make loans that are too high for the rents to support, low-income tenants suffer as landlords must either forego maintenance or use these and other tactics to push out lower-income, lower-rent paying tenants to bring in higher-paying tenants. When banks lend to landlords with known records of poor conditions, harassment and displacement, tenants suffer as they now face these harsh conditions and pressures. Displacement can impact renters and also small businesses and nonprofits who can no longer afford their rent. Reports from California and elsewhere raise similar concerns about the financing of displacement of low income people and people of color.

a) We see nothing in the OCC's ANPR or more recent brochure indicating there will be stronger consequences for displacement. And in fact, with a rating based strictly on volume, the chances look even worse. Can you explain how displacement financing will be deterred through the new CRA proposals?
b) Is it true that banks can get CRA credit for loans they knew or should have known would lead to, and/or did in fact lead to, displacement?
c) Should banks be able to get credit for these types of loans?
d) How can the CRA be strengthened to stem the tide of displacement, penalize banks when they fuel displacement with their loans or investments, and encourage responsible lending?

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Response:

On December 12, 2019, the FDIC and OCC approved a notice of proposed rulemaking[45] to modernize the regulations implementing the CRA, which had not been substantively updated for nearly 25 years. The proposed rule was intended to increase bank activity in LMI communities where there is significant need for credit, encourage more responsible lending, and promote improvements to critical infrastructure. On May 20, 2020, the OCC adopted a final rule implementing the proposed changes to the CRA regulations. The FDIC strongly supports the efforts to make the CRA rules clearer, more transparent, and less subjective. However, the agency was not prepared to finalize the CRA proposal at that time, and FDIC-regulated banks continue to comply with the same CRA framework as they did before the proposal.[46]

[45] *See* Community Reinvestment Act Regulations, 85 Fed. Reg. 1204 (Jan. 9, 2020), available at https://www.govinfo.gov/content/pkg/FR-2020-01-09/pdf/2019-27940.pdf.
[46] *See* Statement by FDIC Chairman Jelena McWilliams on the CRA Joint Proposed Rulemaking (May 20, 2020), available at https://www.fdic.gov/news/news/speeches/spmay2020.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Alexandria Ocasio-Cortez:

Access to Banking & Affordable Housing

Question 2: The CRA was passed in response to redlining and disinvestment among low-income people of color and neighborhoods. CRA is most impactful when banks are responding to local needs and evaluated based on the impact of their dollars, not merely the dollars invested. Roughly 330,000 units of affordable housing have been built since the CRA passed, a third of which was built by nonprofit developers. In high-cost large cities like NYC, these same families struggle to access credit, and are often prone to displacement when irresponsible investment comes into their neighborhoods. This is particularly harmful when, say, a bad acting landlord rents to low-income people and then displaces them through harassment, disinvestment, or other tactics. But other large-scale developments can also lead to displacement of small businesses and cultural institutions.

Further, 7.9% of households are completely unbanked in the NY metro area, well above the 6.2% unbanked nationwide. In the same area, 15% of Black households and 18% of Hispanic households are unbanked, as are close to a third of households earning under $30,000. Communities of color throughout NYC have long lacked adequate access to bank branches and products.

a) How can the CRA be strengthened to increase access to bank branches and banking for underserved New Yorkers? Particularly low-income, people of color, immigrants, and seniors.

Response:

The notice of proposed rulemaking would have maintained the importance of branches in assessing a bank's record of serving its communities by requiring banks to designate assessment areas surrounding branches, headquarters, and deposit-taking ATMs and including an evaluation of a bank's distribution of branches when assessing the impact of CRA activities. The notice of proposed rulemaking set forth numerous questions on the proposed approach, including whether it appropriately incentivizes banks to place or retain branches in specified areas of need, including LMI areas.

b) How can the CRA be strengthened to encourage impactful loans and investments, large and small, that lead to long-term affordable housing, deep affordable housing, access to quality jobs?

Response:

The proposal would have expanded the investments in affordable housing that qualify for CRA credit by, among other things, including rental housing for LMI individuals and middle-income

individuals in high-cost areas. The proposal would have clarified the criteria to incentivize banks to meet the affordable housing needs of their communities through a variety of activities including workforce housing that would allow public employees – such as teachers, police officers, and firefighters – to live close to the communities they serve.

c) How will banks be deterred from supporting displacement financing, and penalized when they do so? How will you ensure that community needs and input are strong components of the CRA?

Response:

The proposal sought to encourage banks to increase lending and financial services provided to or benefitting LMI individuals, including, for example, by no longer providing CRA credit for mortgage loans to high-income individuals living in low-income census tracts.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative J. French Hill:

Question 1: Chair McWilliams, banks in my district have concerns that the FDIC spends more time on their "large bank" exam process, meaning banks with between $10 and $50 billion in assets, than the Federal Reserve or the OCC. Have you found this to be the case? Is the exam process for large banks similar across the agencies? Do you coordinate with the other prudential regulators to ensure similar processes?

Response:

In my conversations with FDIC-supervised institutions, I have heard concerns about certain aspects of the examination process, including the length of time. There are challenges in making accurate comparisons across regulatory agencies due to differences in each agency's supervision and examination programs and the specific risks and business models of supervised institutions in each agency's portfolio, and the length of our examinations depends on these factors. My staff is looking into this issue and will address these concerns as appropriate.

With respect to coordination, FDIC examinations of banks between $10 billion and $50 billion in assets are closely coordinated with state authorities and other federal banking agencies, as appropriate. The FDIC applies a risk-focused examination approach to institutions that it directly supervises, and examination hours are driven by the risk profile and complexity of each institution. For FDIC-supervised institutions with more than $10 billion in assets, staff develops an annual supervisory plan in coordination with all relevant external stakeholders that outlines onsite review schedules, offsite monitoring activity, responsibilities, and projected resource needs for the coming year. These supervisory plans are thoroughly vetted and independently reviewed for consistency with established internal guidelines. Additionally, FDIC staff periodically compares examination plans and processes with those of other supervisory authorities relative to similar size banks to ensure that our program is consistent, efficient, and effective. We also meet regularly with federal and state banking agencies to discuss examination priorities and other supervisory matters.

In developing supervisory plans and planning for a specific targeted review, FDIC staff are aware of other regulators' examination planning timelines and strategies and ensure communication is sufficient to address any changes in targeted reviews throughout the examination cycle. State agencies are an integral part of the supervisory process for FDIC-supervised banks with more than $10 billion in assets. Furthermore, staff closely coordinate in areas such as exam scheduling, participation in target reviews, management meetings, training initiatives, sharing of offsite analysis, and development of examination findings and reports.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative J. French Hill:

Question 2: Chair McWilliams and Vice Chair Quarles, I have heard from banks in my district that the enforcement actions for BSA compliance have increased without updated guidance from the prudential regulators. What are the prudential regulators doing to ensure a joint approach to help provide more clarity to banks with regards to the BSA examination process?

Response:

The FDIC, along with the other federal banking agencies and FinCEN, issued a joint statement[47] on July 22, 2019 to clarify the risk-focused approach to examinations of banks' BSA/AML compliance programs. The statement is intended to improve transparency into the risk-focused approach used for planning and performing BSA/AML examinations and does not establish new requirements. Concepts of that statement were also incorporated into the 2019 safety and soundness training that was delivered to all commissioned examiners, case managers, and management.

The statement emphasized that banks structure their compliance programs to be risk-based and to identify and report potential money laundering, terrorist financing, and other illicit financial activity. Federal banking agencies tailor BSA/AML examination plans and procedures based on the unique risk profile of each bank. The extent of examination activities necessary to evaluate a bank's BSA/AML compliance program generally depends on the risk profile of the bank and the quality of processes implemented by the bank to identify, measure, monitor, and control risk and to report potential money laundering, terrorist financing, and other illicit financial activity.

[47] *See* FDIC FIL-43-2019, *Bank Secrecy Act: Interagency Statement on Risk-Focused Bank Secrecy Act/Anti-Money Laundering Supervision* (July 22, 2019), available at https://www.fdic.gov/news/news/financial/2019/fil19043.html.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Anthony Gonzalez:

Question 1: I appreciate the insights provided by the regulators in their Interagency Statement on the Use of Alternative Data in Credit Underwriting. I am deeply committed to helping the underserved access credit to help themselves and their families and I think that AI and the use of alternative data points could be a part of the solution. As a part of the AI Task Force I have learned about the attendant issues here and would love for either of you to expound on what the statement refers to as the potential for a "second look" for applicants that may have been denied under legacy underwriting and scoring systems and what that second look might mean for their ability to ultimately access credit?

Response:

In the context of the policy statement, a "second look" refers to a program in which a firm chooses to use alternative data only for those applicants who would otherwise be denied credit. In these cases, consumers who would be denied credit based on traditional credit data are reevaluated based on data that was not used in the initial review. For example, a 2019 report[48] notes that "in at least one case, the company uses the cash-flow data to assess applicants who do not pass an initial screen using more traditional criteria. In such 'second look' models, the cash-flow variables may enable credit to be extended to consumers who otherwise would have been denied credit using only the 'first look' attributes." The interagency statement highlights that, used in this fashion and in compliance with applicable consumer protection laws, second look programs may improve credit opportunities.

[48] *See* FinRegLab, "The Use of Cash-Flow Data in Underwriting Credit" (July 2019), available at https://finreglab.org/wp-content/uploads/2019/07/FRL_Research-Report_Final.pdf.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Anthony Gonzalez:

Question 2: At the end of your statement you assert that the agencies "may" provide more guidance on the use of alternative data. Can you pledge to me that you will work in tandem on all things related to any clarification of existing regulations and guidance related to AI, and that you will work with the CFPB as well, which is not represented here today? It is so important that we have regulatory consistency on these issues, issues like model risk guidance and things like the use of alternative data as well as fair lending related matters. Will you pledge to work on an interagency basis?

Response:

As you note, the interagency statement states that, as the agencies gain a deeper understanding of alternative data usages, we may offer further information on the appropriate use of alternative data. In addition, I have publicly expressed an interest in developing guidance for banks that use AI and ML. I appreciated your question on this issue during the hearing on December 4, 2019, and pledge to make every effort to coordinate with fellow regulators on this matter. I would note that agency staffs have already been engaging in discussions on this issue.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Anthony Gonzalez:

Question 3: I have a question about the regulatory workforce. AI and machine learning tools are powerful and complex. The race for talent for those that focus on these issues is competitive. Do you think regulators are well equipped to properly supervise the use of these powerful new tools using the existing framework? Do regulators have the required personnel in place to understand these tools and work with industry to address any concerns? I know regulators have lots of lawyers and economists, but do you all have lots of data and computer scientists as well?

Response:

The FDIC's ability to fulfill its mission depends on having an experienced, knowledgeable, and agile workforce. In order to keep pace with the rapidly changing banking environment, including the increasing use of AI and machine learning by supervised institutions, the FDIC has taken several steps to create the workforce of the future. Last year, the FDIC established a new office of innovation, the FDIC Tech Lab (FDiTech), with a focus on how to best utilize technology to meet consumer demands while maintaining safety, soundness, and consumer protection. We are seeking a wide range of technologists to join this office, including a Chief Innovation Officer, data scientists, process engineers, software developers, and network security experts. Our supervision and compliance programs are also focusing on hiring candidates with the technical skills needed to effectively execute our examination mission, including individuals with skills in technology, data science, quantum computing, and other STEM-related fields.

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Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Anthony Gonzalez:

Question 4: When is the insured depository institution resolution planning rule (IDI Rule) going to be finalized? For many institutions, the IDI resolution plan would normally be due July 1, 2020 under current rules. But in connection with the April 2019 Advanced Notice of Proposed Rulemaking, the FDIC voted to delay the next round of submissions under the IDI Rule until the rulemaking process has been completed. It's unclear whether firms should continue planning for an IDI resolution plan submission in 2020, and how much notice firms might be given. For example, if the rulemaking were completed in early 2020, that leaves very little time to complete a July submission.

Response:

On April 22, 2019, the FDIC issued an advance notice of proposed rulemaking (ANPR) seeking comment on potential changes to the resolution planning rule for IDIs.[49] The next step is to issue a notice of proposed rulemaking (NPR). Following the issuance of the NPR, the FDIC will provide a period of time for the public to comment on the proposal, and then the FDIC will review comments prior to issuing a final rule. In connection with approving the ANPR last year, the FDIC Board voted to delay the next IDI resolution plans until the rulemaking process is completed. Once a final rule is issued, the FDIC will ensure that firms have adequate time to prepare and submit any required resolution plans.

[49] *See* Resolution Plans Required for Insured Depository Institutions With $50 Billion or More in Total Assets, 84 Fed. Reg. 16620 (Apr. 22, 2019), available at https://www.govinfo.gov/content/pkg/FR-2019-04-22/pdf/2019-08077.pdf.

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December 4, 2019

Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Denver Riggleman:

Question 1: I commend the Fed, FDIC, FinCEN, OCC, and CSBS on the joint statement to "provide clarity regarding the legal status of commercial growth and production of hemp and relevant requirements for banks." The statement goes on to say that since hemp has been de-scheduled via the farm bill that SARs are no longer required because it is a transaction involving hemp and that banks should follow standard BSA / AML procedures on these accounts. Finally, the statement says that FinCEN will issue additional guidance after further review of the USDA's rule. What has the FDIC and Fed done to limit redundant or unnecessary SARs, and what can your agencies do to work with FinCEN to ensure that whatever guidance is issued is done so expediently and in a manner that is clear and concise for both examiners and financial institutions, especially regarding hemp banking?

Response:

During 2019, all FDIC safety and soundness examiners, case managers, and managers received training emphasizing that filing a suspicious activity report (SAR) on customers solely because they are engaged in the growth or cultivation of hemp in accordance with applicable laws and regulations is not required. The FDIC anticipates that this direct, relevant, and timely training will reduce the amount of unnecessary SAR filings relative to hemp-related customers. Additionally, the FDIC has provided banks with a point of contact for hemp-related inquiries. As needed, the FDIC will collaborate with FinCEN as it develops guidance in this area.

U.S House Committee on Financial Services
"Oversight of Prudential Regulators: Ensuring the Safety, Soundness, Diversity, and Accountability of Depository Institutions?"
December 4, 2019

Questions for The Honorable Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation, from Representative Denver Riggleman:

Question 2: Has your agency engaged with any of the public private partnerships that are driving a consensus driven AML reform, and if so, will your agency be releasing any of the results or findings to the public?

Response:

The FDIC is an active member of the Bank Secrecy Act Advisory Group (BSAAG) and associated working groups. We regularly participate in and contribute to the AML Effectiveness Working Group, which has developed recommendations to reform and modernize the U.S. AML/Countering the financing of terrorism regime to be more effective and efficient.

The BSAAG, which consists of representatives from federal regulatory and law enforcement agencies, financial institutions, and trade groups, is the means by which the Treasury receives advice on the operations of the Bank Secrecy Act. As chair of the BSAAG, the Director of FinCEN is responsible for ensuring that relevant issues are placed before the BSAAG for review, analysis, and discussion. Ultimately, the BSAAG will make policy recommendations to the Secretary on issues under consideration.

Importantly, BSAAG AML Effectiveness Working Group recommendations that directly impact the FDIC's authority will be considered and implemented, as appropriate, by our agency.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Chairwoman Waters:

Community Reinvestment Act

We discussed the importance of the Community Reinvestment Act (CRA) and its implementation during the hearing. Shortly following the hearing, the OCC and the FDIC issued a notice of proposed rulemaking (NPR),[1] which FDIC Board Member Martin Gruenberg characterized as, "a deeply misconceived proposal that would fundamentally undermine and weaken the Community Reinvestment Act."[2] Furthermore, the Federal Reserve does not support the proposal and despite a request being made by stakeholders and a number of Members of Congress that any proposal should not be rushed and allow for, at a minimum, at least 120 days for the public to review and comment on the proposal, this proposal provides only 60 days for public comment.

1. Vice Chair Quarles and Chairman McWilliams, if regulators finalized different regulations to implement the Community Reinvestment Act, could this lead to regulatory arbitrage in the marketplace? Leading up to the last financial crisis, when the Office of Thrift Supervision lowered standards for thrifts compared to other banks, was that kind of regulatory arbitrage helpful or did it lead to a race to the bottom? Should consistent application of the CRA be one of the highest priorities regarding any changes to its implementing regulations?

[1] https://www.occ.treas.gov/news-issuances/news-releases/2019/nr-ia-2019-147.html
[2] https://www.fdic.gov/news/news/speeches/spdec1219d.pdf

While the Federal Reserve Board (Board) did not join the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) in their Notice of Proposed Rulemaking (NPR) revising elements of Community Reinvestment Act (CRA) regulation, the Board has shared detailed analysis and proposals on CRA reform with our counterparts at the OCC and FDIC in the preparation of the NPR, and the NPR reflects much input from the Board. We are reviewing the comments that were submitted to the FDIC and OCC on the NPR, and we expect to learn much—including much related to the aspects of the NPR that reflect our own input—from the review. As a result, it would be premature to identify any specific areas of disagreement—rather, we are all in the process of working to determine the best path forward. We continue to view a common approach as the best outcome, but we have not yet determined the best next steps to achieve that outcome.

3. Vice Chair Quarles, what concerns does the Federal Reserve have with the NPR put forward by the OCC and FDIC? Is the Federal Reserve prepared to issue its own CRA proposal?

If so, will you provide 120 days for the public to comment on your proposal, and how soon do you plan to issue your own proposal? What would be the key differences compared to the approach the OCC has developed?

Throughout our discussions with our interagency colleagues, we have shared detailed analysis and proposals in an effort to forge a common approach on CRA reform. Our hope is that the three agencies will ultimately develop a shared set of reforms that reflect local credit needs, minimize burden, and calibrate evaluations to local conditions, bank size and business model. We look forward to gaining valuable insights from a variety of stakeholders through a careful review of the public comments received in response to the agencies' proposal.

The OCC's initial Advance Notice of Proposed Rulemaking (ANPR) regarding modernizing CRA regulations issued in August 2018 asked whether CRA credit "...[should] be limited to loans to LMI borrowers and loans in LMI or other identified areas...."[3] The architects of CRA sought to combat redlining. While tax credits and other federal programs might encourage investments in infrastructure – roads, bridges and hospitals – and projects that benefit a community more broadly, CRA has historically and should remain targeted on access to credit and financial services for LMI borrowers and communities traditionally underserved by the nation's financial system.

4. Vice Chair Quarles and Chairman McWilliams, do you agree that CRA regulations should remain narrowly targeted on providing banks credit for lending and investing activities to LMI individuals and LMI areas? Should roads and bridges and other general community-building activities, as a general matter receive more CRA credit than they get today? How does infrastructure expenditures combat redlining and promote access to credit?

[3] https://www.occ.gov/news-issuances/news-releases/2018/nr-occ-2018-87.html

First, I think it is important to note that both bankers and representatives of community organizations provided comments in the roundtable meetings that the Federal Reserve conducted in 2018 and 2019[2] and in response to the OCC Advance Notice of Proposed Rulemaking about the uncertainty regarding what community development (CD) activities count for CRA consideration. My sense is that all of the agencies have been looking for ways to address areas of uncertainty in some cases by clarifying definitions. In the stakeholder feedback referenced to above, some industry stakeholders indicated support for some broadening of eligible community development activities while consumer/community organizations generally had reservations on expansion of the definition beyond the current low- and moderate-income (LMI) focus. Further, stakeholders have offered perspectives on ways to provide clarity, with some requesting a process for the regulators to provide advance approval of eligible CD activities or to create standards and limit documentation required for activities with qualified nonprofit organizations.

We appreciate the interest in having some type of pre-approval process so that banks can get advance clarity on whether CD loans would be eligible. There also is an opportunity to clarify CD definitions. For example, one issue that could benefit from clarity is defining when naturally occurring affordable housing is eligible for CRA purposes so that banks and community groups would both have a better understanding of when this important affordable housing would get

[2] See https://www.federalreserve.gov/publications/files/stakeholder-feedback-on-modernizing-the-community-reinvestment-act-201906.pdf.

consideration while reflecting the intent of the law to meet the credit needs of LMI communities.

The OCC's approach could reduce most or all of a bank's CRA evaluation to a simple mathematical formula and could contribute to, not mitigate, CRA grade inflation. Already 98% of banks pass their CRA exams – a pass rate that suggests higher levels of lending, investment and financial services in low-and moderate-income (LMI) and underserved communities than actually exists, especially since more than 60 metro areas across the country continue to witness redlining.[4] Reliance on a topline dollar volume metric approach could diminish the local analysis bank examiners undertake, including the geographic distribution of bank lending across various neighborhoods, borrower profiles and whether the bank has first met the mortgage, small business, affordable housing and other credit needs of their local community before receiving CRA credit for what could be more profitable activities around the country.

5. Vice Chair Quarles, do you agree that focusing on a topline dollar volume metric could diminish several necessary aspects of the CRA's purpose, for example, to determine how a bank's lending and investing activities are distributed throughout their community?

[4] https://www.revealnews.org/article/for-people-of-color-banks-are-shutting-the-door-to-homeownership/

I believe there is a common goal, which is to strengthen the CRA regulations to help banks better meet the credit needs of the local LMI communities they serve and more closely align with changes in the ways financial products and services are delivered. Our hope is that the three agencies will ultimately develop a shared set of reforms which achieves this objective.

The OCC's ANPR suggests a redefinition of "community" under CRA so that banks can get CRA credit "in the aggregate, at the bank level, in addition to activities in its traditional assessment areas or local geographies." The law explicitly requires that banks demonstrate that they "...serve the convenience and needs of the communities in which they are chartered to do business." The OCC suggests grading banks and dispensing CRA credit for far-off activities, however worthy they may be on their face, without first requiring that the bank meet the needs of the local communities where it takes deposits and without any examination of whether those far-off loans and investments serve the convenience and needs of the communities where they are being made.

6. Vice Chair Quarles, do you agree that banks should first meet the needs of their local communities where they have bank branches and are accepting deposits, before getting CRA credit in other areas? And, do you agree that examiners should determine even outside their local areas if the lending and investing are meeting the local credit needs, and not providing CRA credit to banks that cherry pick the most profitable activities they can find around the country?

We have heard from both banks and community groups that the CRA regulations should better reflect the evolution of the banking industry, including the use of digital networks to deliver banking products and services. Currently, a bank with a large lending and deposit presence in a

geography but no branches has no CRA obligation in that area. At the same time, both industry and community groups commented on the importance of branches as a venue for banks to engage with their communities. Branches are the places that provide the personal face-to-face assistance valued by many consumers and business customers. Moreover, branches provide a local presence for lenders to get to know the borrowers and the communities in which they live, lend, and invest.

We are focused on ensuring that any CRA reforms adopted by the Board help better meet the needs local LMI communities and more closely align evaluations with changes in the way financial products and services are delivered.

FDIC Board Member Gruenberg outlined several concerns with the proposed evaluation metric in the OCC and FDIC's NPR, including that, "First, under this single metric approach, a bank must calculate the value of its CRA qualifying activities, at the bank and assessment area level, based on the dollar value of qualifying activities originated, made, and purchased by the bank. The problem with this approach is that adding up the dollar value of qualifying activities -- lending, community development investments, and community development services -- into a single metric undermines the evaluation of the bank's performance in each of these areas. It is a 'count the widgets' approach that does not take into account the quality and character of the bank's activities and its responsiveness to local needs."[5]

7. Vice Chair Quarles, do you share Mr. Gruenberg's concerns? Do you agree that focusing on a topline dollar volume metric would diminish several necessary aspects of the CRA's purpose, for example, allowing banks to overlook or redline underserved communities with impunity?

[5] https://www.fdic.gov/news/news/speeches/spdec1219d.pdf

While we are still in the process of evaluating public comment received in the NPR, it would be premature for me to comment on the specifics of the other agencies' proposal. My view is that the agencies share common reform goals. We all want to bring greater clarity to what counts and how it counts for CRA and to more closely align CRA with the way banks deliver financial products and services today. My hope is that we can ultimately have a common set of interagency CRA standards that benefit from the best ideas from each of the agencies. We are thoroughly reviewing the comments that have been received and hope to gain valuable insights that will help inform how best to achieve meaningful reform.

FDIC Board Member Gruenberg raised another concern with the OCC and FDIC's NPR to modernize CRA, specifically that, "[T]his proposal would allow a bank to achieve a less than satisfactory rating in nearly half of its assessment areas and still receive a satisfactory or even outstanding rating. Banks would have the flexibility to focus their stronger community reinvestment-qualifying efforts on as few as half of their assessment areas while minimizing their efforts elsewhere."

9. Vice Chair Quarles, does the Federal Reserve share these concerns outlined by FDIC Board Member Gruenberg with respect to the NPR?

Please see my response to question 7.

Since 2016, banks have negotiated $86 billion in community benefit agreements (CBAs) with local stakeholders because of CRA and its community input provisions during mergers/acquisitions, resulting in banks providing more mortgages, small business and community development loans and investments in LMI communities around the country. OCC Comptroller Otting has admitted that part of his CRA reform plan is to make it harder for community groups to "hold [bankers] hostage" when bank merger and expansion deals are up for regulatory approval.

10. Vice Chair Quarles and Chairman McWilliams, do you agree that a bank's CRA rating should remain a key consideration in whether a bank is allowed to merge? Under what circumstances, do you believe it is important to have a public hearing in the case of a bank merger?

The CRA statute requires the Board to take into account the CRA performance record of an institution in mergers and acquisitions applications, and the Board will continue to implement this requirement, consistent with the law.

We make a case-by-case judgement on whether to have a public hearing, considering a number of factors such as the potential impact of the merger on the community, the track record of the entities being considered for the merger, and the views of affected stakeholders.

Volcker Rule

The Volcker Rule, which bans proprietary trading and ownership of private funds by publicly insured banks, is one of the most important rules that your agencies are charged with enforcing. Yet there has been a very disturbing lack of public disclosure concerning how exactly your supervisors are enforcing this rule, or indeed whether they are enforcing it stringently at all.

20. Vice Chair Quarles: To my knowledge, there has been only one case where a bank was actually penalized for violation of the Volcker Rule. Deutsche Bank publicly admitted that it had been unable to properly comply with the rule and paid a $20 million fine. In the six years since the Volcker Rule regulation was finalized at the end of 2013, have there been any other cases where a bank was found to have violated the rule and penalized for it?

The Board monitors the banking entities under its jurisdiction for compliance with the Volcker Rule. Consistent with past and current practice, the Board supervises and enforces the restrictions of the Volcker Rule similar to the manner in which other laws and regulations are enforced. The Board uses a variety of tools including reporting and examinations. Most issues

are resolved through the normal supervisory process. All final enforcement orders as a result of violations of applicable laws, including the Volcker Rule, are made public by the Board.[3]

21. Vice Chair Quarles: Despite the ban on proprietary trading under the Volcker Rule, the major trading banks at the center of Wall Street continue to earn about one quarter of their revenues from trading activities, which is about the same amount they earned in the years prior to when the Volcker Rule regulation was finalized in 2013. In light of this, how can the public understand what the impact of the Volcker Rule has been on actual trading activities at banks?

Under the Volcker Rule, proprietary trading is generally prohibited, but there are a number of trading activities in which a banking entity may still engage, such as market-making, underwriting, and risk-mitigating hedging. In addition, the Volcker Rule does not apply to trading in certain types of financial instruments, such as U.S. government securities.

The largest trading banks report quantitative information about their trading activities subject to the Volcker Rule. However, the metrics are not a dispositive tool for identifying permissible or impermissible activity. Rather, they provide indicia for supervisors to look further into specific activities or transactions. Overall, based on staff analysis, the metrics reported to the Board by the largest trading banks help staff determine whether these firms are generally engaged in the types of trading activities that are permissible under the Volcker Rule.

22. Vice Chair Quarles: I understand that the Federal Reserve may collect a large number of daily trading metrics from banks subject to the Volcker Rule. Yet it has never been made clear exactly how these metrics are used to determine whether a bank is complying with the rule, nor have any of the metrics been released to the public. Is that true? How exactly is the Federal Reserve determining if a bank's trading activity is in compliance with the Volcker Rule, and how can the public determine if you are doing so?

The metrics reported by the banks with the most significant trading operations let supervisors evaluate trading activities for potentially impermissible proprietary trading activity. As noted above, the metrics are not a dispositive tool for identifying permissible or impermissible activity. Rather, they provide indicia for supervisors to look further into specific activities or transactions. Board staff analyze data reported to the Board to evaluate whether a bank's trading activities are consistent with what one would expect to see if the firm were not engaged in impermissible proprietary trading. For example, one metric analyzed by Board staff is a trading desks' Sharpe ratios, which standardize trading desks' profit and loss based on the risk taken by the desk. This metric allows Board staff to review how a trading desk is making money, for example from new positions (e.g., through fee income from permissible market-making activities), or from changes in the value of existing positions (which, if significant, may warrant additional scrutiny). The metrics represent sensitive, confidential business and supervisory information and, as a result, the Board does not disclose such information on a firm-specific basis.

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[3] See https://www.federalreserve.gov/supervisionreg/legal-developments.htm.

Weakening Bank Supervision

According to data from your supervisory reports, in 2007 as the financial crisis was beginning, Federal Reserve supervisors rated 97% of large bank holding companies as "satisfactory" or above.[7] Today, you are rating only about 60% of large bank holding companies as "satisfactory" or above.[8] If that is the case, it would not seem to make sense to ease up on supervision. You've removed qualitative supervisory ratings from bank CCAR stress tests. In a recent speech you said that making sure supervisors are "acting fairly" is an equally important priority as addressing financial stability risks.[9]

[7] https://www.federalreserve.gov/publications/2018-11-supervision-and-regulation-report-accessible-page.htm#xfigure13outstandingsupervisoryfindi-e4ac896e
[8] https://www.federalreserve.gov/publications/files/201911-supervision-and-regulation-report.pdf
[9] https://www.federalreserve.gov/newsevents/speech/quarles20190927a.htm

24. Vice-Chair Quarles: Would you agree that maintaining the discretionary power of front-line bank supervisors to act when they see a risk to safety and soundness or to consumers is critical for protecting the public?

Our supervisors maintain a wide range of supervisory tools to correct safety and soundness deficiencies or protect consumers, and it is important that the Federal Reserve has the ability to employ these tools expeditiously when warranted. Supervision is most effective when expectations are clear and supervision promotes an approach to risk management that encourages good behavior and sound decisions by banks.

Diversity and Inclusion

Based on feedback from the nation's largest banks to an inquiry led by myself and Rep. Beatty, the Committee found that while the U.S. population is over 50% women and 40% minorities: the boards of directors of the largest banks are comprised of only 29% women and 17% minorities; there is no U.S. global significantly important bank (G-SIB) with a female or minority CEO at the helm; chief diversity officers do not report directly to the CEO at any G-SIB; only 4 out of 8 megabanks spent more than $1 billion on diverse suppliers in 2018; and, while $1.4 billion is the average spent by U.S. G-SIBs on supplier diversity, less than 1% of megabank spending is devoted to diverse asset managers and suppliers, and only 4% of externally managed assets go to diverse-owned firms.[11]

29. Chairman McWilliams, Vice Chairman Quarles, and Chairman Hood: What new steps can regulators and Congress take to promote diversity and inclusion in banking?

[11] FSC Press Release, "Committee Finds More Work is Needed to Improve Diversity at Megabanks," Aug. 13, 2019

The Board continues to receive, track and assesses the regulated entities' Diversity and Inclusion Self-Assessments (self-assessments). We continue to emphasize the importance of institutions'

participation in self-assessments and how impactful policies and practices can create and sustain diversity and inclusion in the financial industry. To that end, the Board's Office of Minority and Woman Inclusion (OMWI) collaborated with the OMWIs of the OCC and FDIC and the American Bankers Association to host a webinar regarding self-assessments. The webinar was held in November 2019 with approximately 100 companies registered. On October 24, 2019, the financial regulators also hosted the second "Diversity and Inclusion Summit" held in Chicago, Illinois at the Federal Reserve Bank of Chicago. Approximately 125 companies attended representing entities regulated by the Federal Reserve, OCC, FDIC and National Credit Union Administration. The primary purpose of the program was to continue open communications and sharing of diversity and inclusion policies and practices within the financial industry and ways to collaborate with the industry in addressing a lack of diversity, recruitment, outreach and organizational accountability. Also, the regulators provided information on the types of reports companies could include as part of their self-assessments describing initiatives and actions taken relating to diversity, equity and inclusion practices such as newsletters, annual reports, and sponsored programs.

Faster Payments and Fintech

In August, the Federal Reserve Board announced plans to develop a new payment and settlement service by 2023 or 2024, called the FedNow Service. An interbank 24x7x365 real-time gross settlement service that would process individual payments within seconds. A real time payments system can be the difference between making rent and putting food on the table or not doing so for many underserved populations in our districts. Instant payments also can help numerous families across the country avoid paying hefty fees related to late payments due to their funds being withheld for several days. This initiative is broadly supported by community banks, credit unions, small businesses, fintech companies and consumer groups.

34. Vice Chair Quarles: How soon can the Fed get the FedNow Service up and running? Despite the broad support from a wide range of stakeholders, why did you dissent from the Fed's decision to set up its own real time payments service?

The development of the FedNow[SM] Service will be a key focus area for the Federal Reserve for the foreseeable future. The Federal Reserve currently projects that the FedNow Service will be available sometime in 2023 or 2024, although an official launch date has not yet been established. When a specific launch date and implementation timeline have been finalized, that information will be provided publicly. The Federal Reserve recognizes that time-to-market is an important consideration for many industry participants and is committed to establishing the FedNow Service as soon as practicably possible. Ongoing work to finalize business requirements, determine engagement with external vendors, and assess the industry's views on features and design will help inform the implementation timeline for the FedNow Service.

I dissented from the Board's decision to set up its own real-time payments service because I believe that

(1) the private sector is quite capable of providing this service (indeed, one private sector

solution was already in existence); these private sector solutions do not appear to need supplementing to reach network ubiquity;

(2) the Fed's entry into this area will deter other private sector actors from entry, and thus crowd out further U.S. innovation and price competition in this area;

(3) the Fed's development of its own system will materially delay widespread availability of real-time payments in the U.S. because of the length of time it will take the Fed to implement a solution, and many participants will wait until the Fed service is available before adopting any real-time system;

(4) the rapid development of technology in this area creates a real risk that the Fed system will be out-of-date before it is completed, limiting smaller banks and their customers to a less satisfactory service (or, alternatively, limiting demand for the FedNow Service, thus further complicating the Fed's compliance with the legal requirement that we recover our investment costs);

(5) the technological obstacles to completion of this effort are large, creating significant execution risk as well as ongoing system management challenges; and

(6) the Fed's entry is extremely likely to result in higher costs to consumers, businesses, and smaller banks.

Reasonable people can of course differ about these views, and all of my colleagues on the Board concluded that the development of the FedNow Service is appropriate at this time. The reasoning behind their conclusion was laid out in detail at the time the Board voted to proceed with FedNow, and none of that reasoning is baseless; I simply disagreed. With that decision taken, I believe the Fed should devote the resources necessary to move this difficult project forward as quickly and soundly as possible.

Use of Alternative Data in Credit Underwriting

Financial regulators recently issued a joint statement on the use of alternative data in credit underwriting by banks, credit unions, and non-bank financial firms.[12]

39. All Witnesses: in the use of alternative data, how do policymakers ensure consumer's permission to access this data is not abused? For example, how do we ensure that the data is not used for a purpose the consumer never intended such as targeted marketing after providing an initial, general consent to the company?

[12] https://www.consumerfinance.gov/about-us/newsroom/federal-regulators-issue-joint-statement-use-alternative-data-credit-underwriting/

The use of consumer-permissioned and other alternative data may have benefits for consumers, including increasing access to credit products and improving credit underwriting. While consumer permissioning can enhance transparency and consumers' control over their data, the

use of such data raises important questions, including whether consumers understand what data are being shared; how their data are being used, and by whom; and how to address the potential for bias, data mishandling, or privacy breaches.

The Federal Reserve has a responsibility to ensure that institutions we supervise comply with applicable statutes and regulations that apply to the use and sharing of consumer data, including consumer protection laws. For example, the Gramm-Leach-Bliley Act, the Fair Credit Reporting Act, and their implementing regulations include certain requirements and restrictions applicable to consumer data used for marketing purposes. In addition, laws that prohibit financial institutions from engaging in unlawful discrimination and unfair or deceptive acts or practices might apply, depending on the circumstances. Further, the CFPB has express rulemaking authority under section 1033 of the Dodd-Frank Act to address consumers' access to their financial data.

Within this framework, the Federal Reserve has sought to promote socially beneficial and financially sound innovations, while ensuring the risks that those innovations present are appropriately identified and managed. Accordingly, the Federal Reserve and other regulators coordinate on consumer data access issues in a number of fora, including the FFIEC Task Force on Supervision and the FFIEC Task Force on Consumer Compliance.

As with prior developments in the evolution of credit underwriting, including the advent of credit scoring, the use of alternative data and analytical methods raises questions regarding how to effectively leverage new technological developments in ways that are consistent with applicable consumer protection laws.

40. All Witnesses: the interagency statement states that, "Based on that analysis, data that present greater consumer protection risks warrant more robust compliance management." What kind of alternative data, or uses of that data, are your agencies referring to that has "greater consumer protection risks"?

Alternative data can encompass a wide range of data, including data that are directly related to consumers' finances and how consumers manage their financial commitments and other data without such a relationship.

Consumer protection risks can be heightened when alternative data do not have a relationship to creditworthiness, or are derived from protected characteristics under fair lending laws. A 2016 Federal Trade Commission (FTC) report, "Big Data: A Tool for Inclusion or Exclusion?" as well as a 2017 article entitled "Keeping Fintech Fair: Thinking about Fair Lending and UDAP Risks" in the Federal Reserve System publication *Consumer Compliance Outlook* provide more insights into the risks of using consumer data.[4]

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[4] FTC, Big Data: A Tool for Inclusion or Exclusion? (2016); https://www.ftc.gov/reports/big-data-tool-inclusion-or-exclusion-understanding-issues-ftc-report. Federal Reserve Board; Evans, Carol A. Evans, "Keeping Fintech Fair: Thinking About Fair Lending and UDAP Risks," *Consumer Compliance Outlook* (Board of Governors of the Federal Reserve System, December 2017); https://www.consumercomplianceoutlook.org/2017/second-issue/keeping-fintech-fair-thinking-about-fair-lending-and-udap-risks/.

41. All Witnesses: the statement does not discuss racial or gender disparities that may exist in alternative data, especially when combined with artificial intelligence and machine learning. What steps will your agencies take to prevent the use of opaque algorithms or AI that may result in discriminatory outcomes in credit underwriting and other uses of alternative data?

The Federal Reserve recognizes the potential fair lending risks that may arise from the combination of alternative data and new analytical techniques, such as artificial intelligence and machine learning. Federal Reserve staff have been actively engaging in outreach to better understand these issues, and have met with consumer advocates with expertise in research and analyzing consumer protection issues related to the use of artificial intelligence and machine learning as applied in the areas of financial services, employment and housing. The Federal Reserve also has highlighted these potential risks through the recently issued Consumer Compliance Supervision Bulletin, its *Consumer Compliance Outlook* publication, public webinars and examiner training.[5] Additionally, Board members have raised these concerns in speeches.

The Federal Reserve is committed to promoting fair lending and identifying illegal discrimination in the institutions we supervise. We strive to learn about new fair lending risks and to educate our examiners so they may recognize them. The Federal Reserve evaluates fair lending risk at every consumer compliance exam, based on the risk factors set forth in the Interagency Fair Lending Examination Procedures, adopted by the FFIEC. The Federal Reserve's review of fair lending risk would extend to the appropriate use of algorithms in underwriting, pricing or marketing. Our supervisory procedures are designed to elicit information from banks on fintech practices that may create consumer protection risks. If we have concerns about potential lending discrimination, we obtain additional data and information.

Mobilizing Finance Against Slavery and Human Trafficking

One area of interest for this Committee is how the financial sector can better combat the crime of human trafficking. A recent report— "A Blueprint for Mobilizing Finance Against Slavery and Trafficking," prepared by the Financial Sector Commission on Modern Slavery and Human Trafficking— identified the need to strengthen AML tools in relation to addressing modern slavery and human trafficking. In particular, the report highlighted the importance of developing transaction analysis tools to better "identify proceeds of modern slavery and human trafficking in all areas of financial sector activity", especially as it relates to more difficult cases which often involve labor trafficking, debt bondage and forms of modern slavery and human trafficking occurring in the developing world. Furthermore, the report stated, in the case of financing involving sectors with known higher risks of forced labor, anti-slavery and anti-trafficking measures could be developed as part of the loan conditions.

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[5] See, e.g., Consumer Compliance Supervision Bulletin (December 2019); https://www.federalreserve.gov/publications/files/201912-consumer-compliance-supervision-bulletin.pdf; Carol A. Evans, "Keeping Fintech Fair: Thinking About Fair Lending and UDAP Risks," Consumer Compliance Outlook (Board of Governors of the Federal Reserve System, December 2017); https://www.consumercomplianceoutlook.org/2017/second-issue/keeping-fintech-fair-thinking-about-fair-lending-and-udap-risks/.

42. All Witnesses: What is your agency doing to encourage the development of these analytical tools and investments in data innovations, with a specific emphasis on identifying activity related to human trafficking?

The Federal Reserve supports the use of innovative technology by financial institutions in BSA/AML compliance programs. To that end, on December 3, 2018, the interagency Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing (statement) was issued to encourage banks to take innovative approaches to meet BSA/AML compliance obligations.[6] The statement notes, for example, that when banks test or implement artificial intelligence-based transaction monitoring systems and identify suspicious activity that would not otherwise have been identified under existing processes, the Federal Reserve will not automatically assume that the banks' existing processes are deficient.

Accordingly, the Federal Reserve is broadly supportive of the efforts that some financial institutions have made to ensure that they are not in any way facilitating transactions related to slavery and human trafficking. While the Federal Reserve encourages innovation and the development of analytical tools to support these efforts through the banks' AML programs, banks also are afforded the flexibility to develop tools that focus on specific areas of risk, such as slavery and human trafficking.

The Federal Reserve expects banks to take reasonable and prudent steps to combat money laundering and terrorist financing and to minimize their vulnerability to the risk associated with such activities, including slavery and human trafficking. Federal Reserve examiners do not look for specific crimes in conducting examinations, but seek to ensure a bank has an appropriate infrastructure to guard against money laundering and terrorist financing.[7] Banks then provide information produced by that infrastructure to various law enforcement agencies that use it to investigate or prosecute crime.

Within this system, FinCEN and the federal banking agencies recognize that, as a practical matter, it is not possible for a bank to detect and report all potentially illicit transactions that flow through the bank. Examiners thus focus on evaluating a bank's policies, procedures, and processes to identify, evaluate, and report suspicious activity. However, as part of the examination process, examiners do review individual Suspicious Activity Report filing decisions to determine the effectiveness of the bank's suspicious activity identification, evaluation, and reporting process.

43. All Witnesses: What is your agency doing to support better identification of risks relating to human trafficking within the financial sector and the steps needed to mitigate these risks?

Please see the response to question 42.

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[6] See SR 18-10, at https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20181203a1.pdf.
[7] See https://www.fincen.gov/resources/advisories/fincen-advisory-fin-2014-a008.

Appraisals

Banking regulators have recently determined that raising appraisal thresholds would not be in the public's interest. Specifically, in 2017, after a multiyear review that included several public hearings and open comment requests, banking regulators submitted a "Joint Report to Congress on the Economic Growth and Regulatory Paperwork Reduction." [13]

The Joint Report stated:
"The agencies also considered safety and soundness and consumer protection concerns that could result from a threshold increase for residential transactions. The last financial crisis showed that, like other asset classes, imprudent residential mortgage lending can pose significant risks to financial institutions. In addition, the agencies recognize that appraisals can provide protection to consumers by helping to assure the residential purchaser that the value of the property supports the mortgage amount assumed. Overall, the agencies believe that the interests of consumers are better served when appraisal regulations are coordinated among government agencies."

Yet, in September, the federal banking agencies' issued a final rule to increase the residential appraisal threshold from $250,000 to $400,000, which was approved with the CFPB's concurrence. Under the rule, 72%, or nearly 3 out of 4, home mortgage transactions in the U.S. are now exempt from appraisal requirements, putting taxpayers at serious risk for any future calamity related to the housing market. Furthermore, over 500 comments were received on the proposed rule with a majority in strong opposition to increasing threshold amounts, including 38 consumer and public interest organizations. Many of these organizations requested a public hearing to discuss this issue, but their suggestion was dismissed.

In addition, the NCUA recently issued a similar proposed rule which would align its appraisal requirements with the federal banking agencies as well as approved a final rule which increases the non-residential appraisal threshold level to $1 million, a move that contradicts the final rule that increased the commercial real estate appraisal threshold level to $500,000 for federally regulated banks. I understand this is the first time in history that the NCUA has stepped ahead of the banking agencies on appraisal requirements.

[13] https://www.ffiec.gov/pdf/2017_FFIEC_EGRPRA_Joint Report_to_Congress.pdf.

As we attempt to reconcile apparent inconsistencies between the Joint Report to Congress and your recent regulatory actions to increase appraisal thresholds, please respond to the following:

45. All Witnesses: Did any of your agencies take any supervisory or enforcement actions during or after the financial crisis that related to appraisal and underwriting deficiencies? If yes, does this not suggest there were safety and soundness concerns relating to appraisals in the lead up to the financial crisis a decade ago?

The Federal Reserve examines supervised institutions for compliance with its appraisal regulations as part of an overall assessment of real estate lending and underwriting practices. During the financial crisis, the Federal Reserve issued Matters Requiring Attention and Matters Requiring Immediate Attention to institutions related to real estate lending, credit administration, and appraisals. Enforcement actions related to loan documentation, underwriting and lending, and credit administration were issued during the crisis and included actions related to appraisals and appraisal program administration.

Prior to the 2007 financial crisis, the Federal Reserve and the other agencies did observe weaknesses in regulated institutions' underwriting standards in their residential mortgage lending activity, particularly in nontraditional mortgage products. As a result, the Federal Reserve and the prudential federal regulators issued supervisory guidance to remind institutions that their underwriting standards should comply with the agencies' real estate lending standards and appraisal regulations.[8] The Federal Reserve also issued a statement on sub-prime mortgage lending.[9] In 2008, the Federal Reserve issued a rule, applying to all residential mortgage transactions secured by a consumer's principal dwelling, that prohibited creditors, mortgage brokers and their affiliates from directly or indirectly coercing, influencing, or otherwise encouraging an appraiser to misstate or misrepresent the value of the dwelling. This rule contained several examples of prohibited conduct.[10] After the crisis, several regulations were issued to address problems specific to residential mortgage lending such as the Valuation Independence Rule and the Dodd-Frank Act ability-to-repay requirements and qualified mortgage (QM) standards.[11]

46. Vice Chair Quarles and Chairman McWilliams: Appraisal problems was a contributing factor to the last financial crisis identified by the FDIC's Inspector General report entitled, "Comprehensive Study on the Impact of the Failure of Insured Depository Institutions." In fact, the word "appraisal" is used 345 times in the report. Did the banking agencies review this report or related Material Loss Review reports examining bank failures during the financial crisis in determining there are no safety and soundness concerns relating to appraisals? If not, why not?

Federal Reserve staff reviewed reports prepared by the Board's Office of the Inspector General including the Summary Analysis of Failed Bank Reviews, dated September 2011, and various Material Loss Review Reports prepared on specific bank failures. The summary report covered the period between June 29, 2009, and June 30, 2011, and included an assessment of 35 failures of state member banks. The common elements noted as contributing to bank failures were: (1) aggressive growth and poor strategic decision-making; (2) asset concentrations in construction and land development loans; (3) reliance on specific funding sources; (4) ineffective controls and poor risk management; and (5) compensation incentives that encouraged inappropriate risk taking. Appraisals were not identified as being a primary contributor to bank failures during this period, although in some cases, a bank's poor appraisal practices were identified as risk

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[8] See SR letter 16-15/ CA letter 16-12, "Interagency Guidance on Nontraditional Mortgage Product Risks," at https://www.federalreserve.gov/boarddocs/srletters/2006/SR0615.htm.

[9] See SR 07-12/ CA 07-3, at https://www.federalreserve.gov/boarddocs/srletters/2007/SR0712.htm.

[10] See, e.g., 73 FR 44522, 44604 (Jul. 30, 2008).

[11] See 76 FR 27390 (May 11, 2011).

management issues. The Board, OCC, FDIC, NCUA and Office of Thrift Supervision took steps to strengthen appraisal guidance by revising the Interagency Appraisal and Evaluation Guidelines in 2010.

47. Vice Chair Quarles and Chairman McWilliams: Why were the dates of January 2017-December 2018 chosen to review Reports of Examination, given 2018 was the first year since 2006 without a bank failure?

The agencies selected a two-year period that was intended to capture their supervision of appraisal practices that reflected the enhanced expectations imposed by post-crisis regulatory and policy changes, such as the 2010 Valuation Independence Rule, the 2010 Interagency Appraisal and Evaluation Guidelines, and the 2013 QM Rule. The presence or absence of bank failures was not a consideration in the selection of the period.

48. All Witnesses: Please provide aggregate year-by-year data on examiner findings regarding appraisals and evaluations since enactment of Title XI of FIRREA.

At the Federal Reserve, appraisal and valuation practices are included as part of real estate lending and general underwriting examinations. Examiner findings for these exams were reported on a consolidated basis until 2015, after which data on appraisals and evaluations was gathered separately.

49. All Witnesses: With respect to oversight of individuals conducting evaluations, what recourse does a consumer have who may have issues arising from an evaluation product, which currently has no regulatory oversight?

The consumer has recourse whether an appraiser or bank employee prepared the evaluation. For evaluations prepared by appraisers, consumers can contact the State Appraiser Regulatory Agency responsible for licensing the appraiser. For evaluations prepared by bank employees or non-appraisers, consumers can contact the primary federal regulator. The Federal Reserve's Office of the Ombudsman will assist in resolving issues related to evaluations prepared by bank employees.

In addition, certain federal consumer financial protection laws provide protections to consumers who may have problems or disagree with an evaluation that is prepared by a bank. Consumers may file a complaint with their primary federal regulator or the CFPB.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Barr:

In your testimony you stated that the Federal Reserve Board is currently considering how best to implement the remainder of the international Basel III agreement, or Basel endgame, as a package -- and that the FRB is aware that the impact of implementing Basel III revisions into the U.S. framework may result in "significantly raising the aggregate level of capital in the industry." You also stated that the FRB "regularly look[s] at the calibration of the GSIB surcharge and we are considering it in the context of the overall body of regulation."

Additionally, Chairman McWilliams noted that the Basel Committee conducted a quantitative impact study (QIS) in 2009 at one of the worst times for banks' balance sheets that included only 14 U.S. banks. Chairman McWilliams suggested that she would support an analysis focused on a more specific impact in the United States.

I agree with your and Chairman McWilliams' statements that a holistic and comprehensive review of the capital framework in the U.S. is necessary to ensure that capital levels are calibrated appropriately to maintain a level playing field with our international counterparts, especially given the many post-crisis reforms that we have discussed.

When does the Federal Reserve Board plan to complete the comprehensive review and publish the results so that they may be made available to lawmakers and to the public?

If the nature of the review is ongoing and long-term, when can we expect an initial set of findings to be released based on provisions that are currently being implemented?

As I mentioned in my testimony, the Federal Reserve Board (Board) is paying close attention to the coherence of our capital regime. We are reviewing public comments on a proposed stress capital buffer framework, which would simplify our regime by integrating our stress-test and point-in-time capital requirements while maintaining the current strong levels of loss absorbency. We are also actively considering how the final Basel III standards could be implemented to maintain the aggregate level of loss absorbency across the industry, avoid additional burden at smaller banking organizations, and support our principles of transparency and due process.

While the framework developed by the Basel Committee suggests that participating jurisdictions could have a number of years to finish implementation of the remaining elements of the Basel III standards, I believe that we should view these standards as a package in evaluating their effects—implementing none until all are calibrated—and that we should therefore move more quickly to develop a proposal for implementing these remaining standards. This would also facilitate an evaluation of the likely effects on bank capital levels of completing implementation of Basel III, which would in turn enable an evaluation of whether recalibration of any existing standards would be appropriate to reflect Basel III completion (as you know, some of our existing standards were calibrated above international minimums to reflect, among other factors, the fact that some elements of the comprehensive framework were not yet in effect).

While we do not have a fixed deadline for completing this process—and while some portions of it will involve interagency coordination, which further complicates the projection of a timeline—development of a package proposal will be a high priority of mine over the coming year.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Beatty:

1. As you know the Federal Reserve is currently developing capital requirements for insurance companies that own depository institutions, otherwise known as insurance savings and loan holding companies, due to passage of the Insurance Capital Standards Clarification Act in 2014. This legislation clarified that the Federal Reserve should tailor capital standards for insurance companies. I am concerned and perplexed why the proposed rule would impose a separate Section 171 banking capital calculation on these insurance companies. This seems to me to stand in contradiction to congressional intent. Imposing a Basel banking capital calculation on insurance companies is the outcome that Congress was trying to avoid when we passed that law back in 2014.

Will you commit to addressing my concerns in the final rule and ensuring that your rule respects Congressional intent to avoid imposing banking capital requirements on insurance companies?

Section 171 of the Dodd-Frank Act requires the Federal Reserve Board (Board) to establish minimum risk-based capital requirements for depository institution holding companies on a consolidated basis. The Insurance Capital Standards Clarification Act of 2014 (Clarification Act) amended section 171 to permit, but not require, the Board to exclude state-regulated insurers from this consolidated minimum risk-based capital requirement. The Clarification Act does not provide a blanket exemption for an entire holding company structure. In particular, it explicitly does not exempt a depository institution holding company from calculating its capital requirements for non-insurance entities in the corporate chain.

In September 2019, the Board issued a proposal on risk-based capital requirements for certain depository institution holding companies significantly engaged in insurance activities (proposal). The proposal would establish an enterprise-wide risk-based capital framework, known as the Building Block Approach, which is intended to facilitate the assessment of overall risk-based capital adequacy for a depository institution holding company that is significantly engaged in insurance activities by measuring aggregate capital while taking into consideration state insurance capital requirements. The proposal also includes a minimum risk-based capital requirement for the non-insurance entities within the holding company structure required by section 171, as amended by the Clarification Act (section 171 calculation). The section 171 calculation would use the flexibility afforded by the Clarification Act and exclude state-regulated insurers from minimum risk-based capital requirements to the extent permitted by law.

The Board recently invited public comment on all aspects of the proposal, including the section 171 calculation. Some comments suggested that the Building Block Approach would comply with the statutory requirements without an additional calculation. Consistent with the Administrative Procedure Act, the Board will consider this and other comments before making a final rule.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Budd:

1. Mr. Quarles, in addition to FedNow, the Fed also proposed expanding the operating hours of the Fedwire Funds Service. The purpose of this proposal as I understand it is to provide greater liquidity for supporting payments – including FedNow and other real-time payment systems – around the clock.

What is the status of this proposal?

Do you plan to implement these expanded hours before FedNow goes live?

Are there any impediments with moving forward?

The Federal Reserve Board (Board) is currently analyzing an expansion of operating hours for the National Settlement Service (NSS) and the Fedwire® Funds Service, up to 24x7x365, to support a wide range of payment activities, including liquidity management for faster retail payments. As part of its analysis, the Board is engaging with industry participants in order to understand the industry's specific needs and readiness related to expanded hours. In addition, the Board intends to publish at least two *Federal Register* notices in order to seek public comment on issues related to, and potential approaches for, expanding the Fedwire Funds Service and NSS operating hours, and announce its progress and any decisions related to expanded hours.

The timeline for the Board's analysis will depend in part on the diversity and complexity of issues that the Board identifies during its review. In addition, the timeline for assessing and potentially implementing expanded hours will take into account any dependencies and impacts associated with the implementation of the FedNow℠ Service. Given the systemic importance of the Fedwire Funds Service, any decisions on expanding hours could have significant impacts on market participants. The Board is committed to carefully evaluating the potential benefits, risks, and costs of any decision to expand hours of the Fedwire Funds Service and NSS.

At the same time that the Board considers expanding operating hours for NSS and the Fedwire Funds Service broadly, the Board will continue to assess the appropriateness of incremental changes to relevant Federal Reserve financial services in response to specific industry needs. For example, the Board recently completed analysis of an expansion of operating hours for NSS and the Fedwire Funds Service in order to support enhancements to the same-day automated clearinghouse (ACH) service. In December 2019, the Board announced an expansion of operating hours for NSS and the Fedwire Funds Service that will be implemented in March 2021 in order to add a third same-day ACH processing and settlement window.[1]

[1] See https://www.federalreserve.gov/newsevents/pressreleases/other20191223a.htm.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Foster:

1. Vice Chairman Quarles, in recent months, a number of Federal Reserve officials have publicly commented on the impact of climate change impacts to the economy.

In fact, the Fed recently held its first conference on the economics of climate change in November, where San Francisco Fed Chief Daly said that severe weather cost insurers more than $50 billion in 2018 alone, and including uninsured damage nearly doubles that number.

Kevin Stiroh at the New York Fed recently noted that the US economy has experienced more than $500 billion in direct losses over the last five years due to climate and weather-related events, and that number grows by many factors if indirect losses are included.

As I believe is well-established with the Fed by now, climate change is a growing threat to our economy.

a. To date, has the Fed issued any guidance to supervised entities on how to account for these risks? What are the implications of climate change on supervisory policy?

The Federal Reserve Board's (Board) supervisory framework guides supervisors in their oversight of supervised entities with respect to their risk management practices over a wide range of risks, including those that are related to climate-related risks. Long-standing Board guidance encourages bank management to take into account all relevant risks in underwriting and review practices, while other guidance specifically addresses lending to sectors where assessments of severe climate-related risks are critical for due diligence and underwriting.

More broadly, analytic work on the relationship between climate and financial risks is in its early stages, and Federal Reserve researchers are among those working to advance it. The Board and Reserve Banks are exploring new sources of climate-related data and computational resources, engaging in research projects involving existing supervisory data collections, and participating in conferences and workshops to share our efforts with the public. We expect these efforts to improve our ability to assess the ways climate-related risks may affect the safety and soundness of financial institutions, as well as the economy and financial stability more broadly.

b. How should risk managers at financial institutions incorporate climate change risks into their capital models?

The Federal Reserve requires institutions to understand, assess, manage, and monitor, as well as to hold both capital and reserves against, a range of risks material to their operations. The most appropriate way for an institution to meet these requirements—and the most relevant information it uses to do so—may vary according to the characteristics and activities of the institution. The banking institutions we regulate are all expected to measure the risks associated with their business, including their loan exposures. Large institutions typically gather data on the

probability of default and loss on the loans they hold on their balance sheets. In many cases, climate-related risks could affect these measurements.

Depending on the circumstances an institution faces, the data that are relevant to doing so may differ—depending, for example, on whether an institution's credit exposures are secured by coastal or plain property, or are tied to business revenues in agriculture or construction. We expect institutions to use a range of risk-management data appropriate to their activities, and our supervisors consider whether such data is used in a way that promotes safety and soundness.

c. In terms of potential effects on the economy, what data sets or models does the Fed use to evaluate the potential effects of climate change on economic output and productivity?

For the Federal Reserve's near-term macroeconomic analysis, we do take into account information on the severity of weather events. When a severe weather event occurs, we closely monitor the effects on local economies, assess the implications for broader measures of economic production and employment, and adjust our economic forecasts accordingly.

For example, our staff has relied on data from the Federal Emergency Management Agency and the Department of Energy to gauge the disruptions to oil and gas extraction, petroleum refining, and petrochemical and plastic resin production in the wake of hurricanes that have affected the Gulf region. Our staff regularly uses daily measures of temperatures and snowfall from the National Oceanic and Atmospheric Association weather stations to better understand how severe weather may be affecting measured and real economic activity in specific areas.

Our understanding of what economic activities will be affected by a severe weather event depends critically on data produced by the federal statistical agencies, such as the Census Bureau's County Business Patterns data, as those data provide information on economic activity in different geographic locations. In addition, our staff uses credit and debit card transactions data for gauging how specific types of severe weather might be affecting consumer spending in areas affected by those events.

At present, we do not directly model how changes in temperatures over long periods of time affect economic activity. But to the extent that climate change affects the economic data on which our models are built—including the trends and the cyclical behavior of investment, consumption, production, and employment—then climate change will be incorporated in our macroeconomic analysis over time.

d. Governor Brainard recently said that the Fed was in discussions about participating in the Central Banks and Supervisors Network for Greening the Financial System in order to learn from peers abroad. The Network's purpose is to enhance the role of the global financial system to manage risks related to climate change. There are currently 42 Members and 8 Observers, including our peers such as the ECB, Bank of England, Bank of Japan, and Bank of Canada, and major multi-lateral institutions such as the IMF, World Bank, Bank for International Settlements, and the Basel Committee. Do

you think it would be a good idea for the US to join this Network? When do you anticipate the US being able to join?

As I noted at the hearing, I have strongly urged that the Federal Reserve participate in the Network for Greening the Financial System (NGFS). Federal Reserve staff have attended recent NGFS discussions as guests and we will continue to do so. We are also exploring how we might participate further in a way that is consistent with the full range of our responsibilities. A wide range of other international work is also underway on climate-related economic and financial risks, including at the Financial Stability Board, which I chair. We are participating actively in these efforts and have been in close communication with our counterparts in other jurisdictions to learn from their research and supervisory efforts.

2. Vice Chairman Quarles, in October, the Federal Reserve Board finalized "tailoring" rules for enhanced prudential standards and resolution planning requirements for domestic and internationally-headquartered firms. This included incorporating risk-based indicators for determining categorization of firms. However, the Board's supervisory frameworks, such as the Large Institution Supervision Coordinating Committee (LISCC), do not reflect those final categorizations. You testified that the Board is in the process of "considering refinements" to the LISCC designation process.

a. As part of your review, is the Board considering aligning the LISCC framework with categorization under the new tailored regulatory requirements?

b. When do you expect the Board to complete its LISCC review process?

The Large Institution Supervision Coordinating Committee (LISCC) is a Federal Reserve Systemwide committee with the task of overseeing the supervision of the largest, most systemically important financial institutions in the United States and chaired by the director of the Board's Division of Supervision and Regulation. The LISCC was formed after the financial crisis to bring an interdisciplinary and cross-firm perspective to the supervision of the largest, most systemically important financial institutions.

Since the 2007 crisis, we have been giving significant thought to the composition of our supervisory portfolios, and, in particular to whether and how we should address the significant decrease in size and risk profile of the foreign firms in the LISCC portfolio over the past decade. I believe there is a compelling justification to make changes today to the composition of the foreign banks in the LISCC portfolio. I think it is important that all the Federal Reserve's supervisory portfolios have a clear and transparent definition. My goal is to develop, prospectively, a clear and transparent standard for identifying LISCC firms. My preferred approach for achieving this objective would be to align the LISCC portfolio with our recent tailoring categorizations.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Gonzalez:

Some of us on this committee have expressed concern about Facebook's Libra project given that it is based outside the US and that it creates a basket of different currencies that could make it difficult for the Fed to control monetary policy. Some other stablecoin projects seem different, however, in that they're based in the US and are backed only by dollars rather than by baskets of currencies. Vice Chairman Quarles, do you have concerns about these non-Libra, single-currency stablecoins and, if so, what are your concerns?

Single currency, U.S.-based stablecoins likely raise a narrower set of issues than initiatives such as Libra. Nonetheless, they still entail risks and merit attention. For example, these stablecoins raise the same potential for illicit payment activity that other cryptocurrencies do. While the substance and applicability of anti-money laundering expectations are clear in the U.S., monitoring and enforcement challenges may still exist. Additionally, single-currency stablecoins may raise consumer protection concerns similar to cryptocurrencies generally, including risks of fraud and theft. While stablecoins intend to reduce or lessen the price volatility seen with many cryptocurrencies, users of a stablecoin may or may not have a direct claim on its issuer or on the assets held by the issuer, and redemption terms also vary. Relatedly, depending on how they are structured, nonbank digital wallets may not offer the same safeguards as traditional bank accounts, including deposit insurance.

Cryptocurrency and stablecoin products have not to date achieved widespread adoption. As such, these instruments raise limited concerns with respect to financial stability and monetary policy, although more serious policy issues may result if they achieve wide-scale use or experience increasing financial linkages to traditional financial intermediaries. Even for a solely U.S. dollar-based stablecoin, the implications for financial stability and monetary policy would be highly dependent on the speed of its adoption and its design features, such as what kind of assets the stablecoin is backed with, whether it is interest-bearing, and its degree of separation from the traditional banking system.

Single-currency stablecoins, depending on their specific designs, likely would have simpler issuance, redemption, and asset management processes than are described in Libra's public materials. Nonetheless, payment networks that transfer these stablecoins or wider financial products developed from the coins would entail credit, liquidity, and operational risks that should be properly managed and that could create systemic risk at scale. Moreover, commercial bank funding models and the credit provided to households and businesses could also be affected by widespread single-currency stablecoin adoption, depending on the assets backing the single-currency stablecoin and whether households and businesses substitute away from traditional bank deposits.

I appreciate the insights provided by the regulators in their Interagency Statement on the Use of Alternative Data in Credit Underwriting. I am deeply committed to helping the underserved access credit to help themselves and their families and I think that AI and the use of alternative data points could be a part of the solution. As a part of the AI Task Force

I have learned about the attendant issues here and would love for either of you to expound on what the statement refers to as the potential for a "second look" for applicants that may have been denied under legacy underwriting and scoring systems and what that second look might mean for their ability to ultimately access credit?

As noted in the Interagency Statement, some firms may choose to use alternative data only for those applicants who would otherwise be denied credit based on traditional criteria, often called a "second look" approach. Applying alternative algorithms only to such consumers could help ensure that the algorithms expand access to credit. While such "second look" algorithms still must comply with fair lending and other laws, they may raise fewer concerns about unfairly penalizing consumers than algorithms that are applied to all applicants.[1]

At the end of your statement you assert that the agencies "may" provide more guidance on the use of alternative data. Can you pledge to me that you will work in tandem on all things related to any clarification of existing regulations and guidance related to AI, and that you will work with the CFPB as well, which is not represented here today? It is so important that we have regulatory consistency on these issues, issues like model risk guidance and things like the use of alternative data as well as fair lending related matters. Will you pledge to work on an interagency basis?

The Federal Reserve Board (Board) regularly coordinates with our fellow banking agencies on innovation-related matters in the supervision area. For example, staff from the federal financial institution supervisory agencies, including the Consumer Financial Protection Bureau, participate in an Interagency Fintech Discussion Forum, hosted by the Federal Reserve. Past discussion items have included topics such as model risk management, artificial intelligence, and alterative data. The agencies will continue these discussions at future meetings of the Interagency Fintech Discussion Forum. The Board also engages in discussions through an interagency task force on fair lending, as well as through the Federal Financial Institutions Examination Council's Task Force on Supervision and Task Force on Consumer Compliance.

I have a question about the regulatory workforce. AI and machine learning tools are powerful and complex. The race for talent for those that focus on these issues is competitive. Do you think regulators are well equipped to properly supervise the use of these powerful new tools using the existing framework?

The Board is committed to hiring and maintaining a highly professional workforce with the skills necessary to supervise effectively the activities of financial institutions subject to our supervision. As we have with other areas of specific expertise, we have enhanced our workforce with new staff experienced in the area of financial technology (fintech), as well as expanded the knowledge of existing staff. For the latter, the Board has launched a series of fintech examiner training tools to ensure that examination staff are equipped to engage with financial institutions that are adopting innovative technologies to meet their customers' needs. Among those training

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[1] See Carol A. Evans, "Keeping Fintech Fair: Thinking About Fair Lending and UDAP Risks," *Consumer Compliance Outlook* (Board of Governors of the Federal Reserve System, Dec. 2017), https://www.consumercomplianceoutlook.org/2017/second-issue/keeping-fintech-fair-thinking-about-fair-lending-and-udap-risks/.

tools are seminars, online learning sessions, and materials that discuss the latest developments in artificial intelligence/machine learning (AI/ML).

Do regulators have the required personnel in place to understand these tools and work with industry to address any concerns?

In addition to providing broad training programs, the Board maintains specialized examiners skilled in business technology risk assessment who are available to participate in examinations targeted at specific technologies. These include data scientists, technology analysts, and modeling experts with in-depth knowledge of fintech activities, as well as an ability to keep up to speed with the latest developments.

Board staff routinely meet with representatives from industry and academia whose work is on the cutting edge of fintech innovation. Through these discussions, staff remain abreast of recent developments in this fast-changing landscape. In addition to recent hires and ongoing training, Board leaders are exploring further ways to expand current expertise through hiring more staff with key technology skillsets, providing hands-on supervisory experience, and employing academic fellows experienced in financial technologies.

I know regulators have lots of lawyers and economists, but do you all have lots of data and computer scientists as well?

The Board has multi-disciplinary teams working on fintech issues, including (as noted above) data and computer scientists as well as technology analysts and modeling experts. We believe that having a supervisory team with different skill sets, experience, and perspectives provides the most comprehensive approach to understanding and supervising our institutions' use of fintech.

As one of the two national ACH operators, what steps (if any) can the Federal Reserve take to help prevent unauthorized withdrawals or reversals from occurring, such as those that occurred during the MyPayrollHR incident?

As an automated clearinghouse (ACH) operator, the Reserve Banks primarily act as a central clearing facility that receives and distributes payment files and information to its customers (financial institutions) and then performs settlement. The Reserve Banks offer certain risk origination and receipt services for use by financial institutions to help support their role in the payment system. Originating financial institutions are ultimately responsible to know their originators and have the appropriate controls in place in their payment processes. In addition, the National Automated Clearing House Association (Nacha) manages the rulemaking functions, including consumer protections, for the ACH Network. The Nacha Rules do not permit unauthorized withdrawals or reversals.

The MyPayrollHR incident presented a situation whereby the Nacha Rules were circumvented. In response, Nacha formed an industry work group that included the Board to discuss the errors made by ACH participants and the specific violations of the Nacha Rules. This work included the identification of best practices, aimed at further educating the ACH industry, as well as certain proposed amendments to the Nacha Rules to strengthen them going

forward. The Board will continue to pursue and participate in efforts to prevent these type of incidents from occurring.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Luetkemeyer:

President Obama signed the Insurance Capital Standards Clarification Act into law in 2014. That overwhelmingly bipartisan legislation made clear that Congress intended the Federal Reserve Board of Governors to tailor capital standards for insurance savings and loan holding companies and avoid the imposition of bank-centric standards. While there is support in Congress for the proposed building block approach framework, I am concerned by the Board's decision to also use the section 171 calculation, which runs contrary to Congressional intent by imposing a bank-centric capital standard on supervised insurers.

Why has the Board chosen to move forward with this additional calculation when it is not required pursuant to section 171?

Will you commit to working with me to ensure the intent of the Insurance Capital Standards Clarification Act is upheld through the application of tailored capital requirements?

Section 171 of the Dodd-Frank Act requires the Federal Reserve Board (Board) to establish minimum risk-based capital requirements for depository institution holding companies on a consolidated basis. The Insurance Capital Standards Clarification Act of 2014 (Clarification Act) amended section 171 to permit, but not require, the Board to exclude state-regulated insurers from this consolidated minimum risk-based capital requirement. The Clarification Act does not provide a blanket exemption for an entire holding company structure. In particular, it explicitly does not exempt a depository institution holding company from calculating its capital requirements for non-insurance entities in the corporate chain.

In September 2019, the Board issued a proposal on risk-based capital requirements for certain depository institution holding companies significantly engaged in insurance activities (proposal). The proposal would establish an enterprise-wide risk-based capital framework, known as the Building Block Approach, which is intended to facilitate the assessment of overall risk-based capital adequacy for a depository institution holding company that is significantly engaged in insurance activities by measuring aggregate capital while taking into consideration state insurance capital requirements. The proposal also includes a minimum risk-based capital requirement for the non-insurance entities within the holding company structure required by section 171, as amended by the Clarification Act (section 171 calculation). The section 171 calculation would use the flexibility afforded by the Clarification Act and exclude state-regulated insurers from minimum risk-based capital requirements to the extent permitted by law.

The Board recently invited public comment on all aspects of the proposal, including the section 171 calculation. Some comments suggested that the Building Block Approach would comply with the statutory requirements without an additional calculation. Consistent with the Administrative Procedure Act, the Board will consider this and other comments before making a final rule.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative McAdams:

Vice Chairman Quarles, it is reported that the Federal Reserve will not join the FDIC and OCC on a forthcoming proposal regarding the Community Reinvestment Act.

- **Can you elaborate on what aspects of the proposal specifically the Federal Reserve does not agree with the other agencies?**

- **Are you concerned that a lack of coordination amongst the agencies on a reform proposal will create confusion for market participants and community organizations?**

While the Federal Reserve Board (Board) did not join the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) in their recently issued Notice of Proposed Rulemaking (NPR) revising elements of Community Reinvestment Act (CRA) regulation, the Board has shared detailed analysis and proposals on CRA reform with our counterparts at the OCC and FDIC in the preparation of the NPR, and the NPR reflects much input from the Board. We will be reviewing the comments that are submitted to the FDIC and OCC on the NPR, and we expect to learn much—including much related to the aspects of the NPR that reflect our own input—from the review. As a result, it would be premature to identify any specific areas of disagreement—rather, we are all in the process of working to determine the best path forward. We continue to view a common approach as the best outcome, but we have not yet determined the best next steps to achieve that outcome.

In October, the Federal Reserve finalized "tailoring" rules for enhanced prudential standards and resolution planning requirements for domestic and internationally-headquartered firms. This included a categorization of firms based on certain risk-based indicators. It is my understanding that the Board's supervisory frameworks, such as the Large Institution Supervision Coordinating Committee (LISCC), do not match the final categorizations from the tailoring rules. You testified that the Board is in the process of "considering refinements" to the LISCC designation process.

- **As part of your review, is the Board considering aligning the LISCC framework with the categorizations under the new tailored regulatory requirements?**

- **What is the timeframe for the Board to complete its LISCC review process?**

- **In the hearing, you stated that revisions to the "LISCC designation process that will make it both more concrete, more rules based and more transparent." Can you expand upon what steps the Board will take to meet those objectives in the LISCC designation process?**

The Large Institution Supervision Coordinating Committee (LISCC) is a Federal Reserve Systemwide committee with the task of overseeing the supervision of the largest, most

systemically important financial institutions in the United States and chaired by the director of the Board's Division of Supervision and Regulation. The LISCC was formed after the financial crisis to bring an interdisciplinary and cross-firm perspective to the supervision of the largest, most systemically important financial institutions.

Since the 2007 crisis, we have been giving significant thought to the composition of our supervisory portfolios, and, in particular to whether and how we should address the significant decrease in size and risk profile of the foreign firms in the LISCC portfolio over the past decade. I believe there is a compelling justification to make changes today to the composition of the foreign banks in the LISCC portfolio. I think it is important that all the Federal Reserve's supervisory portfolios have a clear and transparent definition. My goal is to develop, prospectively, a clear and transparent standard for identifying LISCC firms. My preferred approach for achieving this objective would be to align the LISCC portfolio with our recent tailoring categorizations.

In general, we want to promote and encourage the long-term growth of companies. Such growth can help companies innovate and create new jobs – but such growth is often dependent on a variety of sources of capital, including directly from banks. I support the policy behind the Volcker Rule to prevent banks from engaging in short-term proprietary trading directly. However, it is my understanding that some provisions of the rule, specifically aspects of the covered funds provisions, may prohibit long-term investments if such investment is made using a fund structure. Chairman Powell has previously testified that a bank's long-term investments in covered funds is not an activity that typically threatens safety and soundness.

In the 2019 final rule related to the Volcker Rule, the agencies stated that they "continue to consider comments received and intend to address additional aspects of the covered funds provisions in the future covered funds proposal."

In this forthcoming rulemaking, do you expect to provide additional certainty to banks through an exclusion for investments in long-term investment vehicles in order to allow additional sources of capital for growing companies?

On January 30, 2020, the Board, the FDIC, the OCC, the Securities and Exchange Commission, and the Commodity Futures Trading Commission (the Agencies) agencies jointly issued approved a notice of proposed rulemaking (NPR)[1] addressing that would amend the covered fund provisions of the Volcker Rule regulations. The NPR, which was developed jointly by the Agencies, includes provisions that would give banking entities increased flexibility to invest in and sponsor venture capital funds and funds that extend credit.

[1] See https://www.federalreserve.gov/aboutthefed/boardmeetings/files/volcker-rule-fr-notice-20200130.pdf.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Riggleman:

I commend the Fed, FDIC, FinCEN, OCC, and CSBS on the joint statement to "provide clarity regarding the legal status of commercial growth and production of hemp and relevant requirements for banks." The statement goes on to say that since hemp has been de-scheduled via the farm bill that SARs are no longer required because it is a transaction involving hemp and that banks should follow standard BSA / AML procedures on these accounts. Finally, the statement says that FinCEN will issue additional guidance after further review of the USDA's rule.

What has the FDIC and Fed done to limit redundant or unnecessary SARs, and what can your agencies do to work with FinCEN to ensure that whatever guidance is issued is done so expediently and in a manner that is clear and concise for both examiners and financial institutions, especially regarding hemp banking?

As noted, the Interagency Statement on Providing Financial Services to Customers Engaged in Hemp-Related Businesses was issued on December 3, 2019.[1] Specifically, the statement clarified that because hemp is no longer a Schedule I controlled substance under the Controlled Substances Act, banks are not required to file a Suspicious Activity Report (SAR) on customers solely because they are engaged in the growth or cultivation of hemp in accordance with applicable laws and regulations. The Federal Reserve Board (Board) will provide training to examiners on this topic through our regular Systemwide Bank Secrecy Act (BSA) trainings, as well as in conjunction with the other federal banking regulators through classes and seminars provided by the Federal Financial Institutions Examination Council.

The guidance also indicates that the Financial Crimes Enforcement Network (FinCEN) intends to issue additional comprehensive guidance regarding hemp, which, in conjunction with the Interagency Statement, should limit redundant or unnecessary hemp-related SARs. FinCEN's additional guidance regarding hemp will be developed in consultation with the Federal Reserve and other banking agencies.

Has your agency engaged with any of the public private partnerships that are driving a consensus driven AML reform, and if so, will your agency be releasing any of the results or findings to the public?

The Board participates in public-private partnerships focused on anti-money laundering (AML) issues led by the U.S. Treasury. For example, the Board participates in the Bank Secrecy Act Advisory Group (BSAAG), where issues of AML reform are discussed on a public-private basis. The BSAAG is the means by which the U.S. Treasury receives advice on the operation of the BSA. The Director of FinCEN, as chair of the BSAAG, is responsible for ensuring that relevant issues are placed before the BSAAG for review, analysis, and discussion. The BSAAG

[1] See Supervision and Regulation letter 19-14, https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20191203a1.pdf.

consists of representatives from federal regulatory and law enforcement agencies, financial institutions, and trade groups with members subject to the requirements of the BSA.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Steil:

Vice Chairman Quarles, I want to thank you for your strong leadership in negotiations related to the Insurance Capital Standard (ICS). Like many members of the Financial Services Committee, I support our state-based system of insurance regulation and I am concerned about the prospect of importing incompatible European regulations through the ICS or a similar agreement.

What are your plans to ensure that the U.S. approach to insurance regulation is respected?

The Federal Reserve advocates for the U.S. approach to insurance regulation at the International Association of Insurance Supervisors (IAIS). As part of this advocacy, the U.S. members of the IAIS are developing an aggregation alternative to the Insurance Capital Standard (ICS). During the recent IAIS negotiations in Abu Dhabi, we agreed to a plan that creates space for this aggregation alternative to be recognized as providing comparable outcomes to the reference ICS. Under this plan, the IAIS will consult on the approach for assessing comparability in 2020 and 2021,with the goal of finalizing the approach in 2022, and then conducting the comparability assessment of the aggregation alternative. The Federal Reserve will continue to advocate for the U.S. approach at each of these decision points.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Timmons:

1. You have previously testified that the International Capital Standard (ICS) as currently structured is not fit for the US economy and could cause harm to the U.S. and maybe other national economies as well. Knowing this, I was pleased to see that as part of the deal reached in Abu Dhabi, there is a provision calling for an economic impact assessment of the ICS as part of the 5-year monitoring period.

- **Can you assure us that the Fed, and the Financial Stability Board, will actively follow up with the International Association of Insurance Supervisors (IAIS) to expedite the economic impact assessment of whether the ICS, if adopted, would cause harm to the U.S. and the global economy, including its effect on the US insurance industry's ability to provide insurance products of vital importance to US consumers?**

Team USA, which includes the Federal Reserve Board (Board), Treasury, and the National Association of Insurance Commissioners (NAICS), was the leading advocate for conducting an economic impact assessment on the International Capital Standard (ICS) during the monitoring period. The Board will contribute to this work and raise issues regarding it in an appropriate forum. The International Association of Insurance Supervisors will provide updates to the Financial Stability Board, which I chair, on developments on the ICS during the monitoring period.

2. Given the vast number of financial contracts that will have to be rewritten and renegotiated before the end of 2021, including many consumer mortgages, do you think it makes sense to extend the deadline for ending the use of LIBOR as a benchmark rate in financial contracts? Especially given the impact to the average consumer?

LIBOR-panel banks have only committed to submit quotes through the end of 2021; the decision to extend this deadline rests with the submitting banks themselves. Thus far, no banks have publicly committed to doing so, and the U.K. Financial Conduct Authority, the regulator of LIBOR, has said that it will not compel banks to submit after 2021. Since the publication of LIBOR is not guaranteed past that date, financial markets and institutions should prepare for such an event.

The Alternative Reference Rates Committee (ARRC) is guiding the transition from USD LIBOR and is acting under the assumption that LIBOR will stop sometime after 2021. The ARRC has encouraged liquidity in markets using the Secured Overnight Financing Rate (SOFR), so that a robust alternative to LIBOR is available to market participants, and has offered recommendations for fallback language for those who continue to issue new LIBOR instruments.

Transitioning away from LIBOR will make our financial system and the global financial system stronger and more resilient. Along with the Financial Stability Oversight Council (FSOC) and other regulators, the Federal Reserve is working with consumer groups, borrowers, and lenders to develop a fair and transparent process to make sure a large number of contracts are not

disrupted when LIBOR becomes unavailable. Consumer awareness about LIBOR cessation is still low and the ARRC is working to broaden retail market education.

Questions for The Honorable Randal K. Quarles, Vice Chair for Supervision, Board of Governors of the Federal Reserve System from Representative Wagner:

1. Mr. Quarles, in your testimony you stated that you are "still aiming to have [the stress capital buffer] done in time for the stress testing cycle," referring to the 2020 Comprehensive Capital Analysis and Review (CCAR). You also stated that you "have not decided yet whether [the Fed] would repropose or proceed in a different administrative fashion."

To clarify, is it the Fed's intention to finalize the stress capital buffer before firms begin receiving CCAR instructions in Q1 of next year?

It is my aim to have the stress capital buffer finalized in time for the Comprehensive Capital Analysis and Review 2020, while considering additional modifications in the future. The Federal Reserve Board continues to review the comments made on the stress capital buffer proposal and will provide further information when it has reached a decision.

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