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OVERSIGHT OF PRUDENTIAL REGULATORS

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTEENTH CONGRESS

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OVERSIGHT OF PRUDENTIAL REGULATORS

Wednesday, May 15, 2024

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

The committee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Patrick T. McHenry [chairman of the committee] presiding.

Present: Representatives McHenry, Lucas, Sessions, Posey, Luetkemeyer, Huizenga, Wagner, Barr, Williams of Texas, Hill, Loudermilk, Davidson, Rose, Steil, Timmons, Norman, Meuser, Fitzgerald, Garbarino, Kim, Flood, Waters, Velázquez, Sherman, Meeks, Scott, Lynch, Himes, Foster, Beatty, Vargas, Casten, Pressley, Tlaib, Torres, and Garcia.

Chairman MCHENRY. The committee will come to order.

Without objection, the chair is authorized to declare recess of the committee anytime.

The hearing today is entitled, "Oversight of Prudential Regulators."

Without objection, all members will have 5 legislative days within which to submit extraneous materials to the chair for inclusion in the record.

Just one additional comment for members about the schedule. This hearing has a hard stop at 2 p.m. and an accommodation of the three regulators before us, so it will not go past 2 p.m. Now I will recognize myself for 4 minutes to give an opening statement.

OPENING STATEMENT OF HON. PATRICK T. McHENRY, CHAIRMAN OF THE COMMITTEE ON FINANCIAL SERVICES, A U.S. REPRESENTATIVE FROM NORTH CAROLINA

We are here to conduct oversight of prudential regulators. There is plenty to discuss. Each of you on this panel has put forward a proposal that requires robust debate and explanation, yes, but you are first up, Mr. Gruenberg, and we all know why. You failed your employees, your Agency, and the American people. The fact that you have not yet resigned proves that you take no responsibility for your actions, and the words that you have used so far also make it clear you take no responsibility for your actions and let me be clear: showing up today is not an act of courage. It is an act of hubris. Last week, we were confronted with a report outlining appalling and abhorrent behavior at the Federal Deposit Insurance Corporation. This includes, Mr. Chairman, your verbally abusive behavior. This is beyond partisanship. It is clear from this report that deep institutional changes at the Federal Deposit Insurance Cor-

poration (FDIC) are necessary. Mr. Gruenberg, you are not the right person to lead those changes.

President Biden once said, "I am not joking when I say this. If you are ever working with me and I hear you treat another colleague with disrespect, talk down to someone, I promise, I will fire you on the spot." So I ask my colleagues, Democrat and Republican, the President, as well, if that behavior outlined in this report does not rise to that level, what does? Unfortunately, some of my colleagues may attempt to defend the indefensible today by shifting blame to Republican FDIC chairs, but let me remind my colleagues, Chair Gruenberg has led this Agency for 10 of the last 13 years. You may hear about employees' favorability ratings, which come from annual surveys conducted of Federal employees at Federal agencies. There was a decline in satisfaction in the 2018 survey, which only included a couple of months of former Chair McWilliams' tenure, so that steep decline was dissatisfaction with Chair Gruenberg. Then in 2020, during the core of former Chair McWilliams' leadership, FDIC employee satisfaction went up to its highest level since 2012, and that was before Mr. Gruenberg's first stint as chair. When Chair Gruenberg returned to lead the Agency again, employee satisfaction plummeted. So I implore my colleagues to be consistent when judging the behavior of our regulators. This is not just about mismanagement. It is clear misconduct.

It is a shame we have to spend this much time talking about your conduct and failed leadership. There are very real issues facing our financial system that deserve this committee's full attention. The Biden Administration's banking regulators are busy pursuing serious agendas, some of us view as partisan agendas, that are focused on policies that do not support the economy, this financial system and the safety and soundness of the financial system, or the needs of American families but first, we have to focus on the conduct of the FDIC chair and ensure that this very important Agency returns to a safe and sound manner and practice as our financial system needs it. So we have significant proposals at the FDIC, yes, and at the Federal Reserve System (Fed), and just earlier this week, Chair Powell testified that the Basel III Endgame proposal would undergo significant changes and I view that as quite promising, and I certainly hope my colleagues will ask Mr. Barr about that as well.

With that, I will yield back and recognize the ranking member for 4 minutes for an opening statement.

OPENING STATEMENT OF HON. MAXINE WATERS, RANKING MEMBER OF THE COMMITTEE ON FINANCIAL SERVICES, A U.S. REPRESENTATIVE FROM CALIFORNIA

Ms. WATERS. Thank you very much, Mr. Chairman. Good morning. I would like to thank our witnesses from the Federal Reserve, the FDIC, and the Office of the Comptroller of the Currency (OCC) for coming before the committee today.

I want to start by addressing the FDIC report on workplace culture and sexual harassment that was released last week. The report was deeply troubling and makes clear that under both Republican and Democratic chairs, the FDIC has not done its job to prop-

erly address the deep-rooted, toxic work culture that has festered over many years at the Agency. All employees deserve a work environment where they feel safe, and it is Chair Gruenberg's responsibility to make sweeping changes properly for the benefit of every FDIC worker. While the report scrutinizes Chair Gruenberg, I am disappointed the report seemed to downplay workplace concerns and complaints of harassment that occurred under prior Republican Agency leadership. Regardless, the FDIC as an institution has a lot of work to do.

The Agency can start by expediting the implementation of the action plan I requested of Chair Gruenberg last year, along with the recommendations laid out in the most recent report. As the report states, tone does start at the top, and I am concerned that Republicans, who have been quick to call Chair Gruenberg to resign, are selectively applying that standard. After all, the top Republican and nominee to be President is currently on trial regarding the first of a series of criminal indictments and has been found liable for sexual abuse. Hopefully, this concerns them, too, and they will call on the former President to step down and withdraw his nomination. Now I look forward to hearing from Chair Gruenberg who has committed to making the necessary changes to turn the tide on the culture at the FDIC.

Under the leadership of Chair Gruenberg, the FDIC has done a lot of important work, including his work to combat modern-day redlining by strengthening the Community Reinvestment Act, not to mention the quick action taken to prevent last year's regional bank failures from spiraling into a full-on financial crisis. As important as this work is, it will be permanently tainted if the working environment of the people doing the work remains mired and toxic. It is crucial that we have a regulator who works every day to not only promote stability and ensure the banking system serves all of our constituents but also treats its employees with fairness and kindness. I am disappointed in your performance on the latter, Chair Gruenberg.

Turning to a few other matters that are the subject of today's hearing, I want to applaud the FDIC, OCC, and Federal Housing Finance Agency (FHFA) by heeding the calls I made after last year's bank failures to implement Section 956 of Dodd Frank, to hold greedy bank executives accountable for reckless risk taking. It is past time for the Fed and other regulators to follow suit and implement this congressional mandate without further delay. In addition, I look forward to hearing what our regulators are doing to build on committee Democrats' record of protecting consumers in light of the proposed Capital One and Discover merger to create the largest credit card lender in the country. I want to hear what regulators are doing to put away the rubber stamp and strengthen bank merger reviews. I am glad the Fed and OCC announced they will hold a public hearing in July. I hope regulators listen to the feedback and then block this deeply flawed merger. As the climate crisis worsens, I am also eager to hear about their efforts to ensure climate risk is taken seriously as a risk to our banking system and that diversity and inclusion is front and center, especially in the light of misguided Republican attacks.

I look forward to today's discussion, and I yield back.

Chairman MCHENRY. I will now recognize the chair of the Financial Institutions and Monetary Policy Subcommittee, Mr. Barr of Kentucky, for 1 minute.

STATEMENT OF HON. ANDY BARR, CHAIRMAN OF THE SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND MONETARY POLICY, A U.S. REPRESENTATIVE FROM KENTUCKY

Mr. BARR of Kentucky. Mr. Gruenberg, the Cleary report on harassment issues at the FDIC outlining your temperament and inability to lead shows an Agency in crisis. As the report made clear, your stubborn lack of self-awareness and mismanagement mean that you are not the person to respond to the FDIC's crises, and you do not have the moral authority to lead the needed transformation of the FDIC. The Cleary report on your prior participation in Operation Choke Point and the leadership coup at the FDIC that you engaged in with Mr. Chopra makes clear that you prioritize politicizing a supposed independent Agency over the safety and soundness of our financial system, and, therefore, it is time for you to resign. Do you think for 1 minute that if the kind of misconduct outlined in the report was uncovered at an FDIC-regulated bank, that Chair Gruenberg would offer any kind of grace to the management of that bank? The question answers itself.

On the issue of Basel III, I want to make my ongoing position clear that the fundamentally flawed proposal must be scrapped, and at most there should be a re-proposal, if justifiable. I yield back.

Chairman MCHENRY. Now the ranking member of the Financial Institutions and Monetary Policy Committee will be recognized for 1 minute. Mr. Foster is recognized for 1 minute.

STATMENT OF HON. BILL FOSTER, RANKING MEMBER OF THE SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND MONETARY POLICY, A U.S. REPRESENTATIVE FROM ILLINOIS

Mr. FOSTER. Thank you, Mr. Chairman. Last week, like many of my colleagues, I was appalled by the findings of the independent review and the allegations of sexual harassment and interpersonal misconduct that have been festering at the FDIC for far too long. The report paints a picture of an Agency plagued by a toxic culture that has allowed inappropriate workplace conduct to persist without accountability. Despite the purported efforts under both Democratic and Republican Administrations to address these ongoing issues for more than a decade, hundreds of current and former FDIC staff bravely shared stories of workplace misconduct with the authors of the report with some, in fact, going to great lengths to hide their identity. As someone who has led successful organizations and teams, I know that an organization's culture starts at the top, and we need agency leaders who comprehend the problem and are committed to implementing and following through the meaningful reforms that will ensure our agencies can attract and retain dedicated staff.

Our banking regulators have important work to do, much of which we will be highlighting today, but it is essential to the success of that work that meaningful action is taken to address these long-term personnel issues. I encourage my colleagues to take the

time to fully review the facts of the situation. Thank you, and I yield back.

Chairman MCHENRY. Today we welcome the testimony of Honorable Michael S. Barr, vice chair for supervision of the Federal Reserve Board of Governors; Hon. Martin J. Gruenberg, chairman of the Board of Directors of the Federal Deposit Insurance Corporation; and Mr. Michael Hsu, acting comptroller of the Office of Comptroller of the Currency.

You will be recognized for 5 minutes to give an oral presentation of remarks. You all are accustomed to this, testifying before this committee.

Without objection, your written statements will be made a part of the record, and without objection, the statement of Hon. Todd Harper, chairman of the National Credit Union Administration, will be included in the record as well. He is not here today because of exigent circumstances, made well aware of the committee well beforehand, so we will include his testimony without objection.

[The information referred to can be found in the appendix on page 110.]

Chairman MCHENRY. Finally, before we begin, I will swear the witnesses in, so if you will please stand and raise your right hand. Once I read the oath, I will ask each of you to respond individually.

Do you solemnly swear or affirm that the testimony you will give before this committee in the matters under consideration will be the truth, the whole truth, and nothing but the truth, so help you God? Again, Mr. Barr?

Mr. BARR. I do.

Chairman MCHENRY. Mr. Gruenberg.

Mr. GRUENBERG. I do.

Chairman MCHENRY. Mr. Hsu.

Mr. HSU. I do.

Chairman MCHENRY. Thank you. You may be seated.

The record will reflect each witness answered in the affirmative.

We will now recognize Vice Chair Barr for 5 minutes to give an oral presentation of your remarks.

STATEMENT OF HON. MICHAEL BARR, VICE CHAIRMAN FOR SUPERVISION, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Mr. BARR. Chairman McHenry, Ranking Member Waters, and other members of the committee, thank you for the opportunity to testify on the Federal Reserve's supervisory and regulatory activities. Accompanying my testimony is the Federal Reserve's Semi-Annual Supervision and Regulation Report. Today, I will discuss current conditions in the banking sector, supervisory activities, and some of our recent regulatory proposals.

Overall, the banking system remains sound and resilient. Banks continue to report capital and liquidity ratios above minimum capital regulatory levels. Overall asset quality remains generally sound. Capital ratios increased throughout 2023, leaving the system better positioned to weather potential losses. Liquidity conditions overall are stable. Notably, liquid assets on bank balance sheets remained above their 10-year average throughout 2023.

Additionally, there has been a decrease in the share of uninsured deposits in the system. However, both supervisors and banks must remain vigilant and ready for expected and unexpected stresses, and presently there are several risks we are monitoring. For example, delinquency rates are rising among certain commercial real estate loans, such as those backed by offices, and some consumer loan sectors. Commercial Real Estate (CRE) delinquencies are now at a 5-year high. Credit card and auto loan delinquencies have been rising. In response to rising delinquencies, banks have increased loan loss provisions. On this basis, combined with their capital positions, the banking sector as a whole should be prepared to absorb loan losses that may materialize and continue fulfilling its vital role providing credit to households and businesses. The Federal Reserve continues to monitor these conditions closely.

It has been a little over a year since the sudden failure of Silicon Valley Bank (SVB) and ensuing stress in the banking system, events which highlighted the need to improve the speed, force, and agility of supervision to better align with the risks, size, and complexity of supervised banks as appropriate. We have been making progress on these goals. First, we are working to ensure supervision intensifies at the right pace as a bank grows in size and complexity. Second, we are modifying supervisory processes so that once issues are identified, they are addressed more quickly by both banks and supervisors. Third, we are finding ways to better incorporate forward-looking risk analysis into supervision.

The lessons learned from SVB are not only applicable to our supervisory framework. Certain aspects of the failure show that enhancements to our regulatory framework would benefit the safety and soundness of the banking system. One of these enhancements was already in process several months before SVB's failure through an advanced notice of proposed rulemaking expanding the application of long-term debt requirements to additional large banks. Subsequently, the Board, the FDIC, and the OCC followed up with a proposed rule that would increase the options available within the resolution process and enhance financial stability. We are going through comments we received on this proposal carefully.

Another important area is liquidity risk management. A striking feature of last year's bank stress was that SVB, Signature Bank, and First Republic struggled to cope with unprecedented deposit outflows. Banks found it difficult to monetize their held-to-maturity securities through repo transactions under severe stress and were not adequately prepared to utilize the Federal Reserve's discount window. We are exploring targeted adjustments to our regulatory framework that would address each of these concerns: deposit outflows, held-to-maturity monetization, and discount window preparedness. The Federal Reserve's lending to banks through the discount window plays an important role in supporting the liquidity and stability of the banking system and the effective implementation of monetary policy. We are reaching out to a wide range of depository institutions of all sizes to learn from their experiences with the discount window in order to improve our operations.

Turning to capital, a safe and sound banking system is critical to a healthy economy, and capital is foundational to safety and soundness. A well-capitalized banking system reduces the prob-

ability that stressful conditions result in financial crises, which inflict devastating economic costs and suffering for families and businesses all across the country. Since my last testimony, we have received numerous and meaningful comments on our proposal. We also received additional data. We are closely analyzing this information, and I expect that we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward. The changes will enable us to have a safer financial system that better serves American households and businesses. Thank you.

[Prepared statement of Mr. Barr follows:]

Scheduled for delivery at:
10:00 a.m. EDT
May 15, 2024

Statement by

Michael S. Barr

Vice Chair for Supervision

Board of Governors of the Federal Reserve System

before the

Committee on Financial Services

U.S. House of Representatives

May 15, 2024

Chairman McHenry, Ranking Member Waters, and other members of the Committee, thank you for the opportunity to testify on the Federal Reserve's supervisory and regulatory activities. Accompanying my testimony is the Federal Reserve's semiannual *Supervision and Regulation Report*. Today, I will discuss current conditions in the banking sector, supervisory activities, and some of our recent regulatory proposals.

Banking Conditions

Overall, the banking system remains sound and resilient. Banks continue to report capital and liquidity ratios above minimum regulatory levels. Overall asset quality remains generally sound. Lending continues to grow but has slowed from the rapid pace of 2022, reflecting decreased demand and tighter lending standards.

Capital ratios increased throughout 2023, leaving the system better positioned to weather potential losses, such as those from defaults on loans, or declines in the fair value of investment securities, which continued to accumulate at some banks this past year.

Liquidity conditions overall are stable. Notably, liquid assets on bank balance sheets remained above their 10-year average throughout 2023, largely the result of a significant buildup in cash positions. Aggregate deposits were generally stable in the second half of 2023 and have been steadily increasing in the first three months of 2024, reaching a level not seen since before the stress of March of last year. Additionally, there has been a decrease in the share of uninsured deposits in the system.

However, both supervisors and banks must remain vigilant and ready for expected and unexpected stresses, and presently there are several risks we are monitoring. For example, delinquency rates are rising among certain commercial real estate (CRE) loans, such as those backed by offices, and some consumer loan sectors. CRE delinquencies are now at a five-year

high. Credit card and auto loan delinquencies have been rising. In response to rising delinquencies, banks have increased loan loss provisions. On this basis, combined with their capital positions, the banking sector as a whole should be prepared to absorb loan losses that may materialize and continue fulfilling its vital role providing credit to households and businesses. The Federal Reserve continues to monitor these conditions closely.

The recovery from the acute stress experienced in March of last year is in no small part due to the success of the Bank Term Funding Program (BTFP). This program was established shortly after the failure of Silicon Valley Bank (SVB) to help assure the stability of the banking system and to support the economy. The BTFP helped to alleviate liquidity pressures, particularly for banks that had experienced significant declines in the value of securities. The BTFP ceased making new loans as scheduled in March without any related liquidity stress in the banking system.

Supervision

It has been a little over a year since the sudden failure of SVB and ensuing stress in the banking system—events which prompted questions about how banks manage risks and how we at the Federal Reserve and other agencies supervise that risk-taking. As noted in my testimonies last year, these events highlighted the need to improve the speed, force, and agility of supervision to align better with the risks, size, and complexity of supervised banks, as appropriate.

As the banking system changes, supervision must adapt with it and appropriately account for banks of different sizes and levels of complexity. Risks can materialize quickly and come from various sources, and in March of last year, we saw that these risks can lead to failure more quickly than ever. Therefore, supervisors must take timely action as risks build up; deploy supervisory tools and escalation effectively; account for changes in market, economic, and

financial conditions in their examination priorities and supervisory conclusions; and identify new and different patterns of risks. We have been making progress on these goals.

First, we are working to ensure supervision intensifies at the right pace as a bank grows in size and complexity. This involves more frequently assessing the condition, strategy, and risk management of large and complex banking organizations and engaging more frequently with these firms through the supervisory process. Additionally, supervisors are encouraging growing regional banking organizations to enhance their risk capabilities commensurately with their risk profiles so that the transition to higher standards is more of a gradual slope rather than a cliff.

Second, we are modifying supervisory processes so that once issues are identified, they are addressed more quickly by both banks and supervisors. For example, examiners have been conducting additional supervisory activities for firms with large unrealized losses on securities, high CRE exposures, or other material vulnerabilities. Where weaknesses in risk management have been identified, examiners are requiring firms to address these weaknesses promptly and encouraging them to bolster their capital and liquidity positions.

Third, we are finding ways to better incorporate forward-looking analysis into supervision. A forward-looking view supports the goal of identifying and addressing material risks before they become serious issues. Forward-looking risk analysis also may help to challenge supervisory assessments and foster meaningful action where risks are underappreciated.

Regulation

The lessons learned from SVB are not only applicable to our supervisory framework. Certain aspects of the failure showed that enhancements to our regulatory framework would benefit the safety and soundness of our banking system.

Long-Term Debt

One of these enhancements was already in process several months before SVB's failure through an advance notice of proposed rulemaking—expanding the application of long-term debt requirements to additional large banks. Subsequently, the Federal Reserve Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (collectively, the agencies) followed up with a proposed rule calibrated to reflect the lower risk profiles of such banks as compared to the largest and most complex. The proposal would increase the options available within the resolution process and enhance financial stability. Losses to the Deposit Insurance Fund related to the bank failures last year could have been mitigated in part by the proposed requirements. We are going through comments we received on this proposal carefully.

Liquidity

Another important area is liquidity risk management. A striking feature of last year's bank stress was that SVB, Signature Bank, and First Republic struggled to cope with unprecedented deposit outflows arising from a loss of confidence by their uninsured depositors. Other banks that experienced spillovers during this period struggled with insufficiently robust liquidity risk management. Banks found it difficult to monetize their held-to-maturity securities through repo transactions under severe stress and were not adequately prepared to utilize the Federal Reserve's discount window. Additionally, the stress revealed that some forms of deposits—such as those from venture capital firms, high-net-worth individuals, crypto firms, and others—may be more prone to faster runs than previously assumed. We are exploring targeted adjustments to our regulatory framework that would address each of these concerns: deposit outflows, held-to-maturity monetization, and discount window preparedness.

Discount Window Operations

Discount window preparedness is essential. The Federal Reserve's lending to banks through the discount window plays an important role in supporting the liquidity and stability of the banking system and the effective implementation of monetary policy. By providing ready access to funding, the discount window helps depository institutions manage their liquidity risks. Providing liquidity in this way is one of the original purposes of the Federal Reserve System. It is important that we continue to work to improve this tool. To that end, we are reaching out to a wide range of depository institutions of all sizes to learn from their experiences with the discount window. From this outreach, we will identify and prioritize changes to operations that can improve the efficacy of our liquidity provision.

Capital

A safe and sound banking system is critical to a healthy economy, and capital is foundational to safety and soundness. Well-capitalized banks have more capacity to support the economy by continuing to lend to households and businesses through stressful conditions. A well-capitalized banking system reduces the probability that stressful conditions result in financial crises, which inflict devastating economic costs and suffering for families and businesses all across the country. Strong capital also reduces the risk that the government would need to intervene in unusual and exigent circumstances.

This brings me to the agencies' proposal to enhance capital requirements. Since my last testimony, we have received numerous and meaningful comments on the proposal. We also received additional data from a special data collection. We are closely analyzing this information, and I expect we will have a set of broad, material changes to the proposal that allow

us to have a broad consensus in moving the proposal forward. The changes will enable us to have a safer financial system that better serves American households and businesses.

Thank you. I am happy to take your questions.

Chairman MCHENRY. Chairman Gruenberg, you are recognized for 5 minutes.

STATEMENT OF HON. MARTIN GRUENBERG, CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. GRUENBERG. Thank you, Mr. Chairman. Chairman McHenry, Ranking Member Waters, and members of the committee, thank you for the opportunity to appear before you today. My written statement reports on the state of the banking industry and the condition of the FDIC's Deposit Insurance Fund. The written testimony also provides an update on FDIC resolution activities and discusses proposed improvements in regulation and supervision. However, I would like to focus my remarks today on the FDIC's ongoing efforts to transform its workplace culture.

Let me begin by saying that I am deeply committed to the FDIC and its mission as well as to the people on whom that mission depends. That is why when reports of sexual harassment, discrimination, and other misconduct surfaced last year, it was essential as a starting point to gain a deeper understanding of the Agency's workplace culture. At my direction, the FDIC initiated an independent third-party review to determine the depth and extent of these issues. Last week, the results of that review, which was conducted by the law firm of Cleary Gottlieb, were released.

The review found that for an extended period of time, the FDIC has failed to provide a workplace safe from sexual harassment, discrimination, and other personal misconduct. I accept the findings of the report, and as chairman, I take full responsibility to anyone who has experienced sexual harassment, discrimination, or other misconduct at the FDIC. I, again, personally want to apologize and express how deeply sorry I am. I also acknowledge my own failures as chairman, both in failing to recognize how my temperament in meetings impacted others and for not having identified the deeper cultural issues at the FDIC sooner. I am personally committed to addressing these issues. We accept all of the recommendations of the report and are incorporating them into our existing action plan for a safe, fair, and inclusive work environment. To restore credibility to our workforce, we must act swiftly on the report's recommendations and demonstrate a commitment to making fundamental changes. For this reason, we are already implementing several key recommendations of the report.

The report recommends that we identify and appoint a transformation monitor who will monitor, audit, and report on our implementation of the recommendations. We have already begun this process and will issue a request for proposals for this purpose as early as this week. The report also recommends that we engage an independent third-party expert to support our efforts. We have begun that process and will also issue a request for proposals for that purpose as early as this week. The report recommends fundamental change to the Agency structure and procedures for receiving and investigating complaints and taking disciplinary action against misconduct in light of the failures of the existing officers delegated to those duties. We will do this by proposing the establishment of an independent office of professional conduct, which will report directly to the FDIC Board of Directors. It will be charged with ful-

filling these responsibilities, including through the use of outside third parties to conduct investigations. The transformation monitor and independent third-party expert will advise us on this proposal.

Since December, the FDIC has been focused on implementing its action plan to address all aspects of the issues raised in the news reports last year. The action plan represents an Agency-wide effort with participation by employees at all levels. Many of the recommendations outlined in the report are already encompassed by the Agency's action plan. The action plan is focused on three core elements: providing more support and resources to victims, strengthening our process for reporting and investigating complaints, and improving accountability for anyone who is found to engage in misconduct, including through separation from the Agency. The new Office of Professional Conduct will address these core objectives.

Mr. Chairman, it is my privilege to lead and work alongside everyone at the FDIC. Our people are dedicated to the Agency and its mission. They deserve a workplace where all feel safe, valued, and respected. There is no higher priority for me than delivering on that commitment. Thank you, and thank you for the additional time, Mr. Chairman.

[Prepared statement of Mr. Gruenberg follows:]

STATEMENT BY

MARTIN J. GRUENBERG
CHAIRMAN
FEDERAL DEPOSIT INSURANCE CORPORATION

on

"Oversight of Prudential Regulators"

before the

COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVES

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2128 Rayburn House Office Building
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Chairman McHenry, Ranking Member Waters, and Members of the Committee, I am pleased to appear at today's hearing on "Oversight of Prudential Regulators." I appreciate the opportunity to report on the Federal Deposit Insurance Corporation's (FDIC) recent work in protecting insured deposits, supervising state chartered banks that are not members of the Federal Reserve system for safety and soundness and consumer protection, and in resolving failed insured depository institutions (IDIs).

My statement reports on the state of the banking industry and the condition of the FDIC's Deposit Insurance Fund (DIF). The testimony provides an update on FDIC resolution activities and discusses the release of a paper reaffirming the FDIC's preparedness to apply the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) Title II[1] framework in the resolution of a global systemically important bank (GSIB). In addition, I discuss improvements in regulation and bank supervision that could help prevent bank failures like those that occurred in the spring of 2023 or mitigate their impact in the future, such as initiatives to improve banks' management of liquidity and funding risks and a rulemaking to strengthen corporate governance at larger banks.

My testimony discusses other important regulatory activities at the FDIC, including an update on the Basel III Notice of Proposed Rulemaking, the release of an FDIC request for information and comment on revisions to the FDIC's Statement of Policy on Bank Merger Transactions, and steps taken to initiate a joint rulemaking on incentive-based compensation.

First and foremost, my testimony will discuss my top priority, addressing workplace culture issues at the FDIC.

[1] 12 U.S.C. §§ 5381, *et seq.*

FDIC Workplace Culture

I am deeply committed to the FDIC and its mission, as well as to the people on whom that mission depends. I love this agency, and its people must be protected.

That is why, when news reports of harassment, discrimination, and other misconduct first surfaced last year, it was essential to gain a deeper understanding of the agency's workplace culture. At my direction, the FDIC initiated an independent, third-party review to determine the depth and extent of these issues. Last week, the results of that review, which was conducted by the law firm of Cleary Gottlieb, were released.[2] The review found that for an extended period of time, the FDIC has failed to provide a workplace safe from sexual harassment, discrimination, and other personal misconduct.

I accept the findings of the report and, as Chairman, I take full responsibility. To anyone who has experienced sexual harassment or other misconduct at the FDIC, I again want to apologize and express how deeply sorry I am. I also acknowledge my own failures as Chairman, both in failing to recognize how my temperament in meetings impacted others and for not having identified deeper cultural issues at the FDIC sooner. I am personally committed to addressing these issues. We accept all of the recommendations of this report and are incorporating them into our existing Action Plan for a Safe, Fair, and Inclusive Work Environment.[3]

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[2] See PR-35-2024, *FDIC Special Review Committee Releases Independent Report on Workplace Misconduct and Culture* (May 7, 2024) available at https://www.fdic.gov/news/press-releases/fdic-special-review-committee-releases-independent-report-workplace-misconduct

[3] See *Action Plan for a Safe, Fair, and Inclusive Work Environment* (Updated December 4, 2023), available at: https://www.fdic.gov/about/diversity/pdf/action-plan-12-4-23-v1.pdf.

To restore credibility with our workforce, we must act swiftly on the report's recommendations and demonstrate a commitment to making fundamental change. For this reason, we have already begun implementing several key recommendations.

The report recommends that we identify and appoint a transformation monitor who will monitor, audit, and report on our implementation of the recommendations. We have already begun that process and will issue a Request for Proposals for this purpose as early as this week.

The report also recommends that we engage an independent third-party expert to support our efforts. We have begun that process and will also issue a Request for Proposals for this purpose as early as this week.

The report recommends fundamental change to the agency's structure and procedures for receiving and investigating complaints, and taking disciplinary action against misconduct in light of the failures of the existing offices delegated those duties. We will do this by proposing the establishment of an independent Office of Professional Conduct, which will report directly to the FDIC Board of Directors. It will be charged with fulfilling these responsibilities, including through the use of outside third-parties to conduct investigations. The transformation monitor and independent third-party expert will advise us on this proposal.

Since December, the FDIC has been focused on implementing its Action Plan to address all aspects of the issues raised in the news reports. The Action Plan represents an agency-wide effort, with participation by employees at all levels.

Many of the recommendations outlined in the report are already encompassed by the agency's Action Plan, and in some instances, our Action Plan goes beyond the recommendations in the report. The Action Plan is focused around three core elements - providing more support

and resources to victims, strengthening our process for reporting and investigating complaints, and improving accountability for anyone who is found to engage in misconduct, including through separation from the agency. The proposal to establish an independent Office of Professional Conduct would advance all of these goals.

It is my privilege to lead and work alongside everyone at the FDIC. Our employees are extraordinarily dedicated to the agency and its mission. The work they do day-in and day-out is critical to maintaining stability and confidence in our banking system, whether by strengthening the safety and soundness and resolvability of U.S. financial institutions, responding to the bank failures of last year, or through financial literacy and inclusion efforts. They deserve to have a workplace where all feel safe, valued and respected. There is no higher priority for me than delivering on that commitment.

State of the Banking Industry

The banking industry has shown resilience after a period of liquidity stress in early 2023. Full-year 2023 net income remained well above levels reported before the pandemic, overall asset quality metrics were favorable, and the industry's liquidity was stable as of the end of 2023. However, banks reported lower net interest margins and higher funding pressures. Some loan portfolios, such as credit cards, auto loans, and non-owner-occupied commercial real estate loans, are exhibiting increasing delinquency and charge-off rates. Although unrealized losses on securities declined in the fourth quarter, they remain elevated compared to historical levels. While the FDIC Quarterly Banking Profile data will not be available until later this month, early reports from the first quarter of 2024 indicate that net interest margin pressures continued, and

higher market interest rates likely have reduced bank securities values, increasing unrealized losses.

In the fourth quarter of 2023, domestic deposits increased for the first time in seven quarters, driven by growth in time deposits. The industry's insured deposits increased by 0.5 percent. Uninsured deposit growth was masked by one large bank that eliminated a significant amount of intercompany deposits. Excluding that bank from the calculations, the industry increased uninsured deposits in the quarter by $92 billion, or 1.4 percent, and growth was widespread among bank size groups. This would have been the industry's first increase in uninsured deposit levels after seven consecutive quarters of decline.

The banking industry continues to face significant downside risks from the continued effects of inflation, volatility in market interest rates, and geopolitical uncertainty. Moreover, the economic outlook remains uncertain, despite sustained economic growth in 2023 that exceeded expectations. These risks could cause credit quality and profitability to weaken, loan growth to slow, provision expenses to rise, and liquidity to become more constrained. Commercial real estate (CRE) loan portfolios, particularly loans backed by office properties, face challenges when loans mature as demand for office space remains weak and property values continue to soften. The FDIC will continue to closely monitor these risk as well as the broader prevailing trends in the banking industry over the coming year.

Condition of the Deposit Insurance Fund

As of December 31, 2023, the Deposit Insurance Fund (DIF) balance declined to $121.8 billion, down $6.4 billion (5.0 percent) from year-end 2022, primarily resulting from an increase

in loss provisions associated with five bank failures during the year.[4] Following the failure of two large banks in March of 2023, the banking industry experienced outflows of total deposits, but also experienced strong insured deposit growth. This growth in insured deposits, coupled with the decline in the DIF balance, resulted in a decline in the reserve ratio of 10 basis points from 1.25 percent as of December 31, 2022, to 1.15 percent as of December 31, 2023.[5]

Philadelphia-based Republic First Bank was closed on April 26, 2024, resulting in an estimated loss of $667 million. This is the only bank to fail so far in 2024 and is not reflected in the DIF balance stated as of December 31, 2023. A total of five banks failed in 2023, resulting in a combined estimated loss at December 31, 2023, of $40.4 billion.[6] As of December 31, 2023, the FDIC estimated the cost for the failures of Silicon Valley Bank (SVB) and Signature Bank to total $23.6 billion. Of that estimated total cost, the FDIC estimates that approximately $20.4 billion was attributable to the cost of covering uninsured depositors as a result of the systemic risk determination made on March 12, 2023, following the closures of SVB and Signature Bank. By statute, that estimated $20.4 billion cost of covering uninsured depositors must be recovered through a special assessment, which was finalized in November 2023.[7] Accordingly, the impact on the DIF from the five bank failures in 2023 is estimated as a loss of $20 billion as of December 31, 2023,[8] which excludes the cost of protecting uninsured depositors as a result of the

[4] The decline in the DIF balance does not include the cost of protecting uninsured depositors pursuant to the systemic risk determination announced following the failures of Silicon Valley Bank and Signature Bank in March 2023, as the FDIC is required by statute to recover those losses through special assessments. *See* 12 U.S.C. 1823(c)(4)(G)(ii).

[5] The reserve ratio is calculated as the ratio of the net worth of the DIF (fund balance) to the value of the aggregate estimated insured deposits at the end of a given quarter. See 12 U.S.C. 1813(y)(3).

[6] Information on all bank failures is available at: https://www.fdic.gov/resources/resolutions/bank-failures/failed-bank-list/.

[7] See *Final Rule on Special Assessment Pursuant to Systemic Risk Determination*, available at https://www.govinfo.gov/content/pkg/FR-2023-11-29/pdf/2023-25813.pdf.

[8] Only the remaining estimated loss from SVB and Signature Bank of $3.2 billion, combined with the estimated losses of the three other banks that failed in 2023, directly impact the December 31, 2023 DIF balance. The three other banks that failed in 2023 include First Republic Bank of San Francisco, CA, at an estimated loss of $16.7

systemic risk determination. It should be noted that as with all failed bank losses, loss estimates are periodically adjusted as the FDIC, as receiver of the failed banks, sells assets, satisfies liabilities, and incurs receivership expenses. The final cost will be determined when the FDIC terminates the receiverships.

As required by the Federal Deposit Insurance Act (FDI Act),[9] the FDIC has been operating under a restoration plan since September 15, 2020,[10] which aims to restore the DIF to the statutory minimum reserve ratio of 1.35 percent within eight years. Notwithstanding the growth in insured deposits and recent losses due to bank failures, including the April 2024 failure of Republic First Bank, the DIF remains on track to meet the statutory minimum reserve ratio of 1.35 percent by the eight-year deadline of September 30, 2028.[11]

Bank Receiverships

Republic First Bank

On April 26, 2024, Republic First Bank (doing business as Republic Bank), Philadelphia, Pennsylvania, was closed by the Pennsylvania Department of Banking and Securities, which appointed the FDIC as receiver. As of January 31, 2024, Republic Bank had approximately $6 billion in total assets and $4 billion in total deposits. To resolve the bank, the FDIC entered into a Purchase and Assumption Agreement with Fulton Bank, National Association of Lancaster, Pennsylvania, to assume substantially all of the deposits and purchase substantially all the assets of Republic Bank.

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billion, Heartland Tri-State Bank of Elkhart, KS, at an estimated loss of $54.2 million and Citizens Bank of Sac City, IA, at an estimated loss of $14.8 million. Loss estimates are as of December 31, 2023.

[9] Section 7(b)(3)(E) of the Federal Deposit Insurance Act, 12 USC 1817(b)(3)(E), available at https://www.fdic.gov/regulations/laws/rules/1000-800.html#fdic1000sec.7b.

[10] 2020 FDIC Restoration Plan, 85 FR 59306 (Sept. 21, 2020), available at https://www.fdic.gov/news/board-matters/2020/2020-09-15-notice-dis-a-fr.pdf.

[11] Section 7(b)(3)(E) of the FDI Act, 12 USC 1817(b)(3)(E).

2023 Regional Bank Receiverships

Since last appearing before the Committee in November 2023, the FDIC, as Receiver, has continued to make progress in managing and selling the assets retained in receiverships of the three regional banks that failed in 2023.[12] The following highlights some significant recent asset transactions.

Silicon Valley Bank

On January 11, 2024, the FDIC, as Receiver, successfully completed a structured sale of a $36 billion purchase money note issued to the receivership by the acquiring institution, as well as a structured sale of approximately $12.4 billion of Ginnie Mae Project Loan Securities to the Federal Financing Bank (FFB), a government corporation under the general supervision and direction of the Secretary of the Treasury. These transactions generated approximately $42 billion in net proceeds, which were paid to the DIF, the most senior claimant in the receivership. In brief, the FDIC, as Receiver, retained approximately $90 billion of assets and, as of March 31, 2024, has disposed of approximately $85 billion of assets.

Signature Bank

In December 2023, the FDIC, as Receiver, completed the disposition of approximately $33 billion in commercial real estate (CRE) loans from Signature Bank. This portfolio represents substantially all remaining loans retained in the Signature receivership, which totaled approximately $60 billion at the time Signature failed. The majority of the $33 billion in the

[12] On March 20, 2023, the FDIC entered into a purchase and assumption agreement for substantially all deposits and certain loan portfolios of Signature Bridge Bank, National Association, by Flagstar Bank, National Association, Hicksville, NY, a wholly owned subsidiary of New York Community Bancorp, Inc., Westbury, NY. On March 26, 2023, the FDIC entered into a purchase and assumption agreement for all deposits and loans of Silicon Valley Bridge Bank, National Association, by First–Citizens Bank & Trust Company, Raleigh, NC . On May 1, 2023, the FDIC entered into a purchase and assumption agreement with JPMorgan Chase Bank National Association, Columbus, OH, to assume all the deposits and substantially all the assets of First Republic Bank, San Francisco, CA.

CRE loan portfolio is comprised of multifamily properties, primarily located in New York City. A large portion (approximately $15 billion) of the CRE loans are secured by multifamily residences that are rent controlled or rent stabilized (RCRS).

To complete the disposition, the FDIC, as Receiver, conveyed the majority of Signature Bank's CRE loans to joint ventures, three of which included the RCRS loans. The joint venture structure allows the FDIC, as Receiver, to retain a majority ownership interest in the future cash flows of loans contributed to the joint venture. A portion of the equity in each joint venture (between 5 and 20 percent) was widely marketed to banks and non-bank financial institutions through the FDIC's financial advisor, Newmark & Company Real Estate Inc. The winning bidders for each joint venture are responsible for the management, servicing and disposition of loans in the joint venture.

The FDIC, as Receiver, disposed of Signature Bank's CRE portfolio in accordance with its statutory obligations required in the disposition of receivership assets, including the obligations to maximize the net present value return from the sale or disposition of such assets; and, in the case of the RCRS joint ventures, to maximize the preservation of the availability and affordability of residential real property for low-and moderate-income individuals.[13] The winning bidder for the RCRS joint ventures is obligated to facilitate the financial and physical preservation of the underlying collateral, subject to comprehensive monitoring by the FDIC, as Receiver.

In brief, the FDIC, as Receiver, retained approximately $87 billion of assets and, as of March 31, 2024, has disposed of approximately $58 billion of assets.

[13] See, 12 U.S.C. § 1811(d)(13)(E).

Resolutions under Title II of the Dodd-Frank Act

The ability of the FDIC and other regulatory authorities to manage the orderly resolution of large complex financial institutions remains foundational to the stability of the U.S. financial system. While recognizing the progress that has been made toward enabling such a resolution and ending "too big to fail," the FDIC also recognizes that the resolution of a GSIB has not yet been undertaken. When it becomes necessary to do so, carrying out such a resolution will come with a unique set of challenges and risks. However, an orderly resolution is far more preferable to the alternatives, particularly the alternative of resorting to public support to prop-up a failed institution or to bail-out investors and creditors. Last month, the FDIC released a paper entitled, "Overview of Resolution Under Title II of the Dodd-Frank Act,"[14] which reaffirms that, should the need arise, the FDIC is prepared to apply the resolution framework that it has worked so hard to develop in cooperation with other domestic and global regulatory authorities. Setting out clear expectations regarding how the FDIC will handle its role in managing failures of systemically important financial institutions is itself a key component supporting the execution of an orderly resolution. The FDIC stands ready to engage with all interested parties to address questions and build further understanding of the FDIC's plans and preparedness for executing our Title II Dodd-Frank Act resolution responsibilities for GSIBs.

Efforts to Strengthen the Regulation and Supervision of Banks

Improving the Management of Liquidity and Funding Risks by Banks

Since the regional bank failures in the spring of 2023, the FDIC has focused on several initiatives to improve liquidity and funding risk management at insured financial institutions.

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[14] See, *Overview of Resolution Under Title II of the Dodd-Frank Act* (April 2024); available at https://www.fdic.gov/sites/default/files/2024-04/spapr1024b_0.pdf.

The agency continues to emphasize the importance of sound liquidity risk management practices and robust contingency funding planning for institutions to manage through liquidity stress. Institutions are expected to assess the stability of their funding and maintain a broad range of funding sources that can be accessed during adverse conditions. Contingency funding plans should consider a range of stress scenarios. The FDIC encourages institutions to incorporate the Federal Reserve's discount window as part of their contingency funding arrangements. Effective contingency funding planning encompasses the development of operational capability to use secondary sources, including the discount window, testing these arrangements regularly, and ensuring that collateral is available. Finally, institutions should revise their contingency plans periodically and more frequently as conditions and strategic initiatives change. To underscore and reemphasize these points, the FDIC issued an update to the *Interagency Policy Statement on Funding and Liquidity Risk Management* in July 2023.[15]

Additionally, the FDIC continues efforts to improve the supervision of interest rate and liquidity risk management, asset growth, and reliance on uninsured and less stable deposits. While the FDIC has regularly monitored uninsured deposit trends across the banking industry, the 2023 bank failures highlight the potential vulnerabilities posed by elevated reliance on uninsured deposits. Across the large regional banks, the FDIC relies on a combination of off-site monitoring and on-site supervisory activities to monitor uninsured deposit concentrations. Since the 2023 bank failures, the FDIC has continued to expand our suite of tools using regulatory reporting data to assess deposit trends across individual banks, develop views of risk posed by uninsured deposits to individual banks, and prioritize supervisory activities. The FDIC has

[15] See *Updated Guidance: Interagency Policy Statement on Funding and Liquidity Risk Management on the Importance of Contingency Funding Plans* (July 28, 2023) available at https://www.fdic.gov/news/financial-institution-letters/2023/fil23039.html.

observed many large regional banks reassessing uninsured deposit outflow assumptions used in internal liquidity stress testing informed by the outflow experiences of the bank failures in 2023. Other observations include the establishment by large regional banks of more granular depositor concentration monitoring and efforts to evaluate the impact of social media and new technologies on deposit stability.

Examiner guidance has been updated to be more explicit about analyses of uninsured deposit concentrations and reemphasize to examiners the importance of forward-looking indicators of risk, such as high growth rates and breaches of internal risk limits. The agency also provided examiner training and guidance on interest rate risk and liquidity risk management, including information on discount window operations.[16] The FDIC continues to coordinate with the federal banking agencies and other financial regulators on liquidity and interest rate risk supervision, training, and policy responses to the stress encountered in the spring of last year.

Strengthening Corporate Governance

The financial crisis of 2008 and the 2023 regional bank failures have taught us that, among other things, IDIs with poor corporate governance and risk management practices are more likely to fail. Reports examining the underlying causes of the 2023 failures noted that poor corporate governance and risk management practices were contributing factors.[17] It is important

[16] See *FDIC's Supervision of Signature Bank* (April 28, 2023) available at: https://www.fdic.gov/news/press-releases/2023/pr23033a.pdf and *FDIC's Supervision of First Republic Bank* (September 8, 2023) available at https://www.fdic.gov/news/press-releases/2023/pr23073a.pdf

[17] The FDIC report on the failure of Signature Bank in 2023 found that the root cause of the failure was poor management without adequate risk management practices and controls. The institution's management did not prioritize good corporate governance practices (*FDIC's* Supervision of Signature Bank, April 28, 2023, p. 2; available at: https://www.fdic.gov/sites/default/files/2024-03/pr23033a.pdf.) The Board of Governors of Federal Reserve System's report on the failure of Silicon Valley Bank also identified governance and risk management deficiencies that led to the failure. (*Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank*, April 2023, p. 1; available at: https://www.federalreserve.gov/publications/review-of-the-federal-reserves-supervision-and-regulation-of-silicon-valley-bank.htm.) Similar findings are contained in the Office of the Inspector General, Board of Governors of the Federal Reserve System, Consumer Financial Protection Bureau's September 25, 2023 *Material Loss Review of Silicon Valley Bank*; available at: https://oig.federalreserve.gov/reports/board-material-loss-review-silicon-valley-bank-sep2023.htm.

to note that the failure of an IDI usually imposes costs on the DIF and negatively affects its customers, employees, shareholders and the public as a whole.

In October 2023, the FDIC published a Notice of Proposed Rulemaking to add a new Appendix C to the FDIC's safety and soundness regulation, 12 CFR 364 (Corporate Governance NPR),[18] to incorporate guidelines on corporate governance and risk management for FDIC-supervised IDIs with consolidated assets of $10 billion or more.[19] The FDIC accepted public comments through February 9, 2024 and is currently reviewing the comments received.

An effective governance framework is necessary for an IDI to remain profitable, competitive, and resilient through changing economic and market conditions. The FDIC's current safety and soundness standards for FDIC-supervised IDIs, as set forth in Appendix A of the safety and soundness regulation and supervisory guidance on corporate governance and risk management, provide baseline corporate governance and risk management expectations for IDIs of all sizes.

However, the FDIC believes larger, more complex IDIs require more sophisticated and formal corporate governance and risk management structures and practices. The proposed guidelines would clarify the FDIC's longstanding expectation that corporate governance and risk management frameworks need to evolve along with the growth, complexity and changing business models and risk profiles of larger IDIs.

In drafting the Corporate Governance NPR, staff studied both the OCC's and the Federal Reserve Board's rules and guidance, and these Proposed Guidelines are intended to be generally consistent with the goals communicated through the Office of the Comptroller of the Currency's

[18] 88 F.R. 70391 (October 11, 2023).

[19] The NPR was issued under the safety and soundness authority provided by Section 39 of the Federal Deposit Insurance Act, which authorizes the FDIC to take formal action if an institution fails to submit and implement, upon FDIC request, an acceptable plan to achieve compliance with safety and soundness standards.

(OCC)[20] and Federal Reserve Board's[21] published issuances in an effort to harmonize corporate governance and risk management requirements for covered institutions that present a higher risk profile with those applicable to entities supervised by the other Federal banking agencies. A notable difference is in the application of the requirements to IDIs over of $10 billion where the other agencies' apply requirements to entities over $50 billion. While the FDIC has long expected that larger banks do need more sophisticated risk management and governance systems and should not wait to develop them, the FDIC is aware and will consider commenters' thoughtful views on this important topic and others before finalizing the guidelines.

The experience of the three large IDI failures last spring demonstrate the need for meaningful action to improve the corporate governance and risk management processes of large IDIs. The governance and risk management standards put forward in this Corporate Governance NPR would be a significant step in that direction.

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[20] See OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches; Integration of Regulations, 79 FR 54518 (Sept. 11, 2014), https:// www.federalregister.gov/documents/2014/09/11/ 2014-21224/occ-guidelines-establishing-heightenedstandards-for-certain-large-insured-national-banksinsured; OCC, Comptroller's Handbook—Corporate and Risk Governance, https://www.occ.gov/ publications-and-resources/publications/ comptrollers-handbook/files/corporate-riskgovernance/index-corporate-and-riskgovernance.html.

[21] See 12 CFR 252.22, subpart C—Risk Committee Requirements for Bank Holding Companies with Total Consolidated Assets of $50 Billion or More and Less Than $100 Billion. The Federal Reserve Board initially set the application of risk committee requirements under Regulation YY, among other requirements, for banks with total consolidated assets of $10 billion or more pursuant to Section 165 of the Dodd-Frank Act of 2010. 79 FR 17239, 17248 (Mar. 27, 2014). This threshold was raised from $10 billion to $50 billion pursuant to changes made under the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018. 84 FR 59032, 59055 (Nov. 1, 2019). 9See SR 16–11: Supervisory Guidance for Assessing Risk Management at Supervised Institutions with Total Consolidated Assets Less than $100 Billion (June 8, 2016; revised and reposted February 17, 2021, p. 3). SR letter 95-51, Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies (Nov. 14, 1995; revised Feb. 26, 2021) remains applicable to state member banks and bank holding companies with $100 billion or more in total assets.

Basel III Proposal

On September 18, 2023, the FDIC, the OCC and the Federal Reserve published a Notice of Proposed Rulemaking (Basel III NPR) that would revise and strengthen the capital requirements applicable to the largest banking organizations.[22]

The Basel III NPR is a continuation of the federal banking agencies' efforts to revise the regulatory capital framework for our nation's largest financial institutions, which were found to be undercapitalized and over-leveraged during the global financial crisis of 2008. Following the 2008 crisis, the federal banking agencies strengthened the banking system through an initial set of revisions to the capital framework.[23] Those revisions raised the quality and quantity of risk–based capital and included the introduction of an enhanced supplementary leverage ratio for our largest, most systemic banking organizations. However, there remained areas of the regulatory capital framework that need improvement.

The Basel III NPR would make important changes to address the capital weaknesses identified in the 2008 financial crisis, enhance the resilience and stability of the banking system, and enable the banking system to better serve the U.S. economy. For example, the proposal would address critical areas of the risk–based capital framework related to credit risk, operational risk, market risk, and financial derivative risk. Taken together, these changes would bolster the financial resilience of our nations' largest banking organizations.

The agencies extended the comment period until January 16, 2024 to allow interested parties additional time to analyze the issues and prepare their comments.[24] The agencies have

[22] 88 F.R. 64018 (September 18, 2023).
[23] See, for example, *Regulatory Capital Rules, etc.*, 78 F.R. 55340 (September 10, 2013).
[24] 88 F.R. 73770 (October 27, 2023).

received over 400 unique comments. The comments have been very helpful in identifying areas of the proposal that may warrant changes in a final rule. For example, concerns have been raised related to the proposed treatment for residential mortgage exposures, certain tax credit equity investments, trading activities, and banking activities that generate large amounts of fee-based revenue. The FDIC continues to consider the comments and engage with our fellow regulators in developing a final rule.

Long-Term Debt and Resolution Planning Proposals

The FDIC, together with the Federal Reserve and the OCC, issued a Notice of Proposed Rulemaking on September 19, 2023, entitled *Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions*. (LTD Proposal).[25] The proposed long-term debt requirement could mitigate resolution challenges encountered in the failure of large regional banks and bolster financial stability. Long-term debt would absorb losses before the depositor class – uninsured depositors and the FDIC – take losses. This would decrease the incentive for uninsured depositors to run. Long-term debt would protect the DIF, helping to make large regional bank resolutions more orderly, and creating additional options for the FDIC in resolution. Long-term debt would make it more likely that a resolution transaction could satisfy the statutory least-cost requirement without the need for a systemic risk exception, whether by a closing weekend sale or the use of a bridge depository institution.

[25] 88 F.R. 64524 (September 19, 2023).

The LTD Proposal's comment period was extended to January 16, 2024.[26] The agencies received 48 comments on the LTD Proposal, which FDIC staff is considering as we work with our colleagues at the Federal Reserve and OCC to finalize this proposal.

In addition to comments received on the LTD proposal, the FDIC is carefully considering comments related to proposed changes to IDI resolution plans,[27] and with the Federal Reserve, the FDIC is carefully considering comments related to proposed guidance for certain firms that submit Title I resolution plans.[28]

Other Regulatory Initiatives

Reviewing the Bank Merger Process

On March 21, 2024, the FDIC Board approved a revised Statement of Policy on Bank Merger Transactions (Proposed Statement of Policy) for publication in the Federal Register for a 60-day comment period.[29] [30] The Proposed Statement of Policy would update, strengthen, and clarify the FDIC's policies related to the evaluation of bank merger applications subject to FDIC approval under the Bank Merger Act (BMA).[31] The Proposed Statement of Policy reflects legislative and other developments that have occurred since the last amendment in 2008, including the establishment of the statutory factor regarding the risk to the stability of the United

[26] 88 F.R. 83364 (November 29, 2023).
[27] *Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets,* 88 FR 64579 (September 19, 2023).
[28] *Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers,* 88 F.R. 64626 (September 19, 2023); and "*Guidance for Resolution Plan Submissions of Foreign Triennial Full Filers,*" 88 F.R. 64641 (September 18, 2023).
[29] FDIC Press Release *FDIC Seeks Public Comment on Proposed Revisions to its Statement of Policy on Bank Merger Transactions* (March 21, 2024); available at: https://www.fdic.gov/news/press-releases/2024/pr24017.html.
[30] In a separate Federal Register notice, the FDIC, as part of its obligations under the Paperwork Reduction Act of 1995, invited comment on the renewal of the existing information collection found in the FDIC Supplement to the Interagency Bank Merger Act application form. 89 F.R. 17848 (March 12, 2024).
[31] Section 18(c) of the FDIC Act, 12 U.S.C. § 1828(c).

States banking or financial system. The Proposed Statement of Policy is more principles based; addresses each statutory factor separately; and highlights other relevant matters and considerations, such as related statutes pertaining to interstate mergers, and applications from non-banks or banks that are not traditional community banks.

The Proposed Statement of Policy reflects consideration of comments received in response to the FDIC's 2022 *Request for Information and Comment on Rules, Regulations, Guidance, and Statements of Policy Regarding Bank Merger Transactions* (2022 RFI).[32] The 2022 RFI solicited comments regarding the effectiveness of the existing framework of the laws, practices, rules, regulations, guidance, and statements of policy in meeting the statutory requirements of the BMA.

Rulemaking Implementing Section 956 of Dodd-Frank – Preventing Misaligned Incentive-Based Compensation

Section 956 of the Dodd-Frank Act[33] addresses an important lesson from the financial crisis of 2008: poorly designed financial institution compensation programs can provide incentives for short-term risk taking that can jeopardize the safety and soundness of the institution. Misaligned incentive-based compensation for executives continues to play a role in the failure of banks. Material Loss Reviews of the 2023 regional bank failures identified common weaknesses that included an excessive focus on growth and short-term profitability, and a lack of risk metrics in compensation policies and practices that may have encouraged excessive risk taking.[34]

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[32] See, 87 F.R. 18740 (March 31, 2022).
[33] Pub. L. No. 111-203, 124 Stat. 1376 (2010).
[34] See, for example, FDIC Office of Inspector General's *Material Loss Review of Signature Bank of New York* (October 23, 2023), available at https://www.fdicoig.gov/sites/default/files/reports/2023-10/EVAL-24-02.pdf.

This month, the FDIC took steps to initiate a joint rulemaking implementing Section 956 by approving for publication a notice of proposed rulemaking (Section 956 NPR), as required by statute.[35] Implementation of the section will provide a critical tool to control excessive risk taking by financial institution executives by aligning their compensation with the long-term safety and soundness of their institutions rather than short-term profits.

The Section 956 NPR re-proposes the rule text previously proposed in June 2016,[36] along with proposed alternatives and questions in the preamble. The proposal uses a tiered approach corresponding to the size of the institution.[37] One of the key provisions applicable to larger covered institutions would require deferral of a certain minimum amount of compensation of senior executive officers and other employees who can expose the institution to material levels of risk, known as significant risk-takers. The proposal would also require those deferred amounts to be considered for forfeiture and downward adjustment and clawback, in the event of undue risk taking. Deferral provides an important mechanism to discourage inappropriate risk-taking by allowing time to pass to evaluate the outcomes of risk-taking behavior and to adjust incentive-based compensation accordingly. The FDIC looks forward to reviewing and considering public comments on the Section 956 NPR.

Implementing the CRA Final Rule

On October 24, 2023, the FDIC, together with the Federal Reserve and the OCC, finalized the first comprehensive rewrite of the Community Reinvestment Act (CRA)

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[35] Section 956 of the Dodd-Frank Act requires the FDIC, OCC, Federal Reserve, National Credit Union Administration, Securities Exchange Commission and Federal Housing Finance Agency to jointly issue regulations or guidelines to implement the provision. Once all six agencies have approved the Section 956 NPR, it will be published in the Federal Register with a comment period of 60 days following publication.
[36] 81 F.R. 37670 (June 10, 2016).
[37] "Covered financial institutions" are financial institutions with at least $1 billion in assets. Section 956(e) of the Dodd-Frank Act.

Regulations in 25 years. The CRA, since its enactment in 1977, has been the foundation of access to credit, investment, and basic banking services on a responsible basis for low- and moderate-income communities and communities of color in the United States. The new CRA rule issued by the federal banking agencies adapts CRA to the changing nature of the banking business and strengthens its provisions to carry out its critically important public purpose. The FDIC is firmly committed to the support of the rule and believe it is entirely consistent with the statute.

Protecting Consumers from Misrepresentations about Deposit Insurance

To protect consumers from misrepresentations by some crypto companies regarding FDIC insurance, in 2022, the FDIC issued an advisory to FDIC-insured institutions and published consumer educational materials on deposit insurance.[38] In December 2023, the FDIC updated its regulation entitled, *Advertisement of Membership, False Advertising, Misrepresentation of Insured Status, and Misuse of the FDIC's Name or Logo*.[39] The regulation requires the use of signs that differentiate insured deposits from non-deposit products and that disclose that "non- deposit products" are not insured by the FDIC, are not deposits, and may lose value. Among other changes, the amended regulation now includes crypto assets in the regulatory definition of "non-deposit product."

In connection with crypto-related activities, in 2023 and 2024, the FDIC issued a number of direct letters demanding persons or entities cease and desist from making false or misleading

[38] See, *Advisory to FDIC-Insured Institutions Regarding Deposit Insurance and Dealings with Crypto Companies, FIL-35-2022;* available at: https://www.fdic.gov/news/financial-institution-letters/2022/fil22035.html; and *Fact Sheet: What the Public Needs to Know About FDIC Deposit Insurance and Crypto Companies*; available at https://www.fdic.gov/news/fact-sheets/crypto-fact-sheet-7-28-22.html.

[39] 12 C.F.R. 328 Advertisement of Membership, False Advertising, Misrepresentation of Insured Status, and Misuse of the FDIC's Name or Logo.

representations about the existence of deposit insurance, misusing the name or logo of the FDIC, or knowingly misrepresenting the extent and manner of deposit insurance.[40]

Eliminating Unnecessary Regulatory Burden – the EGRPRA Process

The FDIC remains keenly aware of the regulatory burden that community banks currently face. In its assessment of regulatory burden in the current environment, the FDIC is cognizant of the importance of balancing safety and soundness and consumer protection regulation with the legitimate business interest of the banks. The FDIC, together with the OCC and the Federal Reserve, initiated the third decennial review under the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA)[41] that requires the agencies to review their regulations to identify those that are outdated, unnecessary, or unduly burdensome and to eliminate such requirements to the extent appropriate.

To facilitate this review, the agencies divided their regulations into 12 categories. On February 6, 2024, the agencies published a solicitation for comment on three categories of regulations: *Applications and Reporting, Powers and Activities, and International Operations*,[42] asking the public to identify regulations they believe are outdated, unnecessary, or unduly burdensome. The comment period remained open for 90 days and closed on May 6, 2024. Over the next two years, the agencies will request comment on the regulations in the remaining categories. In addition, the agencies also plan to hold outreach meetings where interested parties may comment on applicable regulatory requirements directly to the agencies.

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[40] See, for example, *FDIC's Letter to Organo Payments, Inc.* (January 19, 2024): https://www.fdic.gov/resources/regulations/laws/section-18a4-of-fdi-act/letters/2024-01-19-ogpay.pdf; and *FDIC's Letter to Horizon Globex GmbH* (January 19, 2024): https://www.fdic.gov/resources/regulations/laws/section-18a4-of-fdi-act/letters/2024-01-19-upstream.pdf.

[41] 12 U.S.C. § 3311.

[42] 89 F.R. 8084 (February 6, 2024).

At the conclusion of the review, the agencies will publish in the *Federal Register* a summary of the comments received, identifying and discussing the significant issues raised; and submit a report to Congress shortly thereafter. The report will address any significant issues raised by the public, the relative merits of such issues, and whether the agencies have the ability to address regulatory burden through regulation, or whether such burdens must be addressed by legislative action. The FDIC stands ready to address the issues raised during this process in a manner consistent with bank safety and soundness, the protection of consumers and financial stability.

Enhancing Examiner Resources

In the FDIC Chief Risk Officer's report on the FDIC's supervision of Signature Bank, the Chief Risk Officer identified examiner resources as one of the challenges affecting the timeliness and quality of examinations of Signature Bank. Since the issuance of the Chief Risk Officer Report, to insure adequate examination resources going forward, the FDIC has taken a number of actions. To enhance the attractiveness of dedicated examiner positions, the FDIC elevated several positions and instituted incentive payments for certain key staff. To address the high cost of living in San Francisco, New York, Seattle, and Los Angeles, the FDIC is offering a payment supplement in those areas. Additionally, to address higher attrition rates among pre-commissioned examiners in 2021 and 2022, the FDIC increased the commissioning payment in return for a two-year service commitment. Finally, the FDIC is making use of retention payments to retain its retirement-eligible examiner cadre while staffing is bolstered.

These steps are showing positive results, with reduced attrition among pre-commissioned examiners in 2023. The FDIC has also continued to see strong interest among candidates for

entry level positions with two of the largest groups of qualified applicants received in the last six months. The FDIC continues to bring in a substantial class of examiner candidates each year.

Conclusion

I appreciate the opportunity to appear before you today to report on our efforts to address the workplace culture of the FDIC, create a workplace where every FDIC employees feels safe, valued and respected, and fulfill the FDIC's core mission to maintain stability and public confidence in the U.S. financial system through its responsibilities for deposit insurance, banking supervision, and the orderly resolution of failed banks.

I look forward to answering your questions.

Chairman MCHENRY. Mr. Hsu, you are recognized for 5 minutes.

STATEMENT OF HON. MICHAEL HSU, ACTING COMPTROLLER, OFFICE OF THE COMPTROLLER OF THE CURRENCY

Mr. HSU. Thank you, Mr. Chairman. Chairman McHenry, Ranking Member Waters, and members of the committee, I am pleased to appear today to provide an update on the activities and priorities of the OCC.

The overall condition of the Federal banking system is sound. OCC-supervised banks in aggregate continue to have strong levels of regulatory capital and sufficient liquidity buffers, though risks from commercial real estate and interest rate exposure continue to warrant attention. Banks and supervisors need to remain on guard against complacency, one of my top priorities for the Agency.

The OCC's bank supervision operating plan for 2024 highlights asset liability management, credit risk and allowance for credit losses, cybersecurity, operational risk, and consumer compliance risk as our key areas of focus. Another priority for the OCC has been promoting fairness in banking. This April marks the 1-year anniversary of OCC guidance to assist banks in managing risks associated with overdraft protection programs. Since the OCC's heightened attention on overdrafts began, the overdraft fees charged by OCC regulated banks in aggregate have fallen over 40 percent.

Adapting to digitalization has been a third priority for the Agency. We recognize, for instance, that community banks may face hurdles and risk managing their third-party relationships, including with financial technologies (fintechs). Earlier this month, the OCC, Federal Reserve, and FDIC published a third-party risk management guide for community banks with examples of innovative approaches to conducting due diligence and assessing new fintech relationships.

The OCC supports a diverse and dynamic banking system and continues its focus on updating our bank merger analytical frameworks. We remain committed to working with our interagency peers, including the Department of Justice, on this effort. To increase transparency, on January 29, we released for comment a proposed policy statement on bank mergers. We recently extended the comment period to June 15. My written testimony provides greater detail on these and other activities of the OCC.

As co-chair of the FDIC's Special Review Committee, I would like to address briefly the recently released independent report on harassment and misconduct at the FDIC. The top priority for us all must be protecting the staff of the FDIC and putting people first. The harassment and misconduct detailed in the report are totally unacceptable. The number and scope of allegations, the patterns of misconduct in the longstanding culture revealed by the review are highly disturbing and need to be fixed.

The root causes and recommendations cited in the report provide a clear roadmap for what needs to be done and why. That is where our attention must be focused to ensure the FDIC is a safe workplace for all of its employees. As a member of the FDIC board, I am committed to the transformation called for in the report. I am especially supportive of the report's recommendation to engage an

external expert and establish an independent monitor to ensure that the Agency's efforts are tracked, that accountability is enforced. I also believe that Chairman Gruenberg has accepted responsibility for his and the FDIC's past failings and that he is fully committed to lead the Agency and taking the actions necessary to make it a safe place for everyone to work.

Thank you. I will be happy to answer any questions.

[Prepared statement of Mr. Hsu follows:]

For Release Upon Delivery
10:00 a.m. May 15, 2024

Statement of Michael J. Hsu

Acting Comptroller of the Currency

Before the

Committee on Financial Services

United States House of Representatives

May 15, 2024

Statement Required by 12 U.S.C. § 250:
The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily present the views of the President.

Introduction

I am pleased to testify before the Committee on Financial Services to provide an update on the activities underway at the Office of the Comptroller of the Currency (OCC) to ensure that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations.

The OCC charters, supervises, and regulates more than 1,000 national banks, federal savings associations and federal branches and agencies of foreign banks (collectively "banks"). These institutions range in size from very small community banks to the largest, most globally active banks operating in the United States. The vast majority of these institutions have less than $1 billion in assets, while 55 have greater than $10 billion in assets. Together, OCC-supervised financial institutions hold more than $15 trillion in assets, representing nearly 65 percent of all the assets held in commercial U.S. banks.

My written statement provides an overview of the state of the federal banking system, an update on the OCC's work to advance the four critical agency priorities that I set forth after becoming Acting Comptroller, and a description of recent key regulatory developments.

State of the Federal Banking system

The overall condition of the federal banking system is sound. OCC-supervised banks in aggregate continue to have strong levels of regulatory capital and sufficient liquidity buffers, though risks from commercial real estate (CRE) and interest rate exposure warrant attention.

The OCC closely monitors the financial condition of the institutions it supervises and engages directly with them to ensure they are appropriately managing their risks. The OCC's Semiannual Risk Perspective[1] highlights the critical elements of credit, market, operational, and compliance risks that banks are expected to manage. The OCC's Bank Supervision Operating Plan for 2024[2] identifies the agency's current examination

[1] *See* OCC Semiannual Risk Perspective (Fall 2023).
[2] *See* Fiscal Year 2024 Bank Supervision Operating Plan, Office of the Comptroller of the Currency, Committee on Bank Supervision (occ.gov).

priorities and highlights asset liability management, credit risk and allowance for credit losses, cybersecurity, operational risk, and consumer compliance risk, among others, as key areas of focus.

Update on Agency Priorities

Guarding Against Complacency

It is critical to build and maintain trust in the federal banking system that national banks and federal savings associations guard against complacency. As noted above, key areas banks are expected to manage include capital and liquidity levels and commercial real estate exposures. In recent months, regional and community banks have been particularly vulnerable to risks associated with CRE concentrations and exposures. At the same time, the OCC expects the banks we supervise to remain vigilant and focused on risk management. Banks need to successfully manage traditional risks, such as credit, liquidity, and interest rate risks, as well as prepare for emerging risks and tail risk events.

Another critical area for banks to address is operational resilience, which ensures that banks can adapt to and withstand or recover from disruptions. Both the number of potential disruptions and their possible impact are increasing, and may result from external events like natural disasters, malicious actors, pandemics, or global conflicts, or from weak internal systems, controls, or risk management. These disruptions may impede services, like payments, clearing, and settlement, or adversely impact systems or corrupt data. Ensuring that critical operations and banking services can withstand or recover from disruptive events requires planning, prudent investment, well designed systems, and regular testing. To this end, the federal banking agencies have been engaged in discussions to consider potential changes to the operational resilience framework.

Promoting Fairness

Ensuring fairness and addressing discrimination in the federal banking system is an important OCC objective, part of our mission, and critical to safeguarding trust in banks. We remain committed to using all our tools to ensure the institutions we supervise are aware of and comply with their obligations to operate safely, soundly, and fairly.

This April marked the one-year anniversary of OCC guidance to assist banks in

managing the various risks associated with overdraft protection programs.[3] The guidance identified two practices— authorize positive, settle negative and representment—that can result in heightened risk exposure. It also highlighted sound risk management and pro-consumer practices that banks can employ to strengthen their overdraft protection programs. Since the beginning of the OCC's heightened attention on overdrafts, the overdraft fees charged by OCC-regulated banks in aggregate have fallen over 40%, from $6.5 billion in 2021 to $4 billion in 2023.[4] Current supervisory data continue to show declines in overdraft fees quarter over quarter.[5] Among large banks, many have reduced fees and adopted pro-consumer features, such as grace periods.

Importantly, all OCC-supervised large banks have stopped assessing authorize positive, settle negative fees or insufficient funds fees and most have discontinued collecting sustained overdraft fees. OCC-regulated midsize and community banks have made or are in the process of making various pro-consumer changes to their overdraft protection programs. For example, most have eliminated representment fees or started offering de minimis grace amounts or grace periods. This includes those community banks that derive an outsized amount of revenue from overdrafts. Progress with regard to representment has been more challenging due to the critical role played by the core processors. We understand the largest core processors are taking steps that will allow banks to identify and address representment practices. As those plans develop, we will continue to encourage banks and the core processors to take steps to protect and empower consumers.

I also want to recognize the continued progress of the OCC's Project REACh – or Roundtable for Economic Access and Change – which is focused on removing barriers to financial inclusion. Initiatives targeting credit invisibles have resulted in more than 100,000 new entrants into the mainstream financial system who now have credit scores

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[3] *See* OCC Bulletin 2023-12, "Overdraft Protection Programs: Risk Management Practices," April 26, 2023.

[4] Call report data are available on the Federal Financial Institutions Examination Council (FFIEC) Central Data Repository's Public Data Distribution site. Call report data exclude overdraft-related service charges generated by banks with assets of $1 billion or less as of the reporting quarter, which are not required to report overdraft-related service charges as a separate line item in their call report data. The data also exclude overdraft-related service charges generated by all credit unions.

[5] Banks under $1 billion in assets do not report overdraft fee income on the call report, so the data presented do not include those banks.

and access to credit. Investments of more than $500 million in Minority Depository Institutions (MDIs) have resulted in increased partnerships, exchange programs, training and capital. On May 29-30, 2024, the OCC will host the Project REACh Financial Inclusion Summit at our headquarters in Washington, D.C. to discuss progress made on several workstreams, as well as to launch new initiatives to increase economic mobility within financially underserved and under-resourced communities.

In February, the Federal Financial Institutions Examination Council (FFIEC) released a statement on "Examination Principles Related to Valuation Discrimination and Bias in Residential Lending,"[6] which provides principles for the examination of institutions' residential property appraisal and evaluation practices to mitigate risks that may arise due to potential discrimination or bias in those practices and to promote credible valuations. The OCC will consider these principles in the context of consumer compliance and safety and soundness examinations when assessing banks' residential real estate valuation programs.

Adapting to Digitalization

Banks' relationships with third parties, including financial technology (fintech) companies, continue to expand. The use of third parties has significant potential benefits, but poor third-party risk management can hurt consumers, weaken banks, and contribute to an unlevel playing field.

Last year, the OCC and other regulators jointly issued "Interagency Guidance on Third-Party Relationships: Risk Management,"[7] to remind banks of their responsibility to operate in a safe and sound manner and in compliance with applicable laws and regulations regardless of whether their activities are performed in-house or outsourced. The guidance also recognizes that not all third-party relationships reflect the same level of risk and thus do not require the same level of risk management.

Effective risk management of third-party relationships is challenging for financial institutions of all sizes, but we recognize that community banks, including MDIs and Community Development Financial Institutions Funds (CDFIs), may need to navigate

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[6] *See*: FFIEC News Release "FFIEC Issues Statement on Examination Principles Related to Valuation Discrimination and Bias in Residential Lending."
[7] *See* OCC News Release 2023-53, "Agencies Issue Final Guidance on Third-Party Risk Management."

additional hurdles. Last month, the OCC, Board of Governors of the Federal Reserve System (Federal Reserve), and the Federal Deposit Insurance Corporation (FDIC) sought to address this by publishing "Third-Party Relationships Risk Management: A Guide for Community Banks."[8] This guide provided community banks with examples of innovative approaches to conducting due diligence and assessing new fintech companies.

The OCC expects banks to approach and manage the use of artificial intelligence (AI) consistent with principles of safety, soundness, and fairness. To date, banks have generally approached machine learning prudently across a range of use cases, though we are starting to see a notable increase in the number of generative AI pilots at some of the larger banks we supervise. AI has the potential to enable improvements across a range of domains, but it also has the potential to perpetuate and exacerbate the biases, discrimination, and unfairness that are embedded in the data feeding AI systems. To guard against this, banks need to have appropriate oversight and governance of the models they use. In addition, banks must be attentive to the risk of AI-enabled fraud.

The OCC also has focused on exploring the tokenization of real-world assets and liabilities. In contrast to crypto, tokenization is driven by solving real-world settlement problems and can be developed in a safe, sound, fair, and compliant manner. Earlier this year, the OCC hosted a public symposium on tokenization to discuss developments, explore legal and risk management foundations, and promote public debate. The symposium sparked robust discussion on these issues and highlighted the innovative potential of tokenization.

Managing Climate-Related Financial Risks

Consistent with the OCC's safety and soundness mandate, the agency has continued to be engaged with the large banks it supervises to better understand their climate-related financial risk management capabilities and their efforts to identify, manage and control these risks. In 2023, the OCC initiated discussions with banks with over $100 billion in total assets to understand their climate-related financial risk management programs.

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[8] *See* OCC News Release 2024-46, "Agencies Issue Guide to Assist Community Banks to Develop and Implement Third-Party Risk Management Practices."

In general, the OCC has observed that large banks have been making progress to incorporate climate-related financial risks into their risk management frameworks and policies. In light of the withdrawal of insurers from higher-risk markets and rising insurance costs, we have recently observed that large banks are considering the impacts of changes in insured limits or deductibles, premium increases, and lack of insurance coverage in credit risk assessments for commercial and residential real estate portfolios in their risk management work. The OCC is committed to open dialogue and constructive engagement with the large banks it supervises around climate-related financial risk management.

Update on Other Regulatory Initiatives

The OCC has been engaged in developing and finalizing several proposals to promote the resiliency, resolvability, and inclusiveness of the federal banking system.

Revisions to Capital Rules for Large Banks

The OCC remains actively engaged with the Federal Reserve and the FDIC to consider all stakeholder comments received in response to the July 2023 proposal to update the risk-based capital requirements applicable to large banking organizations with significant trading activity. Establishing an appropriate capital framework that adequately captures all of the material risks of these large banks is critically important to the health of the nation's financial system, and the agencies must get it right. The OCC has welcomed the broad range of thoughtful comments received and continues to approach this rulemaking with an open mind.

Community Reinvestment Act Final Rule

Last October, the federal banking agencies issued an interagency final rule implementing the Community Reinvestment Act (CRA), which was enacted in 1977, to prevent redlining and to encourage banks and savings associations to help meet the credit needs of all segments of the communities in which they operate, especially low-and moderate-income (LMI) neighborhoods and individuals.

On February 5, 2024, trade groups filed a lawsuit in federal court against the

OCC, FDIC, and Federal Reserve, seeking to block the implementation of the final rule. On March 29, 2024, the presiding district court judge issued a preliminary injunction that currently prevents the federal banking agencies from enforcing the final rule and extends the effective and applicability dates of the final rule while the injunction is in place. The agencies filed a notice of appeal of this injunction with the US Court of Appeals on April 18, 2024, which is currently pending. At this time, the OCC continues to assess banks' CRA performance under its previous regulatory framework.

Business Combinations Under the Bank Merger Act

The OCC is committed to working with our interagency peers to update our bank merger analytical frameworks, which includes collaboration with the Department of Justice (DOJ) on the competition prong of the Bank Merger Act. This work is ongoing.

In addition, on January 29, 2024, the OCC released a proposal to increase the transparency of the standards that apply to the agency's review of business combinations involving national banks and federal savings associations. The proposal would amend the OCC's procedures and add a policy statement summarizing the principles the OCC uses when it reviews proposed bank merger transactions under the Bank Merger Act.

To provide greater clarity to financial institutions and transparency to the public, the proposed policy statement would outline general principles the agency uses in its review of applications under the Bank Merger Act and the OCC's consideration of the financial stability, financial and managerial resources and future prospects, and convenience and needs factors. The policy statement would also discuss the criteria informing the OCC's decision on whether to hold a public meeting on an application subject to the Bank Merger Act. We recently extended the comment period on the proposal until June 15, 2024, and we encourage all stakeholders to provide comments.

Incentive Compensation

On May 6, the OCC, FDIC and the Federal Housing Finance Agency (FHFA) approved a notice of proposed rulemaking (NPR) to fulfill Congress' mandate through the Dodd Frank Act to address excessive incentive compensation and compensation that could lead to material financial loss. The NPR is based on the proposed rule text issued in

2016, which was supported by six federal agencies, with a new preamble that acknowledges developments and supervisory learnings and is intended to initiate renewed public dialogue on this topic. While the NPR has not been adopted by all six agencies to inform a joint rulemaking as required by statute, we are accepting comments on the proposal and look forward to continuing to engage our interagency peers and the public on how we can most effectively curtail problematic incentive compensation practices.

The OCC Supports Community Banks and Minority Depository Institutions

More than 80 percent of the institutions supervised by the OCC are community banks and federal savings associations. These institutions play a crucial role in providing consumers and small businesses with essential financial services and are a source of credit that is critical to economic growth and job expansion.

We recognize that small institutions face challenges as they work to stay competitive in today's increasingly high-tech financial marketplace. Digitalization has put a premium on online and mobile engagement, customer acquisition, customization, big data, fraud detection, artificial intelligence, machine learning, and cloud management. These activities require expertise and economies of scale that many banks, especially community banks and MDIs, may not have access to. We are also aware of the impact of fraud on community banks and in particular, delays in receiving timely responses to their requests for reimbursements associated with fraudulent returns. The OCC recently initiated a process to receive information from community banks about delays in reimbursements resulting from check fraud so we can determine a supervisory response.

Earlier this year, the OCC, Federal Reserve and FDIC published the first notice requesting comment on specific regulations pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). EGRPRA requires the agencies to review their regulations every 10 years to identify outdated, unnecessary, or unduly burdensome regulations applicable to insured depository institutions. This review will include a series of federal register notices as well as public meetings inviting stakeholder comments for agency consideration. I look forward to a robust EGRPRA process and support a fulsome review of our regulations with the goal of eliminating

unnecessary regulatory burden on community banks.

Conclusion

I am committed to ensuring OCC-supervised banks operate in a safe, sound, and fair manner, meet the credit needs of their communities, treat all customers fairly, and comply with laws and regulations. As we work to ensure that the federal banking system remains a source of strength to the U.S. economy, we will continue to advance key agency priorities to ensure the federal banking system is well positioned to respond to community and consumer needs well into the future.

Chairman MCHENRY. Thank you. I will now recognize myself for 5 minutes.

Vice Chair Barr, if there are significant changes to your capital proposal, will you commit to re-proposing the rule for notice and comment?

Mr. BARR. We have not made a decision on process yet. We are really focused right now on getting the substance right.

Chairman MCHENRY. Do you think there will be an opportunity for noticing comment after whatever the next proposal is?

Mr. BARR. Again, we have not focused yet on the process. We really are still trying to work our way through the substance and make sure we get that right.

Chairman MCHENRY. All right.

Mr. BARR. We have not made any decision yet.

Chairman MCHENRY. We intend for you to comply with the law of the Administrative Procedures Act.

Mr. BARR. Yes, we will.

Chairman MCHENRY. Chairman Gruenberg, let me take you through the timeline of the last 15 months. In March, three major banks failed, including Signature Bank, which is directly supervised by your agency. In April, your own chief risk officer reviewed FDIC's actions leading up to Signature Bank's failure, concluding staffing, whether it be shortages or communication issues, was a major issue. Later in November, revelations about the workplace environment started to appear. When you testified before the committee, the Wall Street Journal had just reported on the toxicity of the FDIC's workplace, describing a culture ripe with harassment and discrimination. Six months later, an independent law firm commissioned by the FDIC released a report not only confirming your inappropriate conduct but confirming the toxicity of FDIC's culture and workplace environment by expanding on the magnitude of both. No need to go into the details of the report at this time, but looking back, I can say with confidence that the FDIC's workplace issues played a role in Signature Bank's failures. Would you?

Mr. GRUENBERG. Thank you, Mr. Chairman. I appreciate the question. As you indicated, our chief risk officer did a review of the failure of Signature——

Chairman MCHENRY. No, I am asking you.

Mr. GRUENBERG. Yes.

Chairman MCHENRY. Do you believe that the workplace issues impacted the Signature Bank failure and the response to it?

Mr. GRUENBERG. I am indicating, Mr. Chairman, that the report did not identify that as an issue.

Chairman MCHENRY. I am asking you, do you think that is the case? You do not need to cover all this stuff to use time.

Mr. GRUENBERG. As far as I am aware, it was not a significant contributing factor, Mr. Chairman.

Chairman MCHENRY. Okay. Let us run through the scenario. This report that you accept, you accept the report from Cleary Gottlieb.

Mr. GRUENBERG. I do.

Chairman MCHENRY. Including the claims of your actions to your direct reports and folks in the Agency.

Mr. GRUENBERG. I do.

Chairman MCHENRY. You accept that?

Mr. GRUENBERG. I do.

Chairman MCHENRY. Okay, so the workplace environment you have, and the report indicates that when presented with bad news, your first reaction is to yell, scream, or berate the person presenting the bad information. Do you think a bank failure is bad information?

Mr. GRUENBERG. It is.

Chairman MCHENRY. Did you remember responding to that bank failure weekend with any level of anger?

Mr. GRUENBERG. No.

Chairman MCHENRY. No anger?

Mr. GRUENBERG. No.

Chairman MCHENRY. Okay, so the report indicates that you are predisposed to pure anger and rage when presented with bad information. Do you accept that as part of the findings of the report?

Mr. GRUENBERG. I do accept the findings of the report, Mr. Chairman.

Chairman MCHENRY. Okay, and so we are to believe that in the weekend where we had three major bank failures, that you were not angry, and you did not get angry when presented with bad information.

Mr. GRUENBERG. I did not, Mr. Chairman.

Chairman MCHENRY. Okay. You have led the Agency for 10 of the last 13 years. We have had significant bank failures. Do you think that the fact that you respond to bad information by attacking or yelling at the person presenting that information makes those people less willing to present bad information to you?

Mr. GRUENBERG. I endeavor to entreat every employee with courtesy and respect.

Chairman MCHENRY. That is not what the report indicates, sir, and that is why I am asking this specific question. If you berate the people you ask the question of——

Mr. GRUENBERG. I think the report indicates that even in circumstances in which I treat employees harshly in a conversation, employees still bring bad news to me.

Chairman MCHENRY. Okay. The report indicates, one senior executive put it, "There is a great reluctance to deliver bad news to Marty Gruenberg," and a number of employees, including senior executives, noted that this reaction could have the effect of chilling open conversations, and that his behavior hampers free flow of communications. You have led the Agency for 10 of the last 13 years. Your behavior is such that you apologize for folks in the Agency experiencing harassment and sexual harassment, but you never have apologized, and your written statements and press reports are here before this committee for your actions in this report. There is no apology for the people that you berated over the last 13 years of the Agency, or actually the last 20 years of the Agency, but you have been leading it for 10 years. Do you apologize to the people that you affected?

Mr. GRUENBERG. I certainly do, Mr. Chairman.

Chairman MCHENRY. You certainly do.

Mr. GRUENBERG. I take responsibility for it.

Chairman MCHENRY. Okay. You take responsibility for it, but you do not apologize?

Mr. GRUENBERG. No, I said I do apologize.

Chairman MCHENRY. Okay. All right. I will recognize the ranking member for 5 minutes.

Ms. WATERS. Chair Gruenberg, at a hearing last November, after the Wall Street Journal articles were published, I asked you to provide an action plan outlining the steps the FDIC plan to take to address workplace issues related to sexual harassment and misconduct, and to ensure that all employees are provided a safe work environment. On December 1st, 2023, you provided that plan, which addressed eight major areas and contained over 30 specific tasks to be completed under those general areas. Approximately half of the tasks were to be completed at this time, and the other half were to be completed before the end of 2024. Which tasks have been completed and what improvements have come from them?

Mr. GRUENBERG. Thank you, Congresswoman. As I indicated, we initiated that plan in the immediate aftermath upon learning about these matters. I directed a third-party review. That review has now been completed. In addition, the action plan had a number of specific action items that we have been in the process of implementing, including increased protection for victims, a hotline, a training program, pulse checks in regard to workplace culture, and a range of other action items that we have been in the process of implementing, and as you indicated, will complete by the end of this year.

In addition, after receiving the new report that was released last week, we have already begun to implement the core recommendations of that report, including action to retain an independent monitor to audit our implementation of all recommendations, to retain an expert third-party to advise us on our culture change efforts and I have indicated the core objectives that we are trying to address for the Agency are to strengthen the ability of employees to report misconduct, to provide independent investigations of misconduct, including by third parties, and to strengthen our disciplinary process so that there is swift and certain justice for victims appropriate to the misconduct that has occurred, including separating individuals from the Agency.

I might also indicate that this year, four individuals have been separated from the Agency for misconduct. We have made management changes in key positions relating to this issue, and the implementation of a new independent Office of Professional Conduct will result in significant additional management changes by the Agency. We are committed to transformational change, to the structural change that I believe is the core recommendation of the report, and we have already begun to implement that.

Ms. WATERS. So what you are saying here in committee today is that you have implemented the plan, some of the tasks included in that plan have been completed, there is still more to be done, but you can see the results of the work of that plan already. Is that correct?

Mr. GRUENBERG. I think we can see certainly strengthened resources for anybody who is victimized, a hotline for anyone to report or seek assistance. We have instituted a training program for

all 6,000 employees, which is already well underway and has already trained a significant number of our employees, and we are following through on all of the action items in the plan.

Ms. WATERS. I believe that employees must feel free to engage in discussions and to give complaints and have their concerns dealt with. Do you sense in what you are doing, you are opening up that opportunity for employees?

Mr. GRUENBERG. I believe we are. We have enlisted employees across the Agency in participating in the implementation of the action plan. We offered expressions of interest to employees in Washington as well as our regional offices to participate, many are. I think the Agency across the board is deeply committed to addressing these issues and to following through on implementing the action items.

Ms. WATERS. Thank you very much, and I yield back.

Chairman MCHENRY. The gentlelady yields back. I will now recognize the vice chair of the full committee, Mr. Barr. Sorry. You are the vice chair of the Fed. I will now recognize the vice chair of the full committee, Mr. Hill, for 5 minutes.

Mr. HILL. I thank the chairman and thank you for calling this hearing with our prudential regulators. Chairman Gruenberg, before I get into the more substantive part of my discussions, you and I had a discussion on the phone, and I said, since the 1990s, the Federal supervisory agencies have held financial services companies to an incredible high standard about workforce practices, human resources practices, diversity training. It is a part of the routine review of bank regulators of regulated institutions.

As I said to you on the phone, I think this is a horrible double standard that here, 35 years later, 30 years later, we are having this kind of discussion about a Federal agency that is at the epitome of leadership in the financial oversight and supervision. I find that really disappointing, and that is why I have joined my colleagues in suggesting, I think in the best interest of banks and the Agency itself and your employees that you step down as chair.

You answered a question to Chairman McHenry that somehow you did not get angry, but I am looking at the report itself. Around the time of Silicon Valley's failure, May 2023, there was a meeting intended to cover corporate governance regulations with the chairman. He switched topics to talk about bank failures and according to one of the participants, Chairman Gruenberg went on a rant for 45 minutes, directing his ire at a particular individual, threatening that he could fire or reassign anybody he wanted. The meeting was so uncomfortable that the person who felt targeted by the chairman sent a Teams message out to everybody who was on the telephone. I want to say I am not sure you answered that question truthfully. Do you want to respond on that to the chairman?

Mr. GRUENBERG. Yes, Congressman. I believe the question directed to me was on that initial weekend of the failures, and I was responding to that. I take the point you raised in regard to the meeting in May, which was well after that, as you know.

Mr. HILL. Yes. Well, I mean, I do not think we should parse words here. I do not consider that responsive. I think the chairman asked an open-ended question.

Let me turn to Vice Chairman Barr. As you know, the courts have previously invalidated agencies' rulemaking where the final rule was not a "logical outgrowth" of the proposed rule. We have a case like that also in broker-dealers in the Securities and Exchange Commission (SEC) in 1993, *Tim Pinero* v. the *SEC and the Investment Company Institute and the CFTC* in 2013, and *Investment Company Institute* v. the *CFTC*, where the Agency's final rule deviated so much from the proposal that the court concluded that commenters were not given an adequate opportunity to have feedback. In other words, if you are going to try to fix a bad proposal, the public must have a meaningful opportunity to comment on these unanticipated changes. Bloomberg and other outlets have reported that the agencies that all three of you represent today have "already decided to adjust the original proposal rather than start over."

So let me start with you, Vice Chairman Barr. Have the agencies already agreed to tweak the existing proposal and not start over and re-propose?

Mr. BARR. We have not made any decision at all with respect to the process, as I indicated to the chair. When that Bloomberg article came out, the Federal Reserve issued a statement indicating as such. We are very much focused on the process.

Mr. HILL. Let me ask Chairman Gruenberg, have the agencies among themselves decided that, in fact, they are going to just simply tweak this rule and make it final and not re-propose? Yes or no.

Mr. GRUENBERG. No, Congressman.

Mr. HILL. Mr. Hsu?

Mr. HSU. No.

Mr. HILL. Very good. Well, that is helpful because Chairman Powell, I think, made very clear that there are substantial changes that need to be made to this rule, and I think to this committee, many of us believe that means this rule should be re-proposed. All three of you are members of Financial Stability Oversight Council (FSOC), and you probably heard Secretary Yellen's call last week that suddenly that we need to establish a new Federal bailout fund for mortgage servicers. Did you hear that comment, Vice Chair?

Mr. BARR. I am not sure I would have characterized the comment in that way, but the FSOC did issue a report on nonbank mortgage servicers that highlighted risks associated with—

Mr. HILL. But did she not call for a Federal fund to support them in case they got into financial trouble?

Mr. BARR. The FSOC report had a set of recommendations. One of those was for Congress to think about an industry-funded liquidity facility.

Mr. HILL. Okay. Let me reclaim my time on that and let me remind all of you why we are in this boat, because Dodd-Frank, pushing the mortgage servicing business out of the depository institutions that were regulated, had high capital, had regular supervision, and shifted it to the nonbank sector. Would you say that was a primary cause, the Dodd-Frank Act did create that incentive, Mr. Barr?

Mr. BARR. I think there were a set of factors that gave rise to——

Mr. HILL. But that was one of the factors. Would you agree with that?

Mr. BARR. I think that one of the factors was the way in which technology changed and the economy changed.

Mr. HILL. I will yield back, Mr. Chairman, but we will have questions for the record on that topic.

Chairman MCHENRY. The gentleman from California, Mr. Sherman, is recognized for 5 minutes.

Mr. SHERMAN. Mr. Chairman, I would hope that we would have a separate hearing devoted exclusively to the horrendous revelations at the FDIC. What we have here is this Hobson's choice of using our time to focus on how 6,600 employees at the FDIC have been treated and how we are going to dramatically affect the entire economy. I am going to focus on the latter, but I hope we have a hearing where we can focus on the former.

Chairman MCHENRY. I am happy to accommodate the ranking member.

Mr. SHERMAN. My concern, especially for Mr. Barr, is that this overall approach, first it is being sold as if it is conforming with a European or international standard, but actually, we are going to have much higher standards than Europe. That means less lending, but then we are going to have these higher standards, but then we are going to have lower standards than we should have for money going to Wall Street. For example, we ignore the interest rate risk on long-term bonds that are in the "hold-to-maturity account." I want to commend you for at least dealing with the available-for-sale account but Wall Street investments, as we learned from Silicon Valley Bank, it is the interest rate risk that is the big risk, and that risk is undercounted.

What we also undercount is we have only a 65-percent rate for loans to publicly traded companies, where an equivalent company that is not publicly traded, 100 percent rate. There are many ways to raise money on Wall Street, but that local pizzeria can only raise money from the bank, and anything that makes that loan less likely to happen concerns me, but I also want to focus on the discount.

There are rumors or reports that you are going to change the rules for discount window. I would hope that you would make that window more available to small-and medium-sized banks and make the technological changes necessary but the proposal is that the amount of capital that would have to be pledged would relate not just to the amount being borrowed, but whatever the bank had in uninsured deposits, and that you would end up with the absurd circumstance that if a bank wanted to borrow $1 million but happened to have $1 billion in uninsured deposits, it would have to pledge $400 million in capital to on borrow $1 million.

Can you assure me that the amount of capital that you have to pledge to borrow from the discount window will relate to the amount you are borrowing from the discount window and not based on the total uninsured deposits of the bank?

Mr. BARR. Thank you, Representative Sherman. You have touched on quite a number of topics. I will say, on the credit side, first of all, with respect to capital——

Mr. SHERMAN. If you could just focus on the question I asked. I have limited time.

Mr. BARR. The question related to discount window preparedness. We are working through the substance of that now. We are looking at a range of measures to make sure that banks are ready to use the discount window—

Mr. SHERMAN. Can you assure me that the amount of capital you pledge will relate to the amount you borrow from the discount window and that this will not relate to just the general balance sheet of the bank?

Mr. BARR. We are looking at a range——

Mr. SHERMAN. It is a "yes" or "no" question, sir.

Mr. BARR. We are looking at a range of ways to think about what——

Mr. SHERMAN. Okay, so that is not an assurance, and the absurd example I just gave could, under your answer, be the new rule.

Mr. BARR. I am not sure I fully understood the nature of the example, but we are looking at a range of ways of making sure that banks have enough discount window preparedness.

Mr. SHERMAN. I would hope that we would make it possible for midsized banks to accommodate charities and businesses that have to have accounts of over $250,000 for operations. I am concerned about the effect that these new rules are going to have on our capital markets, but I do want to focus on that 65 percent rule. You apply it to publicly traded borrowers, but what about mutual funds and pension plans like California Public Employees' Retirement System (CalPERS)? Is there any reason they would not get the 65 percent rate?

Mr. BARR. We are looking at comments on all of these issues with respect to the proposal. We received very helpful comments on credit risk, including the issues you raised with respect to pension funds and mutual funds.

Mr. SHERMAN. Can you assure me that you will treat clean energy tax credits just as we currently treat low-income housing tax credits?

Mr. BARR. We got very helpful comments on the tax credit provision, pointing out, for example, that the return to the investor is not based on the equity investment but really on the tax credit return. So that is a useful piece of information for us as we are thinking about these rules.

Mr. SHERMAN. I would hope that you would design these rules so that banks will lend money to small businesses rather than simply put their money in highly risky, long-term bonds sold on Wall Street, and I yield back.

Chairman MCHENRY. The gentleman yields back. We will now go to the gentleman from Oklahoma, Mr. Lucas, for 5 minutes.

Mr. LUCAS. Thank you, Mr. Chairman. There are certainly many issues that deserve our attention today. It has been concerning to hear that the report on the severity of the cultural issues at the FDIC and workplace problems at the chair level. From the report, it appears that repairing this situation will be an all-consuming task. If this same activity had occurred at a financial institution by a bank executive, I could only imagine how the response would be dramatically and very different. Confidence in our banking regulators matters; leadership matters.

In addition to the top-down cultural overhaul, there are many important policy issues that the FDIC must be focused on that impact all sectors of the economy. The actions of the banking agencies have a profound effect on the folks back home. One particular area of concern I focused on is the Basel proposal's impact on our ag and energy producers, which our constituents depend on to keep food and power both affordable and reliable. The proposal that has generated an unprecedented response from all sectors of the economy.

Mr. Chairman, I would like to enter a few letters into the record to discuss the impact. A Joint Agricultural Trade Association letter, a Joint Energy Trade Association letter, and last a letter from the American Public Power Association and the National Rural Electric Cooperative Association.

Chairman MCHENRY. Without objection.

[The information referred to can be found in the appendix on pages 139-145.]

Mr. LUCAS. I hope you all have the opportunity to review these comments and others from sectors of the economy that typically would not be compelled to weigh in on these issues, which speaks to the breadth and consequences of the current proposal.

Another thought along those lines, I would like to further underscore a consequence from the Basel Endgame proposal that stems from the increased capital requirements to engage in client clearing activities. In Dodd-Frank, Congress mandated central clearing as a way to reduce risk in the system. However, the number of banks that can clear derivatives for end users has reduced over time, making it more difficult to find a bank to offer this service and I have a real concern that the Basel requirements will significantly constrain the capacity of banks to offer central clearing. We should be careful not to reduce market access, particularly at the same time that the SEC is mandating clearing in the Treasury market. I have spoken with Chairman Powell, Secretary Yellen, CFTC Chairman Brennan about this issue, and they have all assured me that this is an area they are following closely.

First to Chairman Gruenberg and then to Vice Chairman Barr, clearing is a risk-reducing function for the market, but the Endgame proposal actively penalizes that activity. How do you reconcile this policy contradiction?

Mr. GRUENBERG. Thank you, Congressman. That is one of the key issues in the report. Clearing derivatives was a major focus of attention during the 2008 financial crisis and has been a focus of attention in the Basel capital accord. We have received a lot of comments on this issue. I acknowledge the points you are raising. This is still a work in progress, as Vice Chairman Barr has indicated. We are taking careful attention to all of the comments we received, including in regard to this.

Mr. LUCAS. Vice Chairman?

Mr. BARR. We are taking those comments very seriously. I agree with you that central clearing is an important way that we reduce risks in the financial system. We have received comments on client-cleared derivatives in a number of areas of the proposal, and we are taking those quite seriously.

Mr. LUCAS. I believe your agencies have a responsibility to ensure that bank capital standards do not unnecessarily discourage

central clearing. Market participants on the clearing side and the end-user side are warning us of what is to come. Again, I urge a complete re-proposal here. Make the material changes necessary and then allow Congress and the public to weigh in. The consequences of getting this wrong are too severe.

Now, in my remaining time, another issue: I have heard concerns about is the FDIC's Corporate Governance Proposal—The guidelines as proposed would be a significant departure from existing practices. The proposal is aimed at banks with much lower asset size than the corporate governance regimes at Fed and OCC are so far more prescriptive. Board of directors play an essential leadership role for a bank and should be held to a high standard. Chair Gruenberg, could you elaborate on this and clarify if it is a high priority of yours to ensure the proposal is in line with the OCC and Fed?

Mr. GRUENBERG. Thank you, Congressman. It is a proposal for comment. We are receiving comment in that proposal. We indeed indicated that institutions over $10 billion would be subject under the proposal. We did consult with the standards used by the Federal Reserve and the OCC, which set a $50 billion standard. We are receiving comment on that, and that is something we are paying attention to.

Mr. LUCAS. My time has expired, Mr. Chairman. Thank you.

Chairman MCHENRY. The gentleman from New York, Mr. Meeks, is recognized for 5 minutes.

Mr. MEEKS. Thank you, Mr. Chairman, I kind of agree with Mr. Sherman. I wish I had another opportunity to have two phases of this. I would love to talk about some of the substance of the economy, but as I sit here right now, if I am going to be honest, I am pissed off. I heard people talk about upset, appalled, but I am pissed off. That is my language and where I come from and I am pissed off because of the very idea that employees suffered from racial and gender discrimination, bullying, mistreatment, and harassment at the FDIC for years. As I see in the report, not a single one resulted in a removal, reductions in pay grade, or any discipline more serious than a mere suspension. That is who I am.

I have advocated for workers, I have advocated for diversity, equity and inclusion my entire career. So I cannot sit up here and say that I am all right with it because I am not. It concerns me greatly. If it was me in my office, I would probably be run out. I do not understand. Maybe you can tell me, how can trust and credibility come back to that Agency for all of the workers that were denied and people who may want to work at the FDIC? How can that trust and credibility be returned under current leadership?

Mr. GRUENBERG. Thank you, Congressman. We are devoting all the resources of the Agency and engaging employees across the Agency in addressing this issue. There is no, if I may say, no higher priority at the FDIC.

Mr. MEEKS. Why was something not done? When did you find out about this report? When did you find out? When was the first time did you find out about the special committee's report that was revealed on November 21, 2023?

Mr. GRUENBERG. You are referring to news articles last year. The special report was just released about a week ago.

Mr. MEEKS. Right. The news articles were there for the investigation to take place. Was that the first time you heard about harassment or anything of that nature?

Mr. GRUENBERG. For the deep-seated workplace culture issues identified, they were in those news reports. I immediately directed the third-party review to get an Agency-wide assessment from an independent source to understand the nature of the challenge we were facing and what we needed to do and that report was released last week, and it has given us, if I may say, a line of sight into the nature of the issue that we have not had before.

Mr. MEEKS. What I do not understand is, number one, how it could take place for all the years that it took place and admittedly you were not the chairman the whole time, but you have been there forever. I would think that if someone saw that type of harassment, those types of activities taking place, somebody should stand up, especially if you are in a leadership position, and say something and I believe I do have the responsibility of holding everybody that comes before us in accountability.

Let me ask Mr. Hsu and I believe Mr. Jonathan McKernan was co-chairs of the special committee. That is correct?

Mr. HSU. Correct.

Mr. MEEKS. I heard you say in that report, there is a report about some of the specific emotions, I will say, the loudness or conduct of Chairman Gruenberg. Is that correct?

Mr. HSU. The report cites 10 root causes of all of the issues that are deeply disturbing. Chairman Gruenberg was not cited as one of those root causes. There are a lot of causes, and they all require work. They require an enormous amount of cultural and structural transformation.

Mr. MEEKS. Let me just clear one at a time. Do you think that the current leadership can restore trust and credibility at the FDIC?

Mr. HSU. I do.

Mr. MEEKS. Let me ask you this question. Do you think that the three women that was added onto this committee were added to the committee enough times that they have meaningful participation in the committee's works?

Mr. HSU. I do.

Mr. MEEKS. I yield back the balance of my time.

Chairman MCHENRY. The gentleman from Texas, Mr. Sessions, is recognized for 5 minutes.

Mr. SESSIONS. Mr. Chairman, thank you very much. Gentlemen, I have on my door in Waco, Texas, our district headquarters: "When leaders sell ambiguity, it dismisses the role of leadership." I think you guys sell ambiguity. I think all three of you sell ambiguity. Mr. Hsu, were you aware that in July 2020, a report found that the FDIC had not established an adequate sexual harassment prevention policy?

Mr. HSU. If you are referring to the FDIC Office of Inspector General (OIG) report, yes, I am aware.

Mr. SESSIONS. I am.

Mr. HSU. Yes.

Mr. SESSIONS. Why did you try and parse the words about which month this was and whether it was just the other day or not? Just in the conversation you had with Mr. Meeks, you referred to, well, 2024. You did not say 2024. You alluded to "just the other day." You did not say just the other day. It became apparent that you were talking about of recent times.

Mr. HSU. I am sorry. I am not sure——

Mr. SESSIONS. Mr. Hsu, did any of these employees that are presented here, did they report to your organization?

Mr. HSU. I am sorry. Can you repeat the question?

Mr. SESSIONS. Within your line of management, did any of these employees that are mentioned here in this report——

Mr. HSU. So——

Mr. SESSIONS. That is a "yes" or "no", Mr. Hsu.

Mr. HSU. Well, I want to make sure that I am complying with privacy laws.

Mr. SESSIONS. Did they report within your organization?

Mr. HSU. I am sorry. I cannot answer this question.

Mr. SESSIONS. Oh, you cannot answer that. Let me go back and tell you, when leaders sell ambiguity, it dismisses the role of leadership. I will expect for you to write us an answer that yes or no, that I will hold private to me, and I would like the chairman and the ranking member to get that also.

Mr. SESSIONS. Mr. Barr, did any of the people that are mentioned in here report within your organization?

Mr. BARR. My understanding is the report focuses on the FDIC. I do not have any information.

Mr. SESSIONS. Okay. Were you aware of a July 2020 report from the Office of Inspector General that specifically said that the FDIC had not established an adequate sexual harassment program?

Mr. BARR. I learned of that report not in 2020, but I am aware that there was such a report.

Mr. SESSIONS. What year do you think you learned about this as a problem by the inspector general?

Mr. BARR. At the FDIC?

Mr. SESSIONS. Well, yes.

Mr. BARR. I do not know. I mean, I learned about it at some point after joining the Federal Reserve Board in 2022, but I could not tell you exactly when. The report is about the FDIC, not about the Federal Reserve.

Mr. SESSIONS. Have you looked at it in the context of your organization?

Mr. BARR. The Federal Reserve has a very strict zero tolerance policy for sexual harassment and discrimination.

Mr. SESSIONS. This is what I am getting at. Your organization had this as a very strict policy. Mr. Gruenberg, why did your organization not have a strict policy?

Mr. GRUENBERG. We had a policy at the time and compliance——

Mr. SESSIONS. A strict policy, Mr. Gruenberg.

Mr. GRUENBERG. The Inspector General (IG) report found shortcomings in our policy. It had 15 recommendations that I believe the Agency addressed. If I may say, in retrospect——

Mr. SESSIONS. That was back in 2020.

Mr. GRUENBERG. Yes, that is what I am referring to, the IG report from 2020.

Mr. SESSION. I am. Why did you have to go and hire an outside firm to tell you what the IG had told you? Did you not want to accept what the IG had said?

Mr. GRUENBERG. I believe the Agency at the time did accept the findings of the report. If I may just say, Congressman, that 2020 report did not identify the type of deep-seated cultural issues that this recent report has——

Mr. SESSIONS. Is that right?

Mr. GRUENBERG [continuing]. and that the news stories last year identified.

Mr. SESSIONS. These were things then that came as a result of your leadership, and they were brand new.

Mr. GRUENBERG. I think the new report——

Mr. SESSIONS. Now, that is what you are suggesting to me that was not old. This is all new.

Mr. GRUENBERG. No. If I may say, Congressman, the report indicates these are longstanding challenges for the Agency. I am simply indicating that the 2020 report did not identify the nature of the deep-seated cultural nature of the issues, and that came along later.

Mr. SESSIONS. Mr. Chairman, I find this very disturbing. I find that there is a lot of ambiguity and lack of acceptance of this, and yet, I find that they openly say we will take responsibility. I see very little responsibility. I yield back my time.

Chairman MCHENRY. The gentleman yields back. I will now recognize the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you, Chairman. Mr. Barr, I want to talk to you about this complex and complicated issue and especially the impact that it is going to have on two groups, our lower-income people and our banking system. This business of lowering the caps on debit card interchange fees will definitely hinder the banks' ability to offer low-cost and no-cost bank accounts to low-and moderate-income Americans. Are you aware of this, and what do we do about it?

Mr. BARR. You raise an excellent point, and I have spent a good bit of my career focused on issues of trying to improve access to credit and financial services for low-and moderate-income people. The Regulation II requirement is a requirement that Congress set out for the Federal Reserve to determine that fees are reasonable and proportional to the costs incurred that are specified under the statute, and the Federal Reserve has made a proposal to update that rule. We have received lots of comments on that proposal, including the kind of comment that you very, I think, appropriately laid out, and we are in the process of thinking about those comments and deciding what to do next.

Mr. SCOTT. I am also concerned about our small business owners and the incurring costs from debit card swipes on a regular basis. Now, as I said, this is a complex problem. It is something that does not need to be rushed into. I do not agree with it but my question to you is, if the allowable fees on debit card swipes are lowered, does the Fed share the bank's concerns? Our banks have big con-

cerns on this, about the availability of low-or no-cost bank accounts for consumers, or are these concerns overstated?

Mr. BARR. We have just finished the comment period, so we are in the process of receiving those comments. We take them very seriously. We are reviewing them now. I do not have an answer to your question yet, but those are the kinds of comments we will take quite seriously in the stage of the proposal that we are.

Mr. SCOTT. Mr. Chairman, I would hope that before we move on anything dealing with this that we get a total understanding of the impact on low-income and on our small businesses because it is clearly complex, it is complicated, and you are rushing to these things unprepared, and you cause great havoc. We did that with Dodd-Frank and when we moved, we wanted to bail out the big banks first, until I raised that objection to the President. I said, "President Obama, I am not voting on this Dodd-Frank here," and he said, "why." I said, "because you cannot solve this problem by bailing out the big banks or looking at it haphazardly. We have to do something about the homeowners who are having mortgages, combined with these high rates of unemployment." Those were the consequences of it, and luckily he told me to go to work and do something. We came back with the hardest hit. I think we probably need to do the same thing with this approach. I yield back, Mr. Chairman.

Chairman MCHENRY. The gentleman yields back. We will now go to the gentleman from Florida, Mr. Posey, for 5 minutes.

Mr. POSEY. Thank you, Mr. Chairman. I would like to yield to the gentleman from Kentucky, Mr. Barr.

Chairman MCHENRY. The gentleman yields.

Mr. BARR of Kentucky. Thank you, Mr. Posey. Mr. Hsu, I am sure that you have seen the Cleary report on the toxic workplace at the FDIC and the temperament of your colleague, Mr. Gruenberg. Keeping in mind that you have a duty to be truthful to Congress, can you testify whether there have been any occasions in which Mr. Gruenberg has directed anger and ill temperament toward you, including in discussion on the 2021 effort by Mr. Gruenberg and Mr. Chopra related to the Bank Merger Act?

Mr. HSU. No, not anger. Passion, yes, but not anger.

Mr. BARR of Kentucky. So you would describe the heated conversation that you had in 2021 related to the Bank Merger Act as passionate, heated, but not ill tempered?

Mr. HSU. Correct.

Mr. BARR of Kentucky. You have said that you think Mr. Gruenberg is capable of resolving these issues despite what you have witnessed. One of the six factors, or capital adequacy, asset quality, management, earnings, liquidity and sensitivity to market risk (CAMELS) ratings, that bank supervisory authorities use to rate financial institutions is the quality of management. If the OCC were to uncover the kind of misconduct identified at the FDIC in the Cleary report at one of your own OCC-regulated banks, what rating would the OCC give to that bank's management on a 1 to 5 scale, with 1 indicating the strongest performance and 5 indicating the weakest?

Mr. HSU. So the rating is a function of a lot of parts of the assessment, so it really depends on the nature of the weakness, how material it is to the safety and soundness of the——

Mr. BARR of Kentucky. You know what I am getting at, Mr. Acting Comptroller: toxic workplace, harassment, sexual harassment, discrimination, interpersonal misconduct replete in the report at the FDIC. If one of your examiners found that at a national bank, how would you rate that management of that bank?

Mr. HSU. We would rate it accordingly.

Mr. BARR of Kentucky. What does that mean? A matter requiring attention?

Mr. HSU. It depends on the severity and the specifics of the——

Mr. BARR of Kentucky. Well, I am talking about this kind of severity.

Mr. HSU. This is severe. I agree this is severe.

Mr. BARR of Kentucky. Mr. Barr, 97 percent of the almost 400 comments on the Basel III Endgame proposal were opposed to or expressed concerns, with 86 percent of negative comments coming from outside the banking sector. You have stated publicly and privately to me that the public will be able to comment on the Quantitative Impact Study (QIS). Given the overwhelmingly negative comments from the proposal from various parts of the ideological spectrum from across the country and various industries, why is there even a question whether or not the proposal should be withdrawn in full?

Mr. BARR. Thank you, Congressman Barr. We are looking right now at the substance of what we think about the comments. As I have suggested to you on numerous occasions, we got good, deep substantive comments. I expect we are going to make broad and material changes across all three areas of the proposal, operational risk, credit risk, and market risk. Once we decide on what we think the appropriate substance is, we will turn to the question of what the appropriate process is. We have not gotten there yet.

Mr. BARR of Kentucky. I appreciate that and I appreciate the fact that the Fed is open to those broad material changes, but to follow on Mr. Hill's excellent line of questioning the case law in the administrative law area is pretty clear. Broadened material changes require withdraw and re-proposal under the law. Again, why is there any question whether or not there would be a withdrawal and re-proposal giving commenters the ability to comment on the new proposal, the re-proposal?

Mr. BARR. Congressman, as I said, we will follow the law. We will follow the Administrative Procedures Act. There is no question about that. We just have not turned to the procedural question yet. We are focused right now on the substance.

Mr. BARR of Kentucky. Thank you for your commitment to allow for comment on the QIS. What is the timeline on the release of the QIS?

Mr. BARR. Staff are working diligently on that. They are in the process of quality control and review. It will be relatively soon.

Mr. BARR of Kentucky. Thank you. Mr. Barr, one final question, and I know you have worked really hard on this, and you and I have gone back and forth but one thing I am concerned about is that the proposal will likely raise capital requirements for U.S. fi-

nancial institutions by more than 20 percent. There is evidence that in the EU and the UK, implementation of the Basel III Endgame proposal would be at a much lower calibration, closer to a 5 to 7 percent increase. Are you concerned about the gold plating here in the United States putting our institutions at a competitive disadvantage?

Mr. BARR. We are looking at all the comments we received on this, including on this question of gold plating. I would say at a much higher level, Congressman, it has been my experience that having very strong capital requirements in the United States has been to a competitive advantage to our firms, who are thriving in the marketplace.

Mr. BARR of Kentucky. My time has expired, but remember, the objective of Basel III Endgame was harmonization. With that, I yield back.

Chairman MCHENRY. The gentleman from Connecticut, Mr. Himes, is recognized for 5 minutes.

Mr. HIMES. Thank you, Mr. Chairman, and thank you to our witnesses for being here. Chair Gruenberg, I despise these congressional pylons for a couple of reasons: Number one, I have always very much enjoyed the working relationship we have had in crafting regulation. Number two, the high dudgeon and moral outrage we show up here suggests that we are great managers and excellent at taking responsibility or do not have feet of clay, and there is no evidence for any of that, but we are charged with oversight.

I have read the report, and I have a particularly difficult time with the sexual harassment part of it. I grew up with a single mom and two sisters and have two daughters and see every day the challenges that women face in the industry and around. So I have a really hard time with some of what we see there. I guess my question for you, sir, is your opening statement here, you say that when news reports of harassment first surfaced last year, were you completely unaware for the 10 years prior of these allegations, these many allegations?

Mr. GRUENBERG. Thank you, Congressman. I was aware of cases being brought under our normal processes, but the kind of deep-seated cultural issues identified in the news reports last year and in the report that was recently released did not come to light, and as I indicated, I view that as a failure on my part. I simply did not identify the deep-seated cultural issues that were revealed in the news reports and in this recent report. I will say, once those reports came forward, we have devoted all the resources of the Agency since that time to addressing this issue.

Mr. HIMES. I want to move on because I have other topics, but you have said you take full responsibility. If you were the skipper of a ship in the Navy or a corporate CEO, I have very little doubt about what would happen in those instances.

But forget about us and forget about the lawyers. I want you to just take a minute because I am stumbling over this, "I am the right guy to fix this thing." So forget about us and forget about the lawyers. I want you to imagine that instead of us, you are looking at the young woman who it was implied that she should be a surrogate for her boss' child, the gay man who felt he had to hide his

preferences because he was called a little girl, the women who got photos of genitals. I want you to imagine that we are those people and just take a minute and tell us, not us, but those people why you are the right leader to lead these critical reforms.

Mr. GRUENBERG. Thank you, Congressman. I have indeed met with some of the people you are describing. I understand keenly the hurt they feel, the impact these kinds of experiences have, and it is why I am totally committed and I believe the Agency is totally committed. We have been working on this now for several months. I believe we are making progress. I think we have been informed by the new report. We are already implementing the recommendations of the new report. We can address this issue, and I think it is critical to move forward and address the issues that have been identified, and we have an opportunity to do that.

Mr. HIMES. Chairman, I do not know how that works for them. I would just ask you to sit with them and persuade them that you are the right leader, and if they are not persuaded, we do not matter. There is more than a whiff of politics up here right now. We do not matter if they are not persuaded. I hope you will do the right thing.

Vice Chairman Barr, I look forward to the moment when I do not have to constantly be thinking, emailing, and talking about Basel III Endgame. When are we going to finalize that process?

Mr. BARR. Thank you very much, Congressman. Right now, as I mentioned, we got lots of comments. They were deeply substantive. We are working our way through that substance. We have made good progress. You have heard me say, you have heard Chair Powell say we are expecting we will make broad and material changes to the rule. I expect those to occur across all three areas—operational risk, credit risk, and market risk. We need to work through that substance, finish working through that substance, turn to the question of what the right process is but, we are not on a timetable that is dictated by anything other than getting it right.

Mr. HIMES. Okay. Okay. Great. I will just make the point we have talked about this a lot. I desperately want to be on your side. I came here in the first quarter of 2009. I spend a lot of time worrying about a world where Citibank goes belly up. I want to be on your side, but as I have said a whole bunch of times, I really need to understand the analysis underlying the call for additional capital standards. If I get that and if it is persuasive, I will be there, but I just need to get that. With that, Mr. Chairman, I will yield back.

Chairman MCHENRY. The gentleman from Missouri, Mr. Luetkemeyer, is now recognized for 5 minutes.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. This is a very deeply disturbing moment to me from the standpoint as a former bank examiner with the State of Missouri for a couple of years and having gone to the FDIC school when I was an examiner. Of course, I did not go there when it was the FDIC Hotel, as reported by this report this morning. While I have deep respect for the FDIC from the standpoint I have worked with the examiners both as an examiner and as a banker, but this report along with the long tenure of Mr. Gruenberg leaves a lot to be desired, is very concerning.

Let us just start with it. An independent third-party report, 167 interviews, or 10 percent of the people, roughly, complained of abusive treatment. Things like gender and race discrimination are documented, as Mr. Meeks indicated this morning. We got anger management issues with the management of the Agency. We have field officers that are in fear of reporting for fear of retaliation. How in the world can people do their work if they are fearful of being able to report what is actually going on? It cannot happen.

We have promotions within the Agency based on the club that they are in, which is nepotism. That cannot be tolerated. The new report indicated that the FDIC's Seidman Center—in the Wall Street Journal article, the FDIC Hotel—there are 24 instances of intoxication, misconduct occurred, two sexual harassment and one rape—two sexual harassment and one rape—within the FDIC Hotel. Now, this morning, we hear from your testimony, Mr. Gruenberg, that you indicate that it just surfaced a little while back and you just learned of it then of the depth of this. Sir, there ware 92 harassment claims according to the report 92. You have to be either totally incompetent or not caring, allow it to go on and be a facilitator of all this activity. Zero resulted in removal, zero resulted in reduction of pay, and no discipline more serious than a suspension or a transfer occurred. Unbelievable. That is facilitation in its purest form.

Now, one of the things that is going to happen here, we are going to try and make sure that Ms. McWilliams, who was interim between your two terms, is also a fall guy in this, and the report says nothing about that. In fact, it speaks pretty glowingly about her. "Within just 3 months of your departure, sir, your successor built enough trust with employees that they felt they could share their stories, and she began to work on the FDIC's culture problems." They actually are supportive of what she was doing." So the report talks about discrimination, gender and race, sexual harassment, nepotism, and your anger management issues, but we know some more, sir. I have been here a long time. This is my 14th year on this committee, okay, which is a long time. I also know that you lied to me, you lied to the chairman, you lied to this committee about Operation Choke Point, and it took an email where we found you involved before we confronted you. You admitted in my office that you were involved in this, and it stopped. Since then, since your new term, you have been involved in it again. Remember the ATM operation? Either you or your individual person was here, along with your three representatives, and also admitted wrongdoing there.

But also, there is weak management from the standpoint of regulation—that is what your job really is—as evidenced by the three banks that failed last year. As a bank examiner, there is no way in the world I would have allowed the bank model of those three banks to exist. Eighty to 95 percent insured deposits. Are you kidding me? No way. You knew about it for a year, did nothing? In doing that, you endangered not only the viability of those banks, but the viability of our system because what happened, they went down. Runs were started on other banks around the country. I got phone calls from everybody, all sorts of bankers worried about

what is going to happen all because of the lax management and a lack of regulation.

Mr. Hsu, you are part of the problem as well. You and Chopra and Gruenberg were the three that went in behind McWilliams' back and tried to do something about this bank merger situation and managed to oust her. Shame on you guys. Mr. Gruenberg, you have become the Michael Cohen and Harvey Weinstein of the FDIC, and you need to go. If you have the decency, please step down. If not, I would urge the President of the United States to replace you ASAP, and with that, Mr. Chairman, I yield back.

Chairman MCHENRY. The gentleman yields back. The gentleman from Illinois, the ranking member of the Financial Institutions Subcommittee, Mr. Foster, is recognized for 5 minutes.

Mr. FOSTER. Thank you, Mr. Chairman. Acting Comptroller Hsu, last Friday, the FSOC issued a report on nonbank mortgage servicing and in your statement following your vote to approve that report, you stated that the report identifies important financial stability concerns that need to be addressed by Congress and the press release announcing the report notes that in 2022, nonbank mortgage companies originated approximately two-thirds of mortgages in the United States and owned the servicing rights on 54 percent.

I came in March 2008, and so I spent a lot of the first years cleaning up the mess of an under-regulated mortgage industry and then looking at the damage that did to families in America and this report notes the benefits of this trend, such as supporting lending to historically underserved communities but also the risks that are associated with it. Could you speak a little bit about some of the risks associated with concentration in this space and other dangers?

Mr. HSU. Thank you for the question, Congressman. As the report noted, today's mortgage servicing is concentrated in a relatively small number of nonbank mortgage servicers, and there are certain fragilities that come with that. So if there are disruptions to those services, that could have impact on many, many people.

Mr. FOSTER. Yes. Could you be a little more specific? I mean, what is the scale of this concern? Would it have implications for the Government-Sponsored Enterprises (GSEs): Fannie, Freddie, Ginnie Mac? What would the contagion look like in this area that would be a source for potential worry?

Mr. HSU. So it depends on the nature of the problem that manifests, but as you pointed out, there are strong connections with the GSEs with regards to these mortgage servicers, and, of course, the GSEs are then connected to the banking system. So the potential for widespread contagion from issues or problems at the nonbank mortgage service companies could be severe.

Mr. FOSTER. Yes. Could you be a little more specific? I mean, what are a couple of example nightmare scenarios where you could have contagion?

Mr. HSU. A nightmare scenario. At the very extreme, there could be massive disruption of mortgage servicing, which would really impact a significant portion of the mortgage market. In which case, that is billions and trillions of dollars that are flowing through the

system that would be disrupted, and that could have knock-on effect onto both GSEs and banks.

Mr. FOSTER. Now, the report includes several recommendations for Congress, including providing additional authorities to help firms manage the risk, to promote information sharing between the State and Federal regulators which share the burden here. Can you speak a little bit about how those recommendations, if followed through by Congress, would promote financial stability?

Mr. HSU. Sure. One of the primary recommendations is for Congress to strengthen both the supervision and the framework around the nonbank mortgage service companies so they are held to a standard that enables safety and soundness in that market. That is the core of it. In addition to that, I think, as was discussed earlier, having an industry-funded fund that would provide liquidity as necessary in case there are liquidity issues at those servicers.

Mr. FOSTER. So this would be like the Deposit Insurance Fund (DIF) or Circle liquidity? I mean, is it liquidity in the sense that you would pledge assets so you would expect a member to take a loss on this fund, or is this something where the industry as a whole would be responsible for replenishing the fund?

Mr. HSU. Yes, it is more of the latter, and I think the details of that would still need to be worked out obviously, but the idea is that the industry itself, the nonbank mortgage servicing industry, would fund it.

Mr. FOSTER. Okay and so then I am immediately led back to Representative Hill's comment about maybe just moving this more back into the banks, and there already is a DIF for it, and trying to understand the reason for the market moving the way it has.

Mr. HSU. For any given activity, especially with mortgages, there is risk, and that risk has to be managed and properly buffered for both for capital and liquidity. We want to make sure that those standards are applied equally and appropriately wherever they take place, whether it is within the banking system or outside of the banking system, and the FSOC report really gets at that.

Mr. FOSTER. Yes. Well, that——

Mr. HSU. We want to level up. We want to make sure that playing field is level and leveled up.

Mr. FOSTER. Yes. I have to say that is the FSOC doing exactly the job that we hoped you would do to actually look around the corner and look holistically at the system and say, okay, are there things that we are going to be having hearings about next year after things blow up and to the extent that you are able to foresee and prevent those, you are doing your job well, so thank you, and my time is up. I yield back.

Chairman MCHENRY. The gentleman from Michigan, the chair of the Oversight Subcommittee, Mr. Huizenga, is recognized for 5 minutes.

Mr. HUIZENGA. Thank you, Mr. Chairman. I want to clarify something that seems to be a well-worn path for some on the committee, about this report only being about you because Cleary Gottlieb simply did not look anywhere else. Sheila Bair was mentioned twice in that report, one referencing the cultural change she started after a 2008 altercation that you had. Chair McWilliams was referenced 4 times, referencing her attempts to improve the cul-

ture, including creating TEAM FDIC, which stands for Transparency, Empowerment, Accountability, and Mission, to implement a ground-up opportunity for FDIC employees to get involved, cleaning up your mess once again. Cleary Gottlieb had said in their briefing to the committee that if there was any negative or derogatory information on any of the chairs, they would have included it. They were silent because those two women were cleaning up your mess, sir.

Now look, we all know the FDIC plays a critical role in our financial system. Your job as chair is to maintain that stability in the system. You had earlier said to the chairman that your staff regularly briefs you on bank policy or issues related to banks and that sometimes that bad news is regarding bank failures. What we learned, though, in our own investigation as a committee—we did dozens of transcribed interviews and had dozens of whistleblowers that came forward outside of Cleary—we learned that in our own investigation that senior advisors actively prepared and coached their staff before briefing you, warning them about your behavior. Did you know that? Yes or no. Do not thank me for the question. Yes or no.

Mr. GRUENBERG. No, Congressman.

Mr. HUIZENGA. You did not? Okay. Your staff also shared stories during their interviews that FDIC staff had been known to cry after leaving meetings with you and that others described having to comfort colleagues after interacting with you. No such stories were documented about either Chair Bair or Chair McWilliams. Cleary Gottlieb found staffers fret and, from the report, "delayed delivering news that they feared would upset you and your reactions, and did have a chilling effect on open communications."

So let me be very clear. If your staffs are so afraid to give you bad news and they delay telling you that news, it simply makes a bad situation even worse. Sir, you are the wrong person for the job to clean up this mess. The mission of the FDIC is far too important, and you are unwilling or unable to accept negative information. Any delay of information getting to the chairman of the FDIC is a recipe for disaster. If you cannot deal with bad news, you are the wrong person for this job.

I want to hit on one other important point. Last time, Mr. Gruenberg, you were before the committee, you were asked directly by the chair if you had ever been a subject of an investigation. You said no. Then after some self-reflection during a break for votes and I believe a call from a reporter, you admitted that you actually had. Just like you did today, you were parsing your words. Cleary Gottlieb's report explained that the 2008 incident, where you made a senior executive feel personally attacked, the report alleges that the staff felt embarrassed and humiliated and that you created a hostile environment.

Mr. Chairman, I would like to include a redacted copy of that 2008 management inquiry into the record.

Chairman MCHENRY. Without objection.

[The information referred to was not submitted prior to printing.]

Mr. HUIZENGA. That person was Arleas Upton Kea while you were vice chairman at the time, and recently you just named an FDIC Chairman's Award for Operational Excellence after Ms. Kea,

Upton Kea. So you named an award after the same woman who you screamed at and the same woman who accused you of withholding information for being disloyal to you. Sir, I certainly hope this is not some sick ruse to buy her silence.

I am going to use your own opening statement to close mine. On page 2, you said, "This misconduct first surfaced last year." That is simply not true. This had been out there as rumors and innuendo and many other complaints, but you also say you regret not having identified deeper cultural issues at FDIC sooner. Sir, you created the culture. You created the culture there, and you are the wrong person for the job, and you finish on page 3, going on to page 4. The three core elements of your action plan provide more support for victims is your first point; number two, strengthening process for reporting and investigating complaints; number three, improving accountability for anyone who is found to engage in misconduct, including through separation from the Agency. How can this not be you, sir? You are the wrong person for the job, and I yield back.

Chairman MCHENRY. The gentlewoman from Ohio, Mrs. Beatty, is now recognized for 5 minutes.

Mrs. BEATTY. Thank you, Mr. Chairman and ranking member and to our witnesses here today.

I am not sure where to begin. I have sat here and listened to my colleagues on both sides of the aisle, and I agree with a lot that has been said on both sides of the aisle. As a Black woman, as someone—when Congressman Himes asked you to reflect on talking to those individuals and especially women, I was sitting here thinking how I would feel and then I reviewed again the massive report and the executive summary of the FDIC report. I am not going to go through it because much has been said and rightly so. This is troubling. It is a longstanding culture of sexual harassment and misconduct.

I do not know where to start with the blame, but this did not just happen now. If you go to the middle of the report, which I have spent many hours, along with my legal counsel and staff here going through this, the report says this has been going on for years. Now, I am not going to maybe accept whether it was William or Bair cleaning it up. I think all of you are at fault. I think everybody that sat in that seat has to take some ownership. I do not know what they tried to clean up, nor you, but I do not make it just this watch. I am so bothered that the three of you to me share in this because this is massive. If we go to the middle of that 300, 400 report, there were some 510 hotline reports. I think it is important to us. So 97 individuals reported 145 separate incidents of sexual harassment, unwelcome sexual advances. Ninety-one individuals reported 141 separate occasions of gender and sexuality-based discrimination. A hundred and eighty-seven individuals reported 320 separate incidents of workplace bullying, threat, and verbal abuse. This is not small.

Now, I do welcome the fact that you accepted responsibility, that you have put a plan together, but I guess I am curious. Are we going to go back and look at all these things? Where is the accountability? Was somebody terminated? Will people go back as a result of this and be terminated? While that will not repair what has hap-

pened to some of these individuals. For a female employee to be touched or to have to watch videos, to be asked to carry a child, that is not something that this Congress would accept.

This is not a Democrat or Republican, but I want to be fair on both sides. It is not you just as a leader with this administration who should be admonished. Everybody should be admonished and I guess what I want to hear is let us open up Pandora's box, let us go look at all those managers. It is from the top down but there are a whole lot of people that are getting a pass today while we are beating the heck out of you. A whole lot of people should be sitting with you and behind you who should also carry in this blame. So I do not want anyone to think—because I am all about putting people over politics, people over politics, and that is what I stand for, and I know my colleagues here do as well. So I just wanted to enter into the record, I do not think I have a question, but I want you and all those who report under you—you should not carry this burden alone.

Now, you should [inaudible], and everything that has been said on both sides of the aisle you are going to have to weather because we have it here before us, but I am suggesting that you go back. A whole lot of other folks need to be responding to the questions that my colleagues are asking to help at least show that we care about all of these individuals that have had to have been exposed to this. Mr. Chairman, I yield back.

Chairman MCHENRY. The gentlelady from Missouri, the chair of the Capital Markets Subcommittee, Mrs. Wagner, is recognized for 5 minutes.

Mrs. WAGNER. Thank you, Mr. Chairman. Chairman Gruenberg, you have been at the FDIC for 19 years, leading it mostly for 10 of those years. During that time, you apparently never once took it upon yourself to look into the toxic workplace that you are leading, that is until the Wall Street Journal published articles detailing your ill temper and inappropriate behavior toward FDIC employees. After your reputation was put at risk, then and only then did you decide to work on getting your house in order, sir. In this report, north of 500 employees came forward with complaints of sexual harassment, discrimination, and other workplace misconduct. This is a massive number, and it is only scratching the surface. For context, you have over 5,000 employees, the FDIC, today.

A quick answer to these questions, sir. Chairman Gruenberg, how often do you get out of DC and visit FDIC regional and field offices?

Mr. GRUENBERG. We have six regional offices around the country, Congresswoman. I try to visit each regional office at least once a year.

Mrs. WAGNER. One time a year, and the field offices?

Mr. GRUENBERG. Generally, not field. We have 70 field offices——

Mrs. WAGNER. So you do not go to the 70 field offices. Once a year you go to the six regional. Sorry. Do you meet with the employees, rank-and-file employees, when you have those once-a-year visits?

Mr. GRUENBERG. Yes, I do.

Mrs. WAGNER. Did it ever once occur to you that something highly inappropriate was going on at these offices?

Mr. GRUENBERG. The kind of deep-seated workplace culture did not come through in those visits.

Mrs. WAGNER. You got to be kidding me.

Mr. GRUENBERG. No.

Mrs. WAGNER. Why? How could you not know? You have been there on the Board 19 years, and you are telling me that you have never heard a single story of harassment? Sir, I remind you, you are under oath.

Mr. GRUENBERG. Congresswoman, I understand the question and why you ask it. In those visits, I met with employees, rank-and-file employees. It simply did not come forward.

Mrs. WAGNER. Well, this report has some of the most horrific H.R. abuses that I have ever read in my life. We can talk all day about your personal management problems, and that I find appalling also, but what is more concerning is the complete ignorance of the well-being of the employees that you are entrusted with leading, and the fact that you do not even visit or talk to them. Once a year to six regional offices, never to one of the 70 field offices. Your employees have lost confidence in you, sir. I have lost confidence in you, and Congress has lost confidence in you. You sir, should be fired. Not resign. Fired.

Mr. Chairman, I ask unanimous consent to enter into the record a letter from the Independent Women's Forum and the Independent Women's Voice requesting Chair Gruenberg's resignation.

Chairman MCHENRY. Without objection.

[The information referred to was not submitted prior to printing.]

Mrs. WAGNER. Mr. Hsu, your report identified—these are all quotes, Mr. Hsu—"patriarchal, insular, toxic boys club culture," where there was, "widespread fear of retaliation," and where "management's response to allegations of misconduct as well as culture and conditions that gave rise to them had been insufficient and ineffective." The report found that cultural and structural changes were necessary. Mr. Gruenberg has been on the FDIC Board for 19 years and been the patriarch for 10 of those years. In those 10 years of leadership, has he failed to address these important workplace conditions and what makes you believe he remains qualified to implement the necessary cultural and structural changes outlined in your report?

Mr. HSU. As the report notes, what is needed for effective leadership of the Agency at this time is leadership that empathizes and fully recognizes all of the problems——

Mrs. WAGNER. Okay. I do not need a regurgitation. Mr. Hsu, your own report states, "Chairman Gruenberg's reputation raises questions about the credibility of the leadership's response to the crisis and the moral authority to lead the cultural transformation." Do you now renounce the findings of your own report, sir?

Mr. HSU. No, I accept those findings. I fully accept those findings.

Mrs. WAGNER. Then how on earth do you believe that Mr. Gruenberg can lead this Agency into a new and better day in culture?

Mr. HSU. I believe Mr. Gruenberg has taken full responsibility for all——

Mrs. WAGNER. No, he has not. He does not even visit the agencies. He was not aware of one single harassment report. My time has expired. I have questions for you too, Vice Chair Barr, but I will submit those in writing. I yield back.

Chairman MCHENRY. The gentleman from Massachusetts, Mr. Lynch, is now recognized for 5 minutes.

Mr. LYNCH. Thank you, Mr. Chairman. I came out of the building trade. I was an iron worker for about 20 years, and it is a rough-and-tumble workplace. We work hard. We play hard. I get that but Mr. Gruenberg, this report makes the iron workers look like boy scouts compared to what was going on at the FDIC. Now, rather than using all my time to recount the parade of horribles here and outrageous conduct on the part of FDIC employees, I am going to ask you: People have spent their time railing at you, and you are not getting a chance to tell us what is the plan here. This cannot continue.

I got to tell you, as a former foreman and a general foreman, I would have fired a whole bunch of people at the FDIC. I would have just fired them flat out, and you need to fire some people if you are going to clean this up. I mean, you do not treat women like this. You do not treat humans like this, whether they are women or people of color or lesbian, gay, bisexual, transgender, and queer or questioning (LGBTQ) kids. I saw an interchange there, where they were handled really poorly. What is your plan? What is your plan going forward? What are you going to do here to straighten this mess out? You say you are the guy to do it.

Mr. GRUENBERG. Yes.

Mr. LYNCH. Tell me about that.

Mr. GRUENBERG. Fundamentally, we got to break the good old boys' network that is at the core of the report, protecting each other and providing an obstacle to employees coming forward to report a piece of experiences. We have to break that. The report says——

Mr. LYNCH. Are you going to fire anybody, or have you fired anybody here?

Mr. GRUENBERG. We have separated four employees this year who have engaged in misconduct, and we have——

Mr. LYNCH. Separated? What is that? Did you fire them or did you reassign them?

Mr. GRUENBERG. Have rather received termination notices and were fired or they have been informed about disciplinary action. Before the disciplinary action takes place, they leave the Agency or retire.

Mr. LYNCH. How many people have you fired?

Mr. GRUENBERG. Four separated this year.

Mr. LYNCH. Sounds like you need to fire more people on that. I am just reading this record. Four people did not do all this. A lot of people did this.

Mr. GRUENBERG. I agree with that.

Mr. LYNCH. Go ahead.

Mr. GRUENBERG. I agree with that.

Mr. LYNCH. Go ahead. What else?

Mr. GRUENBERG. We need, as the report recommends, fundamental structural change to break the network, which is why we are proposing setting up a new independent office outside of the organizational structure of the Agency where we would consolidate all of the misconduct responsibilities for the reporting of complaints, for the investigation of complaints, utilizing independent third parties to do investigations, and for disciplining misconduct when it occurs. That——

Mr. LYNCH. All right. Look——

Mr. GRUENBERG. And it would report directly to the Board of Directors.

Mr. LYNCH. All right. Okay. We need to be informed. We need reports every couple of weeks on who you are firing and the changes that you have made. You are on a short leash. A lot of people here would like to see you gone, to be honest with you. I am not so sure you are the guy to make the changes, but maybe you are. Maybe you can prove that to us. I do not know. I do not know. It will take some doing, but things have to change there.

Mr. Hsu, I would like to talk about financial services at some point here. Tokenization, I know you just had a symposium on that. I am the ranking Democrat on Digital Currencies. I have a question. Is it possible to tokenize any security?

Mr. HSU. It depends on how that term is being used. Now here, I think we have to be very, very careful——

Mr. LYNCH. Which term? "Tokenization" or "security?"

Mr. HSU. No, tokenization.

Mr. LYNCH. Okay.

Mr. HSU. Some people are using that term very loosely, and I would caution against that because for tokenization to solve the underlying problem of settlement, it has to be fully aligned with the legal system. So you have to solve not just the technological problem. You have to solve the underlying who owns it, how do you transfer ownership, how do you do risk management, and that is the right way to approach it. That is the symposium that we held was to tackle all of those questions. There are folks out there talking about tokenization. We are only talking about the technology layer, and that is half of that.

Mr. LYNCH. Okay. My fear is that the tokenization issue, the technological part of it, could turn the traditional security system upside down. Is that a legitimate fear?

Mr. HSU. That is a possibility if it is not done correctly.

Mr. LYNCH. Okay. Okay. All right. Thank you. Mr. Chairman, I yield back. Thank you.

Chairman MCHENRY. The gentleman from Texas, Mr. Williams, is recognized for 5 minutes.

Mr. WILLIAMS of Texas. Thank you, Chairman, and before I begin with my questions, Mr. Gruenberg, I would like to state for the record that I strongly condemn your actions exposed in the recent report. Many of my colleagues have touched on this today, but this 234-page investigation detailed a very toxic environment in your Agency, and I am a small business owner. I know how that can hurt a business, and your actions and the actions of the individuals involved are unacceptable, and we do not tolerate that.

Next, I would like to follow up a little bit what Mrs. Wagner said. How are we, sir, supposed to believe you are willing or even able to implement a culture change if you cannot accept responsibility for your own actions? We have heard that you took a tour to your regional office for listening sessions. Well, it is safe to say that did not go well either, and I have been told that at one of these listening sessions an employee asked you directly who their allies are and asked you directly, "Who is my ally," and you responded, "I have to get back to you." Well, if that answer is too complicated for you, I think you are the wrong person to lead this change, and you will get back to them. The answer here was pretty easy. It is, "me, I am your ally." But you are the chairman of this Agency with a total workforce of over thousands of employees, and at the very least, these employees should feel like you are their ally.

Now that being said, let me move on to Chairman Barr. I would like to begin by discussing the long-term debt proposal. The proposal would require a covered bank to hold debt equal to at least 6 percent of its risk weighted assets. This amount, 6 percent, is far too high for regional banks given their risk profile. This will increase these banks' costs, and these increased costs will inevitably be passed down to consumers like me, a small business owner, without strengthening financial stability. Imposing such stringent requirements on regional banks not only stifles their ability to lend to small businesses and stimulate local economies, but it also undermines the fundamental principles of free market capitalism, which hinders competition, innovation within the financial sector.

So, Vice Chair, how do you see the standardized 6 percent impacting smaller banks, and do you think there is a value in tailoring the percentage required based on the sizes of the financial institution?

Mr. BARR. Thank you, Congressman Williams. It is a really critically important question. We are looking very much at the question of what the right calibration is for different size of institution. We received a lot of comments on that question. We are taking those very seriously. We want to have a requirement that improves the resiliency of the financial system and that also respects the diversity of our financial system, which is really a critical goal.

Mr. WILLIAMS of Texas. Thank you for that. I have serious concerns about how the Basel III Endgame proposal is going to negatively impact small businesses and the institutions that serve them and provide for small businesses' individual needs. I still do not see why we cannot do it the American way, why they cannot follow America. This proposal will severely reduce financing and access to capital for small businesses, making it harder for them to secure funding to hire workers, maintain operations, and expand their operations. This could result in a domino effect, stifling economic growth in local communities where these banks are often a driver of entrepreneurship and businesses like mine, we go to community and local banks. As a consequence, the proposal risks hampering innovation and job creation. Businesses across this country are struggling to navigate this regulatory landscape and, quite frankly, handle the increase in burdensome requirements.

So, Comptroller Hsu, has the OCC held discussions regarding the Basel III proposal with small businesses, and how have you taken business' concerns into account?

Mr. HSU. Thank you for the question. We have received quite a few comments from small businesses and those expressing the interest of small businesses and those comments, we have taken those all into account as part of the process, as my colleagues have pointed out. We are taking it very seriously. We are looking very closely at those.

Mr. WILLIAMS of Texas. Okay. Very good. With that in mind, I yield my time back.

Chairman MCHENRY. The gentleman yields his time. We will now recognize the gentleman from California, Mr. Vargas, for 5 minutes.

Mr. VARGAS. Thank you very much, Mr. Chairman. I do apologize at the outset for my voice. I am starting to lose it. I know it is a bad thing for a politician, but it happens.

I was excited today—some time ago to talk about oversight of the prudential regulations—regulators, I should say—and I was very anxious to talk about Basel III, the Endgame. I was a signatory to a letter that was sent to you. I do have some great concerns, and I also want to talk about something I am very aware of, and that is the climate-related risks, the financial risks that the system faces, and I wanted to talk about that. I think it is very important.

However, obviously, we have delved into what is happening in FDIC. I think it is important. I would associate myself with everything that my good friend, Jim, said, the fine member from Connecticut. I have two daughters, too, and I love them more than life itself. To think that they would be in an organization where they would be harassed and that they would have no recourse and there would be little care for them, just outrageous to me as a father, as a human being. I think it is outrageous. What went wrong, Mr. Gruenberg? I mean, your department seems to be an outlier. What went wrong?

Mr. GRUENBERG. I think this is a long-term issue, Congressman. As the report indicates, I think it was particularly challenging in our field offices around the country. The FDIC supervises nearly 3,000 banks. We have 70 field offices, often in remote locations and that presents opportunities for misconduct and challenges for oversight and supervision, and that has to be a focus of our attention.

Mr. VARGAS. Just to be fair, I was the vice president at Liberty Mutual and a lot of offices all over the place, too, but there was a culture that you did not put up with this crap. You just did not, and you have an avenue to talk to somebody and ultimately get to people like myself. I was in the corporate legal side, and we would do something about it. To me, I do not understand how this could have happened for so long.

Mr. GRUENBERG. I think that is the issue we have to address. This report that has come out has given us a deep line of sight into it, and we are going to work to address it and to fix it. That is the commitment we have made.

Mr. VARGAS. Okay. I do also have some serious doubts of your ability to do it because you have been tangled up in this. Your temperament and other things came out in the report. You were going

to say something. I am going to allow you to say that since I did say something about you.

Mr. GRUENBERG. Sure. Only to say I take responsibility for that. I have committed to addressing it and to accepting the recommendations of the report in regard to it. We have been working on this for a number of months now. We are making progress. This new report gives us additional information, and we will address this——

Mr. VARGAS. I still have some doubts, but I will give you some time. Mr. Hsu, you have been dragged into this a bit, and, in fact, at one point, you pointed to a gentleman in the audience. I believe he is probably your attorney. Could you point to your attorney? I believe at one point he asked you not to answer a question because of some reason. Is that correct?

Mr. HSU. I want to be as open and honest with Congress as possible. I also want to follow the law.

Mr. VARGAS. That is right.

Mr. HSU. There are laws related to Privacy Act and others, where I just want to make sure I follow that. That is why I consulted with him.

Mr. VARGAS. I knew that, and that is why I asked you. I am an attorney myself, and that is why I do not want you to get dragged in unnecessarily. Now, there is some responsibility on you, too, and I want to make sure that you take that very, very seriously. Especially, sexual harassment, discrimination should not happen. I mean, I look over there at Vice Chair Barr and I have to say I have full confidence in him. I know we have had issues here on other things, but I have full confidence in him. I know his background, and I expect that if he had this in his organization, he would do something about it. I hope you have the same attitude as him.

Mr. Barr, I do not have any questions for you now other than, again, I do want to talk later on about the Endgame. I do think that it makes it more difficult for people who are first-time homebuyers to be able to qualify for a mortgage. That is a big deal to me. We will talk later, obviously, about the risks of climate change. It is a big deal to me, but I did want to talk about this. I am a parent too, and I think this is an issue that has to be resolved. Thank you.

Chairman MCHENRY. The gentleman from Georgia, Mr. Loudermilk, is now recognized for 5 minutes.

Mr. LOUDERMILK. Well, thank you, Mr. Chairman, and thank you all for being here today and representing your respective agencies.

It is difficult to have this conversation today, Mr. Gruenberg, but one thing I have noticed, it is troubling to me beyond just this report, and we will get in the report, is one of the things that our local banks, especially smaller banks, tell me is that at one time they felt the FDIC and other agencies were partners with them to help them navigate and make sure that they are compliant with regulation, that regulations made sense, and that both parties worked in the best interest of their customers. They no longer feel that way. They see the FDIC as an adversary, that they are hesitant to ask for advice and this is across the board with a lot of agencies, is that they see it as a "gotcha" organization looking for

a reason to come after them, and it is especially with smaller financial institutions.

So I think that is a broader issue that we have to address, is that our agencies should not be viewed as adversarial but in a partner with institutions. I believe I have been honest in the assessment of the FDIC over the years, both positive and negative. In previous hearings, I have praised some of the informative reports that have come out of the FDIC. However, I must say that I have read the Cleary Gottlieb report, and I am disturbed by the evidence that it presents. Mr. Gruenberg, in the Cleary report, you are quoted as having said that you did not recall specific instances where you were accused of raising your voice, losing your temper, or throwing objects. In your interviews with committee staff, you went a step further and said that you have never yelled at an employee or lost your temper. In fact, you placed the blame on others for misinterpreting your tone and body language.

The Cleary report also noted that you have been unwilling to accept that others have experienced difficult interactions with you. The Cleary report draws on examples of inappropriate conduct dating back to 2007, nearly 20 years ago. You failed to accept responsibility for your behavior for nearly 20 years and only did so reluctantly after public scrutiny. From my perspective, it seems like you had no fear of being held accountable until you were. With these revelations, why should Congress, the public, and your staff trust that you will do better in the future?

Mr. GRUENBERG. Thank you, Congressman. As I indicated earlier, I accept the findings of the report. I am committed personally to addressing them. I am committed to implementing the recommendations made specifically in regard to me and our executives in the report, including having so-called 360 reviews done each year. I understand that employees have experienced my temperament in a way that was disturbing to them. I accept that. That is all that matters. It does not matter what my perception is. It matters what their perception is, and I am committed to addressing that.

Mr. LOUDERMILK. Well, I appreciate that. It seems like maybe that commitment is about 20 years past due, and I think that is the concern that we are having here. The Cleary report also noted that in a 9-year period, 92 complaints were filed, and only two of those complaints resulted in a suspension from the Agency. How can FDIC employees expect their harassers to be held accountable when their leader is not held accountable for his own appropriate behavior?

Mr. GRUENBERG. If I may just add context to that, Congressman. I am not challenging the information in the report, but just to add context, during the period cited there, 2015 to 2023, there were actually 18 employees separated from the Agency, which means they received notices of termination or other disciplinary action. They either left the Agency because of termination, or, in anticipation of disciplinary action, they left or retired, which they have the ability to do, but there were actually 18 individuals separated from the Agency during that time.

Mr. LOUDERMILK. Well, I believe, based on this report, that the hostile work environment at the FDIC is directly related to an in-

ability to take responsibility as a leader. You failed to uphold the integrity of your office by doing the right thing even when no one was watching. Now everyone's watching, and unfortunately, I have no choice but to join in with some of my colleagues in asking for your resignation. With that, I yield back.

Chairman MCHENRY. The gentleman from Illinois, Mr. Casten, is recognized for 5 minutes.

Mr. CASTEN. Thank you, Mr. McHenry. Thanks to all our witnesses here for a long day. This will surprise all of you. I want to talk about climate finance. Before I do that, though, I do not want to pile on. What is the old saying? There is not much that has not been said, but I have not said it.

I share the deep concern of all my colleagues with what happened at the FDIC and the culture that allowed that to happen. I also, as a guy who spent 16 years as a CEO, have sympathy for the loneliness of the corner office, if you will, and how heavy weighs that crown and the responsibility. I also just want to caution all of us on this panel that when we say corporate America would never allow this, they would terminate the leader, this is not corporate America. Those of us on this side of the dais do not have hiring or firing authority with respect to this decision. We do not have the ability to change the culture of the organization. We certainly have the ability to make it politically impossible for you to continue, but we will not be held to account if that is the wrong decision.

I do not read that you were the agent of the problems. I did not see anything there that you have personally harassed or assaulted anybody, or certainly not been convicted of such assaults. I think it is an open question whether your removal would solve the problem, but I just would hope that we would all keep in mind that if we are concerned about the culture, let us not confuse a political scalp with changing culture because finding a new person in that seat is not our job. That is the Senate's and no one would ever accuse the Senate of being a rapid and effective recruiting and hiring manager. It just meets a vacancy.

I want to talk about Basel. Chair Gruenberg, the last time you were here, you and I talked about the concern that I had about this 400-percent increase in risk weighting for tax equity. I think you said at the time that regulators may not have fully appreciated the effect that would have on clean energy. Given the comments, the discussion since, do you at this point support revising those risk weights down for tax equity?

Mr. GRUENBERG. Thank you for the question, Congressman. This is a proposal that is still out for comment. We have not finalized it, so I cannot speak to what we are going to do. Let me simply say we have received a lot of comment. This is an issue that has received a lot of attention by the agencies, and I think we understand the concerns that have been raised.

Mr. CASTEN. Okay. Mr. Barr, there was reporting in Bloomberg last week that final Basel rules might be as soon as August. Would you like to comment on that? Can we anticipate some sense of timing of when we will get clarity on these issues?

Mr. BARR. I appreciate the question. As I indicated earlier, the Bloomberg article did not reflect the reality as I know it on the

ground; that is, we have not made any decisions about the substance. We are still working our way through that. We have made good progress on that. After we are done with that, we will figure out process and timing.

Mr. CASTEN. I want to move on, but the sooner the better. I continue to remain concerned that there are pockets of capital that want to play in this space that are sitting on the sidelines longer than they need to right now, and the sooner we can do that, the better.

Vice Chair Barr, I want to talk a little bit more about the climate scenario analysis that was just done for the Global Systemically Important Banks (G-SIBs). In the report, you mentioned some of the data challenges that banks had modeling physical risks. Can you speak at all to what those challenges were and what, if anything, we need to do to help to get that data?

Mr. BARR. Yes. The banks are, in some ways, at an early stage of trying to understand and measure and manage those risks. One important area, for example, is data about insurance coverage. So some of the institutions for some of their commercial real estate, for example, had some data on insurance coverage but not full data on that coverage across their portfolios. There was a lot of variation across the financial institutions, and, of course, the losses that a bank would suffer are related to the availability of that insurance coverage.

Mr. CASTEN. I am sure you saw the story in the New York Times this week about property and casualty insurers pulling out, not just on the coast, but in my own State of Illinois, because of hurricane or hail risks coming through. As you go through and look at where climate risk is getting into the financial system, I am presuming that the banks once they see the risk will find a way to offload it. In your view, do you have the statutory authority to chase and follow that risk through the system, or do you think your statutory is limited to saying to the G-SIBs, the banks, we have the authority to look at it. If the risk is gone, we do not have to watch it anymore.

Mr. BARR. Well, I would say we have supervisory authority over the banking system. We do monitor risk throughout the financial system.

Mr. CASTEN. I see I am out of time. I want to make sure that if insurers go away and it is left holding the equity and then it falls to property taxes, it is going to come back on our bailiwick. If we need more authority or more direction, let us work with you and follow up offline. I yield back.

Chairman MCHENRY. The gentleman from Tennessee, Mr. Rose, is recognized for 5 minutes.

Mr. ROSE. Thank you, Chairman McHenry, and thanks to Ranking Member Waters for holding this hearing, and thank you to our witnesses for being with us today.

Chair Gruenberg, I know this is not a fun day, but I want to focus on your leadership at the Federal Deposit Insurance Corporation. As the vice chairman of the Oversight and Investigations Subcommittee, it is important that we appropriately understand the damaging implications of the independent Cleary report and your conduct. Yes or no, when an FDIC employee has a legitimate com-

plaint about a colleague mistreating them, is there a formal process for them to file a complaint?

Mr. GRUENBERG. Yes.

Mr. ROSE. That is right, yes. Chairman Gruenberg, it is my understanding that the complaint process is that human resources work with the FDIC legal division to investigate and hold individuals who are accused of being a harasser or a bully accountable. Is that correct?

Mr. GRUENBERG. Yes, Congressman.

Mr. ROSE. What happens, though, when you, Chair Gruenberg, are the bully or the harasser? Having read the report, I can tell you what happens. Your behavior goes unchecked, sadly. Your victims are too afraid to complain to HR. Some are even too afraid to speak to this committee or Cleary investigators and with all who have heard your testimony and watched this hearing today, we have heard how you berated a senior executive and made her feel like she was working in a hostile environment. We have heard how your senior staff fear giving you bad news because you scream at employees.

Chairwoman McWilliams immediately became aware of the cultural issues you created when she started, but in 20 years, you have spent 20 years at the FDIC, you have failed to address any of these issues effectively. Your reign of fear and mistreatment at the FDIC must come to an end, sir. I hope all of the members of this committee join me in saying that correcting harassing and bullying behavior in a toxic workplace cannot be successfully carried out, frankly, by the person responsible for creating these issues in the first place, like you have.

It has become clear to me that based on today's hearing, my reading of the Cleary report, and how you plan to address these issues by, frankly, handpicking your own so-called third-party monitor, it is clearly time, sir, for you to resign. Chair Gruenberg, in terms that I hope you can understand, that I am sure you can understand, I conclude that your chairmanship is insolvent. Thank you, Mr. Chairman. I yield back.

Chairman MCHENRY. Will the gentleman yield?

Mr. ROSE. Yes, I yield to the chair.

Chairman MCHENRY. Mr. Gruenberg, you repeatedly say that you have a process to clean up the Agency, right? You outlined that in some answers. You have not outlined how you intend to clean up your actions, the subject of this report. Can you speak to that?

Mr. GRUENBERG. Yes, Mr. Chairman. As I indicated, I accept the findings of the report in regard to me. I am personally committed to addressing the issues identified——

Chairman MCHENRY. How are you going to address those issues? That is my question.

Mr. GRUENBERG. Well, at the end of the day, it seems to me it is a personal effort on my part to address these issues and also to accept——

Chairman MCHENRY. Describe your effort on your part. The personal piece, describe that.

Mr. GRUENBERG. I think it is incumbent on me to be more sensitive to how my conduct may be received by employees and to un-

derstand the only thing that matters is not my perception but their perception.

Chairman MCHENRY.How long have you been at the Agency?

Mr. GRUENBERG. Since August 2005.

Chairman MCHENRY. How long have you been the leader of the Agency, cumulative?

Mr. GRUENBERG. Well, I became acting chairman in July 2011. I became chairman in 2012, served until 2018.

Chairman MCHENRY. It is 10 years roughly, right?

Mr. GRUENBERG. Approximately.

Chairman MCHENRY. How are you going to convince the people that are reporting your behavior, the problems of your behavior, how are you going to convince them that you are not going to treat them like you have treated them for the last decade?

Mr. GRUENBERG. As the report indicates, I——

Chairman MCHENRY. No, I am asking you, not the report. I have read the report. I am giving you an opportunity to say you are going to seek anger management counseling. Do you intend to do that?

Mr. GRUENBERG. I am happy to—I am certainly——

Chairman MCHENRY. No, no, no, I am asking what you intend to do. I am not trying to convince you in a hearing. I want to hear a plan. You have given us no plan on what you as the head of the Agency are going to do to change your treatment of your direct reports. You have said nothing about that.

Mr. GRUENBERG. The report specifically recommends a 360-review on an annual basis——

Chairman MCHENRY. I know you are talking about to the Agency employees. You have said nothing about what you intend to do about your treatment, which is the subject of most of these questions today. I understand you are going to refer to the report again. I do not need to hear that. I wanted to hear a better answer, and this is a very disappointing answer that you have given. I yield back to the gentleman, and the gentleman's time has expired.

Mr. ROSE. I yield.

Chairman MCHENRY. Thank you, Mr. Rose. I will now recognize the gentlelady from Massachusetts, Ms. Pressley, for 5 minutes.

Ms. PRESSLEY. Thank you, Mr. Chair. The work of the FDIC is paramount in supervising our banks, strengthening our financial system, finalizing important regulations like Community Reinvestment Act, Basel III, and in times of economic crisis, FDIC is even more important. It was just last year when folks in my district, the MA–7, were constantly refreshing the Agency's webpage to see if their money was safe after the failure of Silicon Valley Bank.

The Agency's mission is critical, and there is much work to do. I had initially planned to spend this time discussing regulations and requesting updates from Chair Gruenberg on the timeline for finalizing the rules that stabilize our financial system. However, after reading the recent report into the FDIC's workplace, the public needs answers on the toxic culture of racial discrimination and misogyny that has taken root and festered at the FDIC. Chair Gruenberg, you have failed your staff, people of every walk of life, but especially women employees who have brought their knowledge and their skills to serve at the FDIC. You have failed the American

public who relies on the Agency to work productively and to put forth policies that protect consumers from bank malfeasance.

Now, I have to just consider the source here when it comes to some of the outrage from my colleagues across the aisle because these are the same people who seek to actively defund diversity, equity, and inclusion, who denied and undermined the Me Too Movement, who voted against the Violence Against Women Reauthorization, and who do not want to support finally passing the Equal Rights Amendment. That is why I am truly disgusted by the fact that you have created an opportunity for Republicans who did all of those things to advance their anti-regulation agenda and to use survivors, which I am one of abuse as political pawns. Moreover, there is not one woman on this panel, and I almost walked out just on the strength of that, but the only reason why I did not is because that is a systemic issue here in Congress and often for people who come before this committee. If you do not have one woman in a position of leadership and authority that should be there, then that is also a problem.

But again, the report detailed hundreds of women who experienced harassment with no recourse. For over a decade, the FDIC, under your leadership and your predecessors, ignored them. Chair Gruenberg, in November, in fact, not that long ago, you stated that the FDIC already has "appropriate policies and procedures in place." This is a yes or no question. I am serious. Do you now agree that the policies and procedures in place have been a cataclysmic failure and an affront to the many women who have been harassed, pushed out of the FDIC, and forced to change their career goals and life trajectory?

Mr. GRUENBERG. They have failed, yes, Congresswoman.

Ms. PRESSLEY. "Small," "ashamed," "traumatized," "humiliated," "alone." These are just a few of the words to describe the intense feelings of sexual harassment and what survivors endure. According to the FDIC's own reporting, more than 80 percent of harassment complaints resulted in zero discipline, and when there were repercussions, not a single one resulted in removal, reductions in grade or pay, or any discipline more serious than a temporary suspension. I am so tired of white men failing us. This lack of accountability is a shameful, inadequate, and deeply unsatisfactory, and it is re-traumatizing.

Chair Gruenberg, can you guarantee right now no employee at the FDIC will face any form of intimidation or retaliation for reporting an incident of sexual harassment regardless of confidentiality agreements?

Mr. GRUENBERG. That is our goal, Congresswoman. Yes, the answer to that is yes.

Ms. PRESSLEY. It is shameful that through your inadequate leadership at the helm of this Agency that you have fueled calls for your resignation from the political opportunists across this aisle and jeopardized critical regulations pending finalization at your Agency. Personally, I do not have confidence that you can continue to lead in this role because there is a deficit of trust, and your credibility has been undermined to lead the FDIC through the changes it needs to make to affirm the dignity of the survivors of

harassment, discrimination, and abuse at your Agency. Thank you, and I yield.

Chairman MCHENRY. The gentleman from Ohio, Mr. Davidson, is now recognized for 5 minutes.

Mr. DAVIDSON. I thank the Chairman. I would like to ask unanimous consent to enter the 2018 letter from African American FDIC employees, a letter that the ranking member also received in 2018, into the record.

Chairman MCHENRY. Without objection.

[The information referred to was not submitted prior to printing.]

Mr. DAVIDSON. Mr. Gruenberg, yes or no. Are you aware of a September 2018 letter that Chairman McWilliams received from a group of anonymous African American employees describing discrimination and a toxic workplace that they had experienced at the FDIC?

Mr. GRUENBERG. Yes, Congressman.

Mr. DAVIDSON. This letter described African American employees as being "afraid to speak about issues they faced for fear of repercussions because of the FDIC's culture and claimed this discrimination had persisted since 2001." How long into your chairmanship did you become aware of this?

Mr. GRUENBERG. The letter you referenced was not shared with me until 2022, Congressman.

Mr. DAVIDSON. What actions have you taken to try to address that culture because culture has been bad there, and, presumably, that was part of why you were considered the right person for the job. Now, errors in judgment aside, what have you done to actually positively influence the culture there because much has been made of the things that you have failed to do, and, frankly, some errors and omissions in the past. What could you say that you have actually done to try to address these concerns that were part of the culture that you were brought into shape?

Mr. GRUENBERG. That letter raised a number of issues in regard to the opportunities for African American employees at the FDIC in terms of hiring, retention, promotions. We have had a strategic plan, and it has been a core priority of the FDIC——

Mr. DAVIDSON. I would just say the plan has not worked well. Look, I think I join my colleagues in saying I think that we need new leadership at the FDIC and in a broader of our agencies. It is incredibly disappointing to see the culture, and, frankly, a culture that does not seem like you are the right person. Look, lots of people can find excuses. Leaders find a way, and clearly, you have not found a way to positively influence the culture. If anything, it has gone the opposite direction, so I think it is a real problem for the FDIC.

The work of the FDIC is really important, and when you look at the core mission, the FDIC really has not done well as a regulator. When I look broadly at the three regulators that are here today, there have been a lot of problems in the regulatory space. If you look at Silicon Valley Bank, we had a failure of the San Francisco Fed, we had a failure at the FDIC, and clearly a failure of fiduciary duty by the Board and the leadership of Silicon Valley Bank. When I look at the role of Congress in this, maybe the biggest void is with the Fed because at least we can say that the FDIC and very

clearly the OCC have more control with appropriations. A lot of you have a lot of autonomy to the point where we see things like Operation Choke Point. I do not know whether it is 2.0 or 6.0, but the idea that the Federal regulators are not going after things that are illegal, but things that are just disfavored.

So, Vice Chairman Barr, one of the actions recently is this idea that we are going to designate new things systemically important to financial institutions, nonbank mortgage lenders. Were you part of any of those discussions with Secretary Yellen?

Mr. BARR. Congressman, the Financial Stability Oversight report did not recommend designation as an answer to the problems raised in the report.

Mr. DAVIDSON. Chair Yellen, who is a woman, I will point out to my colleague, the leader of Treasury, is she free range on this? Is that something that you support, that you really believe we should expand the number of Systemically Important Financial Institutions (SIFIs)? Is that supported, or is she kind of out there on her own on that?

Mr. BARR. I have a practice, sir, of not commenting on other public officials. As I said, the FSOC report itself is focused on a set of measures that are designed to improve the resilience of the nonbank mortgage servicer sector, and the report did not suggest that designation was one of those measures at this time.

Mr. DAVIDSON. Thank you for that clarification, and, Director Hsu, I am really concerned about the OCC's role in approving bank mergers. I mean, one of the things that we tried to do with tailoring was to be able to go after appropriate size, fit-for-size regulation. Part of the challenge is, when you look at the biggest banks, there is a wide range between the very biggest banks and the next tier. How do you see mergers and acquisitions appropriately proceeding in that environment because we have essentially artificially capped the ability for the market to function for these banks?

Mr. HSU. Yes. There is no artificial cap. A merger application that fulfills all the statutory factors, being pro-competitive, pro-financial stability, pro-convenience in the needs of the community, will be approved. The question is, what kind of merger comes in and how are all those issues being analyzed and how do they stack up?

Mr. DAVIDSON. I hope that resolves favorably, and I look forward to working with you. Thank you for your time and testimony. I yield back.

Chairman MCHENRY. The gentlewoman from Texas, Ms. Garcia, is now recognized for 5 minutes.

Ms. GARCIA. Thank you, Mr. Chairman, and thank you for the witnesses and their time and attention today. It is always good to see you all.

Let me begin with you, Chair Gruenberg. The Cleary report discussed the 15 recommendations included in the 2020 inspector general report on sexual harassment. That is a 2020 report. A year later, in 2021, the inspector general reported that the same recommendations were closed and addressed. Now, in that inspector general report, some of those recommendations were about this very topic of sexual harassment and workplace environment, were they not?

Mr. GRUENBERG. Yes, that was the subject of the report.

Ms. GARCIA. That was the subject of the report.

Mr. GRUENBERG. Yes.

Ms. GARCIA. So we went through all that up to 2021. Were you chair then?

Mr. GRUENBERG. No, Congresswoman.

Ms. GARCIA. Who was the chair then?

Mr. GRUENBERG. I believe Jelena McWilliams.

Ms. GARCIA. I am sorry?

Mr. GRUENBERG. Jelena McWilliams.

Ms. GARCIA. Ms. McWilliams. Presumably, if there was a culture and there were recommendations made, the inspector general felt like they had been taken care of and it got closed. Is that an assumption that can be made?

Mr. GRUENBERG. They found that the Agency's response to the recommendations was satisfactory from the IG's standpoint.

Ms. GARCIA. Right. Well, I am trying to reconcile that with the fact that on page 88 of the report, it says that the allegations covered the period from 1980s. That is way before the 2020 inspector general report and way before today. Is that true?

Mr. GRUENBERG. Yes, Congresswoman.

Ms. GARCIA. So this culture has been going on for a long time, and apparently the steps taken under the leadership of then Chair McWilliams were either inadequate or the review was inadequate. I am just trying to reconcile what has really happened in terms of timeline. Now the hotline itself—I did not get any detail as to when the incidents occurred, but they talked about sexual assault and unwanted advances, harassment, gender-or sex-based discrimination, workplace bullying, threats. I mean, it goes into a lot of detail over a lot of allegations. So it just really kind of stuns me that something could have been going on since 1980s, but an inspector general may have closed the file in 2021, but now we have all these things, okay?

When I look at the history, you all have had probably since the 80s maybe 12 or 15 different chairmen. You have been acting chairman a couple of times. You are chairman now. When was it that you first really heard—and I do not mean news reports. I do not mean inspector general, but you personally—hear, see, or even feel anything that was inappropriate?

Mr. GRUENBERG. Congresswoman, in terms of the deep-seated workplace culture issues, it was the news reports that came out last year that identified them in a way that——

Ms. GARCIA. So from 2021 when the inspector general closed the report until last year, you had heard zero?

Mr. GRUENBERG. Yes. The 2020 IG report identified shortcomings in policies and procedures and training by the Agency. It made generalizations about workplace culture but did not make the kind of findings that you saw in the news reports last year or——

Ms. GARCIA. Right. Did your board have a committee that dealt with this at all during this time period? I am not talking about the new one that you are creating, but the Board itself. Did you have a committee that dealt with human resources, personnel, personal conduct?

Mr. GRUENBERG. Not a committee devoted to that. That would have been a board responsibility and a management responsibility for the chairman.

Ms. GARCIA. Right. Well, I am just trying to make sense of this. Number one, it is totally disappointing and totally unacceptable. I am just not even sure sometimes how something like this could have existed for so long under so many administrations—we are talking about since the 1980s—and through so many chairmanships but the bottom line is, you are there now. You take full responsibility?

Mr. GRUENBERG. I do.

Ms. GARCIA. You will implement all these programs?

Mr. GRUENBERG. I will.

Ms. GARCIA. Will you enter in some type of self-improvement program as the chairman has suggested?

Mr. GRUENBERG. Yes.

Ms. GARCIA. What might that include?

Mr. GRUENBERG. I think that is something we would have to develop, but certainly coaching or counseling, as well as the 360 review recommended in the report.

Ms. GARCIA. No, I am talking about you yourself, sir.

Mr. GRUENBERG. Yes. I think it is fundamentally an issue for me to address in terms of my personal interactions with staff and be more sensitive to how staff receive interactions with me and ensure that they are appropriate and the only thing that matters——

Ms. GARCIA. Will you take an anger management course?

Mr. GRUENBERG. Yes.

Ms. GARCIA. Okay. Thank you. I yield back.

Mr. STEIL [presiding]. The gentlewoman's time has expired. I now recognize myself for 5 minutes.

Mr. Gruenberg, do you know who Eric Lander is?

Mr. GRUENBERG. No, I am not familiar with him.

Mr. STEIL. He is the former director of the Office of Science and Technology Policy. Do you know who Martin Dickman is?

Mr. GRUENBERG. No, sir.

Mr. STEIL. Dickman was the inspector general for the United States Railroad Retirement Board. If you do not know who either of these are, you may not know what they have in common. Both were either fired or resigned for mistreating their staff. Mr. Lander resigned in February 2022 after reports surfaced that he bullied and mistreated subordinates. Mr. Dickman was subject to an investigation like the one the FDIC just underwent. That investigation found that he created a "toxic work environment and engaged in abusive treatment." Mr. Biden fired him 2 months ago. You probably remember that on the day before his inauguration, President Biden laid out a zero-tolerance policy for this kind of behavior.

Here is a direct quote from President Biden, "If you ever work with me and I hear that you treat another colleague with disrespect or talk down to someone, I will fire you on the spot. No if, ands, or buts." So these two men lost their jobs crossing the line set out by President Biden, but you are still here, even though a thorough review is found that you have done some of the same things. To be honest, I think it is transparent what is happening here. The administration cannot afford to lose you, in particular,

your vote on the Board, which is key to getting the Basel III Endgame done and engaging in an aggressive political agenda.

Let me shift gears and dig into the report briefly here. In the report, it found that you are aggressive. Do you dispute the findings?

Mr. GRUENBERG. I accept the findings, Congressman.

Mr. STEIL. So you accept that you are aggressive to your staff?

Mr. GRUENBERG. I accept the findings in the report. I do.

Mr. STEIL. So you also accept that you are harsh to your staff?

Mr. GRUENBERG. I accept the findings in the report, yes.

Mr. STEIL. You accept that you are vitriolic to your staff?

Mr. GRUENBERG. I accept the findings in the report, Congressman.

Mr. STEIL. You accept that you are disrespectful to your staff?

Mr. GRUENBERG. I accept the findings in the report as you indicate.

Mr. STEIL. Because I think it is important, some of the language that I have heard you use is that people observe you in this way. The report actually finds that you are those terms, and I think there is a big distinction here because it is not in the eye of the beholder as sometimes your terminology has indicated. It is, the report found that you had been aggressive, harsh, vitriolic, and disrespectful to your staff. I think that is why I and others have zero faith in your ability to be an effective leader of the Agency and have called for your resignation.

Let me shift gears and talk about what the Agency is doing, the FDIC under your work, and I want to talk specifically about the role the FDIC should be playing in innovation and the role that it is playing in innovation. Over the last few years, innovative businesses have begun to change the way we bank and for the better. Yet. I have continued to receive complaints about seemingly arbitrary enforcement actions, and I have heard stories from FDIC staff refusing to provide feedback to fintechs on regulatory questions. It has gotten so bad that vice chair, Travis Hill, has said publicly that the perception you have created is the FDIC is "closed for business."

So what are you doing to counter this perception in what we have seen is an aggressive enforcement action as it relates to fintechs? You went from one enforcement in 2021 to 14 in 2023. Is that correct?

Mr. GRUENBERG. I have to check the record on that, Congressman. I do not know offhand.

Mr. STEIL. Well, I will tell you that it is, and do you think that you have an aggressive enforcement action preventing innovation in the fintech space?

Mr. GRUENBERG. I do not think so, Congressman.

Mr. STEIL. Is there a reason for the dramatic increase in the number of enforcements?

Mr. GRUENBERG. I would look into the record. I would say most banks manage third-party relationships, including with fintechs, effectively and well, and they offer useful business opportunities for both. We have had some instances in which those relationships were not managed well by banks in which they overreached and had significant risk management and consumer protection issues.

Mr. STEIL. So what are you doing with the third parties in partnering with financial institutions in meeting compliance obligations before an enforcement action is brought against the banks?

Mr. GRUENBERG. We engage with both parties. As I say, in most instances, banks manage those relationships well. In some instances——

Mr. STEIL. So you would disagree with those that say you have a hostile stance toward fintechs' partner banks?

Mr. GRUENBERG. Yes.

Mr. STEIL. Very nice. I yield back. I now recognize Mr. Torres for 5 minutes for the purpose of asking questions.

Mr. TORRES. Thank you, Chair. Mr. Gruenberg, I appreciated your leadership during Signature. There were 80,000 units of affordable housing that were at risk of losing their affordability, and I felt like you were instrumental in preserving the affordability of those units, but I am deeply troubled by the findings of sexual harassment, racial discrimination at the FDIC, and so I have been struggling to figure out how I should respond. I am curious, imagine for a moment our roles were reversed. Imagine if you were a Congressman on the House Financial Services Committee, and I was the chair of the FDIC, under the cloud of a scandal. Would you call on me to resign?

Mr. GRUENBERG. No, Congressman.

Mr. TORRES. Imagine if you were a Congressman from the Bronx, and one of your constituents approached you—and you know the Bronx well; you were an organizer in the Bronx—and one of your Bronx residents approached you and said, Congressman, why you are not calling for the resignation of an FDIC chair whose Agency has been found to have a pattern of sexual harassment and racial discrimination. What do I tell my constituent?

Mr. GRUENBERG. I would tell them, this is a serious problem. The chairman has recognized it, taken responsibility for it, and is working hard and has been working hard since last year to address it. I think it is important to give him a chance to do that, and interrupting leadership at this point would not advance that objective.

Mr. TORRES. The problem, that issue predates you?

Mr. GRUENBERG. It does, Congressman.

Mr. TORRES. Okay. So it is neither a Democratic nor a Republican issue?

Mr. GRUENBERG. I think that is true.

Mr. TORRES. It is so systemic that it transcends party affiliation?

Mr. GRUENBERG. I think that is true.

Mr. TORRES. I want to ask about Basel III, Vice Chair Barr. On March 6, 2024, I asked Fed chair, Jerome Powell, the following question: how do you reconcile the Fed's repeat reassurances about a well-capitalized banking system with Basel III's assumption of an undercapitalized banking system. The Fed Chair replied with the following answer, "I have said for years in this room that I thought the level of capital in the U.S. banking system is about right." Vice Chair Barr, do you agree with Chair Powell that the level of capital in the U.S. banking system is about right?

Mr. BARR. Thank you, Congressman. I very much appreciate the question. As you have heard me say before and you have heard Chair Powell say before, I am not in the business of commenting

on other public officials' comments. I will say, from my perspective, overall, the banking system is sound and resilient. The capital proposal we put forward is designed to correct particular weaknesses in the approach that we have right now.

Mr. TORRES. I want to interrupt for a moment. Setting aside Chair Powell, do you agree with the assessment that the level of capital in the U.S. banking system is about right? Set aside the source of the quote.

Mr. BARR. Yes. Again, I am not going to comment on that. I will say that with respect to capital in the system, I think the system overall is sound. I am not worried about risks in the banking system beyond those that I have identified but I do think we can do better, and the Basel III approach is about doing better for that.

Mr. TORRES. So when setting capital requirements, there is a tradeoff between safety and soundness on the one hand and capital formation on the other, right? The best regulatory outcome lies not in maximizing safety and soundness to the exclusion of capital formation, nor does it lie in maximizing capital formation to the exclusion of safety and soundness. The best outcome lies in striking an optimal balance between the two.

If you as a banking regulator, you get the balancing act wrong, as you may well be doing with Basel III, it could mean less credit for households and businesses. It can mean less financing for clean energy in an age of catastrophic climate change. It can mean less equity and debt financing for affordable housing at a time when housing costs are a disproportionate driver of inflation. Simply put, the loss of credit is no abstraction, and so can you state with certainty to the public that your Basel III proposal has objectively identified the optimal level of capital in the banking system?

Mr. BARR. Congressman, I do not think anyone can say that on either side of it. The risk of doing too little in this space is that we have another devastating financial crisis that shutters American businesses and harms American households. What we are trying to do is get that balance right.

Mr. TORRES. No, no one disputes the need for safety and soundness, but you could increase capital requirements by 50 percent on the basis of safety and soundness, and in the service of preventing a financial crisis, right? The question is, how do we know with certainty whether we are optimizing the level of safety and soundness and capital formation?

Mr. BARR. I do not think either of us are in the business of certainty, sir.

Mr. TORRES. Well, I see my time is about to expire.

Mr. TIMMONS [presiding]. Thank you. I now recognize myself for 5 minutes. Thank you, Mr. Chairman, and thank you to the witnesses for being here today.

Vice Chair Barr, I am becoming increasingly concerned about rising rates of check fraud, particularly duplicate presentment fraud, which occurs when fraudsters make multiple deposits of the same check. According to recent testimony from the American Bankers Association (ABA), check fraud has become one of the fastest growing categories of fraud across the country. Duplicate presentment fraud has posed exceptional challenges in recent years comprising over one-quarter of all check adjustments handled by the Federal

Reserve in 2022. I feel like technologies should solve this problem. Mr. Barr, would the Fed consider operationalizing the Fed's duplicate check notifier service or explore other technological solutions that can enable real-time fraud detection across all check processing organizations?

Mr. BARR. Thank you for the question. I agree that check fraud is a significant problem. It is one that we are quite focused on. We are looking at various technological ways that we can help but also working with banks as supervisors throughout the system. It is an issue that when I travel around the country, community bankers often raise to me. Really, banks of every size are concerned about this.

Mr. TIMMONS. Is this something that you think technology can play a role in solving or at least reducing substantially?

Mr. BARR. Technology might help. It is not the only answer, but there are technologies we are thinking about that can help in this space, some of which are being deployed in the banking system today.

Mr. TIMMONS. Thank you. Chair Gruenberg, it is made clear in the long-term debt proposal that the specific calibrations of the rule were determined using the current capital framework that the Basel III Endgame seeks to amend, making an accurate assessment of the long-term debt proposal impossible. It seems premature to finalize the long-term debt rules without fully understanding the impacts of Basel III Endgame. While I continue to believe that Basel III Endgame proposed rule should be withdrawn and reissued, would you agree that the agencies should not finalize a long-term debt proposal until banks have a better understanding of the capital requirements they will face under Basel III?

Mr. GRUENBERG. The long-term debt rule was really developed, if I may say, Congressman, independently of the Basel capital rule. It is really designed to create a buffer of long-term debt for institutions over $100 billion that could absorb losses in the event of stress and avoid a failure of the institution or reduce the cost of failure. So it is certainly fair to take into account capital requirements, but I think the debt requirement here really stands separate from that.

Mr. TIMMONS. Would you say that it is unreasonable for this to be implemented if you do not actually know what the result is going to be?

Mr. GRUENBERG. I think we have received extensive comment. I think we have an understanding of what the impact would be. We have not finalized the rule. We are still considering the comments received, but I would not link the long-term debt rule per se with the Basel capital rule.

Mr. TIMMONS. Thank you for that. I have been in Congress for 5-and-a-half, almost 6 years now, and I have not seen the bipartisan calls for anyone's resignation to the extent that I have seen yours. You do not seem to be intending to resign. What are you going to do to change the culture issues that are present at the FDIC?

Mr. GRUENBERG. The Agency has a fundamental challenge. We have been working on them since last year. Fundamentally, we have to break the current culture of a good old boy's network that

is obstructing proper complaints and accountability for misconduct, and I believe the Agency has the ability to do that. As a starting point, we would implement a new independent office reporting directly to the Board that would consolidate all of the functions of reporting, investigating, and holding people accountable for misconduct. Then we have a challenge in addition to our decentralized structure field offices around the country, we have to impose closer oversight and accountability there. If we can do those two things, I believe we can significantly impact the deep-seated issues that have been identified.

Mr. TIMMONS. If there is this culture problem, I am sure that there are ways to have metrics associated with it. You can send out surveys and whatnot. At what point, let us say 6 months from now, 12 months from now, if things have not substantially improved, will you reconsider the calls for you to change leadership?

Mr. GRUENBERG. What we intend to do, and as part of our action plan, is to monitor carefully the implementation of the recommendations and their impact. We have already begun the process of identifying an independent monitor, who would monitor, who would audit the implementation of the recommendations, and engage an expert third-party to advise us on addressing the culture change issues. These were both recommendations of the recent report.

Mr. TIMMONS. My time has expired. I yield back. I now recognize the gentlewoman from New York, Ms. Velázquez.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman. Vice Chair Barr, why did the Fed not move forward with a Notice of Proposed Rulemaking (NPR) on Section 956 last week?

Mr. BARR. Thank you, Congresswoman. We are committed to finalizing a joint rule on Section 956. After discussion with my Board colleagues, we decided that it would be appropriate to have additional analysis done within the Fed, and we are conducting that analysis at this time.

Ms. VELÁZQUEZ. Do you support the need for this rulemaking?

Mr. BARR. I am committed to it, Congresswoman.

Ms. VELÁZQUEZ. When do you expect for this rule for the Fed to join the other regulators?

Mr. BARR. Yes. Unfortunately, I do not have an answer to that. I am consulting with my Board colleagues on the substance of it.

Ms. VELÁZQUEZ. Okay. Can you explain the problem we are trying to solve under Section 956?

Mr. BARR. Yes. Section 956 is designed to address problems with respect to executive compensation that can lead to excessive risk tanking at banks, that ends up causing serious harm to the country.

Ms. VELÁZQUEZ. We should not wait for another Silicon Valley.

Mr. BARR. I agree. Silicon Valley was, in part, a problem of executive compensation that was not well aligned with risk taking.

Ms. VELÁZQUEZ. Do you remember or you recall that this rulemaking was required to be done in April 2011?

Mr. BARR. Yes, that is correct.

Ms. VELÁZQUEZ. All right. Okay. Thank you. Mr. Gruenberg, today's hearing should be an opportunity to discuss the very pressing challenges facing our prudential regulators and the economy as a

whole, but unfortunately, the working environment described in the Cleary Gottlieb report paints a disturbing picture. This includes allegation of sexual assaults and harassment, gender discrimination, workplace bullying, and racial discrimination, and these were not isolated incidents. The report makes clear that these were widespread and long running.

Mr. Gruenberg, I have spent my entire career fighting against these practices in the workplace and in all areas of life. No employee, as I mentioned to you yesterday, should have to work in an environment like this. Yet, this was the reality for more than 500 staffers who were demeaned as they attempted to serve their country through their work. Simply put, the issues outlined in this report must be addressed, and they must be addressed now. To be frank, I am not satisfied by the answers, Chairman, you have given about how you plan to ensure that no FDIC employee has to go through something similar.

The culture of any organization starts at the top. I do not tolerate this in my office. Yet, this horrid working environment has persisted at the FDIC where you served as head for 10 of the last 13 years. As leaders, it is on us to protect our employees and have zero tolerance for this type of behavior. For decades, the FDIC has failed in this basic responsibility. I am seriously questioning my confidence in your ability to change the culture of the FDIC and lead the Agency moving forward. Mr. Chairman, I yield back.

Chairman MCHENRY [presiding]. The gentlelady yields back. We will now go to the gentleman from South Carolina, Mr. Norman, for 5 minutes.

Mr. NORMAN. Thank all of you for appearing today. Mr. Hsu, Michael, would you comment on the fact that September 2022, political activists lobbied the International Organization for Standardization to adopt a merchant category code to track the sale of firearms and ammunition with the stated goal of facilitating and monitoring and reporting of constitutionally protected activities? The goal was to enable government entities to discriminate against both these lawful businesses and their customers despite the fact that individuals have passed a background check. I was very troubled to learn that the Financial Crimes Enforcement Network was pressuring the financial sector to utilize this category code to flag supposed suspicious transactions. Has the Office of the Comptroller of the Currency in any way and been involved in the effort to weaponize firearm specific merchant category codes?

Mr. HSU. Not to my knowledge, no.

Mr. NORMAN. So the Agency has not?

Mr. HSU. Not to my knowledge.

Mr. NORMAN. Do you think it is an appropriate role of the Federal Government to weaponize the financial system and engage in this kind of discrimination against the firearm business?

Mr. HSU. No.

Mr. NORMAN. Do you agree that pressuring the financial sector to reveal the purchasing history of gun owners raises privacy concerns?

Mr. HSU. There are concerns that our role is to ensure the safety and soundness and fairness of the banking system. That is our

focus. We do not believe that the banking system should target particular industries. It has to have a risk basis.

Mr. NORMAN. Okay. I am glad to hear that. I am in the real estate business. The common tsunami is in the office space. The default on loans is going to affect this whole country, not just from coronavirus disease (COVID), but other things as well. The Republicans have been sounding the alarm about the regulatory tsunami that is going to overwhelm the banking industry. They have been asked to implement the new capital 1071, the late fee issue, the Community Reinvestment Act (CRA) rules, as well as other guidance documents issued by the Consumer Financial Protection Bureau (CFPB), which they are not guidance. They are vague and a lot more mandatory than they used to be. "Shall" has been the word used instead of "option," I guess.

Are your agencies considering an impact on banks, and this is for any of you, particularly community banks, on implementing all of these regulations, guidance documents that have been published over the last 12 months. Mr. Barr, do you want to start off?

Mr. BARR. I do think it is important for banks and supervisors to focus on risks to the safety and soundness of the banking system. Like you, we have seen issues in the office commercial real estate space. We are quite focused on making sure that banks have the appropriate risk measurement and management practices in place to address those issues.

Mr. NORMAN. Mr. Gruenberg?

Mr. GRUENBERG. I agree with what Vice Chairman Barr said. I would suggest that the rulemakings that we focused on generally impacted the larger institutions over $100 billion, either for broader financial stability concerns, also specifically responding to the vulnerabilities identified in the bank failures last year. I would say, in regard to the CRA rule, we were particularly sensitive and responsive to actually lightening regulatory burden for the majority of community banks in the United States.

Mr. NORMAN. Any comment?

Mr. HSU. I agree with what my colleagues say. In addition, when I meet with community bankers and they raise these issues, I invite them to engage with us to identify which of those regulations would be most burdensome.

Mr. NORMAN. Mr. Gruenberg, do you agree that the resources like the FDIC believe that the banking sector should be oriented toward profitability and stimulating economic activity rather than unrelated political and social goals? Is it appropriate, in your opinion, for banks to discriminate against lawful commerce such as energy development, mineral extraction, and the firearm industry?

Mr. GRUENBERG. They should not. No, Congressman.

Mr. NORMAN. Okay. You agree with that. I have 23 seconds. Thank each one of you for coming. I yield back, Mr. Chairman.

Chairman MCHENRY. The gentlelady from Michigan, Ms. Tlaib, is now recognized for 5 minutes.

Ms. TLAIB. Thank you, Mr. Chair. Thank you so much. Vice Chair Barr, I think all of us have been eagerly wanting to see 956 being implemented. I mean, I think it has been 13 years, and we already know that this was not a suggestion or a recommendation. It was required by law but Vice Chair Barr, did Greg Becker, the

Silicon Valley Bank's former president and CEO, did he sit on the San Francisco Fed Board before his own bank failed?

Mr. BARR. Yes, Congresswoman.

Ms. TLAIB. Most people are, of course, familiar with the idea of regulatory capture in terms of corruption or the revolving door. These are real issues. Do you agree?

Mr. BARR. I have not seen issues of corruption in the regulatory structure in my experience.

Ms. TLAIB. So the Federal Reserve System is structured such that bank executives hold positions of significant influence and status, correct, on these boards that oversee——

Mr. BARR. The board members of the regional reserve banks play no role whatsoever in supervision. They are prohibited by law from doing that, and under the Federal Reserve Act, banks are elected to the board by statute. That is not something that we just decide to do.

Ms. TLAIB. Okay. Vice Chair Barr, in terms of Fed employees, for instance, working on the proposed rule, how often do they interact with the executive officers from banks?

Mr. BARR. I am sorry. I could not hear the beginning of the question.

Ms. TLAIB. In terms of the Fed employees working on proposed rules, do they often interact with the executive officers from banks because they are over there on these Federal Reserve Banks?

Mr. BARR. Senior staff at the Federal Reserve do receive comment from the banking sector, at staff of all different kinds of levels. Usually, the more senior staff or executive as an organization——

Ms. TLAIB. Yes. I am just trying to figure out why it took 13 years. In terms of Federal Reserve Board of Governors, for instance, to what extent do members' social networks overlap with those bank executives?

Mr. BARR. I do not know the answer to that question.

Ms. TLAIB. Are financial executives commonly part of members' social circles?

Mr. BARR. I do not know.

Ms. TLAIB. Okay. How often do members of Board of Governors of Federal Reserve interact with bank executives at work or personal capacity?

Mr. BARR. That work what?

Ms. TLAIB. How often do members of the Board of Governors of the Federal Reserve system interact with bank executives at their workplace?

Mr. BARR. I often meet with bank executives. It is part of my job. I engage with them as a supervisor and also receive comments from them on our regulatory process. Other members of the Board also regularly interact with them.

Ms. TLAIB. Yes. Again, this is really me trying to figure out what is going on, why 13 years? This might come up, I do not know, maybe because regulators identify with those that they regulate, sharing overlapping social networks, or simply perceive finance executives to have a high intellectual economic status. I mean, I am just trying to figure out if it is all within this circle and folks are

just making decisions based on their social networks, not based on what is required by law.

Mr. BARR. My experience at the Board over the last nearly 2 years is that Board members are trying to do their best to reach a substantive judgment based on their own understanding of——

Ms. TLAIB. So it is going to take 13 years every single time to enforce the law——

Mr. BARR. Obviously, I cannot speak to the 13 years. I am just describing my experience——

Ms. TLAIB. Vice Chair Barr, I believe that you have intention of implementing. I just hope it is soon. Is it going to be 2 months, 3 months, 4 months, before we see actual implementation of Section 956?

Mr. BARR. Again, I cannot commit to a timing. I am doing my best to work with my Board to resolve these issues in a way that is meeting the congressional statutory requirement.

Ms. TLAIB. Chair, we have spoken and you know that I am a survivor myself, my first job outside of college, you know this. I read one of and I tried not to, I needed to see how—I mean, I saw the numbers. I saw the incidents, but one FDIC employee reported to them that she feared for her own physical safety after a more senior colleague who had been stalking her, continued to text her even after she made a complaint against him for, among other things, sending unwelcome sexualized text messages that feature partially naked women engaging in sexual acts. My God, like that. There is more. There is more, Chairman. I told you this, when it happened to me and I told people, they were not surprised. I lasted 5 months because no one did anything.

Chairman, you understand there is no trust right now. Many of the people have been impacted directly from the lack of action, lack of accountability, and this sounds like, I did not know, I did not get it until then. It is a long list. We are not talking about 10, 20, or 30 people. Over 500 people called that hotline. Some of it is even on religious discrimination, on just all these other things but I know as a woman in a workplace, it is that power they put on you, the way that one of them even lured her away to rub on her. I mean, Chairman, this is incredibly serious.

So I just want you to know, I do not know how you do it. I do not know how you build trust among the people that are now relying on you to make sure it never happens again, and I do not know how we heal or address the trauma and really the culture that has been created within just the whole Feds. I mean, this is pretty unbelievable. Thank you, Mr. Chairman.

Chairman MCHENRY. The gentleman from Pennsylvania, Mr. Meuser, is recognized for 5 minutes.

Mr. MEUSER. Thank you, Mr. Chairman. Vice Chair Barr, good afternoon. The QIS, it earlier, that would be released, I believe you said, very soon. Can we get a better idea of when it will be released in that?

Mr. BARR. I do not have a precise timetable. I said relatively soon. I think it will be relatively soon. As I indicated, the staff have gone through a process of cleaning the data and they are doing quality control. When they are done with that, we will release it.

Mr. MEUSER. Six weeks?

Mr. BARR. Again, I do not want to specify beyond what I have said, which is relatively soon.

Mr. MEUSER. Okay, let me ask you this then. In light of the continued inflation, and increasing unemployment and housing issues, commercial real estate effects on banks, and rental prices going through the roof, and credit card debt of consumers at the highest levels, I think, in recorded history, interest rates going to stay at higher levels, I mean, not going to come down with continued inflation, and all the consumer price index (CPI) numbers and everything else, access to capital for small businesses is already very much of a challenge as minimal capital investment taking place within small businesses and large businesses. So the economy is on very thin ice and why would you want to with Basel III, is where I am going with this, put more weight on that ice at a time when things have not improved where, I guess, any way that you have not estimated they would be at this point. My understanding is that you, Fed, probably understood, inflation would be almost under control or at least better than it is right now, and the economy would be a little bit more stable, unemployment will be going up but yet, that has got to factor in your decisionmaking on Basel III, the state of the economy and where the economy is likely going to be in the next 3 or 4 months really not getting better.

Mr. BARR. Thank you, Congressman. Let me say a little bit about the economy and a little bit about Basel III. On the economy overall, inflation has come down over the last 2 years from a high of 7.1 percent to 2.7 percent on a personal consumption expenditures (PCE) basis today. We still have more work to do to get it down to 2 percent. We are cognizant of the effect this has on the economy. It is important for us to be able to achieve that lower inflation in order to have stable employment——

Mr. MEUSER. But the real question is not on the session on the economy—excuse me—but why Basel III with the state of affairs?

Mr. BARR. With respect to Basel III, we are not trying to decide whether a capital rule is appropriate for 3 months from now. We are trying to decide over the long term through the economic cycle what is the right balance of risk and reward tradeoffs in that space. So we are designing for the long——

Mr. MEUSER. It is factoring into your decisionmaking. Can we agree that it is factoring——

Mr. BARR. Pardon me?

Mr. MEUSER. The current affairs, as they are, are factoring into your decisionmaking related to Basel III.

Mr. BARR. We do not think in the short term about the economy. We think over the long term what is the right way of judging the health of the economy.

Mr. MEUSER. All right. So you are going to ignore the state of affairs and just continue ahead based upon other things related to Basel III?

Mr. BARR. We are not at all going to ignore the state of affairs.

Mr. MEUSER. Okay. Okay. So you are not going to ignore it.

Mr. BARR. Our job is to really take all the comments in and to assess those as we are thinking about the——

Mr. MEUSER. That will be good. That will be good. We have talked about this, and that will be good. That is what is very im-

portant, particularly from small business, which does most of the employment.

Mr. BARR. I am happy to follow up with you.

Mr. MEUSER. All right. Great. Thanks. Chairman, I wanted to speak to you today about the business payroll, the Deposit Insurance, but in light of everything else here. Was anyone fired along the course of this situation at FDIC?

Mr. GRUENBERG. We have had four individuals this year.

Mr. MEUSER. Did you fire them?

Mr. GRUENBERG. The Agency issued a termination.

Mr. MEUSER. Lawsuits? Is this going to cost the taxpayer a lot of money in lawsuits? There have got to be lawsuits.

Mr. GRUENBERG. I do not know what recourse individuals may take.

Mr. MEUSER. You do not know? I was secretary of revenue in Pennsylvania. I knew every instance of any trouble whatsoever. You do not know? Then we had 2,500 employees. You got 10,000. That is not that many.

Mr. GRUENBERG. I am simply indicating these four individuals who are separated from the Agency.

Mr. MEUSER. See, that is just unacceptable. I mean, think about it, right? Let me ask you a question. If one of your regional offices you got a report like this or rumors or complaints over the last couple of years at one of your regional offices, would that regional director be held responsible by you? Would you fire him? Would you throw them out as quickly as you could?

Mr. GRUENBERG. We have had changes in four of our regional directors since those reports came out.

Mr. MEUSER. Since the report came out last Thursday?

Mr. GRUENBERG. No, no. I am sorry. The news reports last year.

Mr. MEUSER. Okay. I yield back, Mr. Chairman. Thank you, Mr. Chairman. I yield back.

Chairman MCHENRY. The gentleman's time has expired. We will now go to the gentleman from Wisconsin, Mr. Fitzgerald.

Mr. FITZGERALD. Thank you, chairman. We are obviously all appalled at the findings of the report into the toxic culture at the FDIC. Quite honestly, I cannot believe you are sitting here today before the committee. I thought you would have resigned already. One FDIC employee reported how she feared for her own physical safety, so we are not just talking about the harassment. If you have employees that feel that way, it is far more serious than I think we could even describe here and in the short period of time that we have been given. I mean, you cannot consider the FDIC a good work environment right now for employees, specifically women, do you?

Mr. GRUENBERG. We have a lot of work to do, Congressman.

Mr. FITZGERALD. Would you feel comfortable if your own daughter worked at FDIC?

Mr. GRUENBERG. Yes, and then we have many employees who do have daughters working at the FDIC.

Mr. FITZGERALD. Well, I think I join a long line of Members of Congress that simply wish that you would resign and turn leadership over to someone who may be more competent and have a better handle on the issues within the FDIC.

I have a few questions for some other witnesses. I have been pleased to see that some of my colleagues on the other side of the aisle see the problem with Basel implementation proposal. Rather than going back to the drawing board, some of my colleagues are pushing only for the narrow carve-out from increased capital requirements for green energy tax credits from the Inflation Reduction Act. Mr. Barr, this is directed to you.

So I think you would likely see that there are some tradeoffs necessary to prevent kind of any financial crisis that does not help families likely to obtain a mortgage under the proposal, which is something I have just been personally focused on. However, if such a carve-out is granted to address only one of the many problems in your proposal, while much of it remains intact, what message would that send not just on the independence of the Federal Reserve, but to families who may have more difficulty getting a mortgage, or a small business who would see reduced access to credit, because I feel like that is really at the heart of a lot of issues that have emerged is the lack of the ability of what we considered a wealth builder, which is homeownership and small businesses being able to flourish. I am wondering if you have any comments about that.

Mr. BARR. Thank you, Congressman. We take very seriously the comments that we got on the proposal. We expect to make material changes, broad changes to it. I will say even the proposal, as proposed, would have a very, very small effect on the price of credit in the economy, including with respect to mortgages and small business, but we heard those comments very much. We are looking at the prospect of making changes on all three aspects of the rule with respect to credit, operational risk, and market risk and we are working through the substance of that now.

Mr. FITZGERALD. Do you think the consequences of the merger delays could significantly harm both kinds of acquiring institutions and the targets, which could cause greater operational risk, I guess you could say, whether it is increased costs or even reputational kind of concerns? Do you think, with kind of this prolonged uncertainty, what effect do you think it is having right now?

Mr. BARR. Well, most mergers that we review at the Federal Reserve, the median merger application approval time is in under 2 months, so most mergers go through quite smoothly and easily. We do have much more complex cases often involving larger institutions where either we need to gather more information or there are difficulties in the application itself that have to be worked through, and we have to meet the congressional factors for approval or disapproval. Again, most mergers are pretty straightforward. Some mergers are much more complicated.

Mr. FITZGERALD. If there is something discovered, how do you guys typically handle? Do you circle back then and re-address these concerns or how was that initially kind of addressed, and, ultimately, with the idea of maybe there is an opportunity to kind of make a change to the initial application?

Mr. BARR. Yes, Congressman, there is a lot of conversation back and forth if the application initially presents issues. Those can sometimes be addressed through the process. If there is information lacking, those can sometimes be addressed through the proc-

ess, and at the end of the day, we need to meet the congressional five objectives that are laid out for us.

Mr. FITZGERALD. Very good. Thank you. I yield back, Mr. Chairman.

Chairman MCHENRY. The gentleman yields back. I will now recognize the gentleman from New York, Mr. Garbarino, for 5 minutes.

Mr. GARBARINO. Thank you, Mr. Chairman. Thank you to the witnesses for being here today.

Vice Chair Barr, I would like to follow up on a question that Representative Timmons asked you about the interaction between the long-term debt and the Basel III Endgame proposals. To be direct, do you plan to finalize your Basel proposal before you finalize the long-term debt proposal?

Mr. BARR. We have not made any procedural decisions. As I indicated earlier, we are really focused on the substance, now. we got a lot of substantive comments on both the Basel III Endgame and long-term debt. We are working our way through those. We are looking at the interaction across all of our rulemakings, and we will make a decision on process after we make sure we have landed properly on substance.

Mr. GARBARINO. All right. Given how interrelated these rules are, I think the long-term debt proposal should not be finalized before Basel III Endgame and Basel III needs to be re-proposed with the new notice and comment period as required by the Administrative Procedure Act.

Comptroller Hsu, I know the FDIC, which you sit as a Board member, has looked at changes to passivity agreements. I am concerned about the potential negative impacts these changes could have on access to bank capital, especially at the time of massive changes you are proposing on the Basel front. I am also concerned about jeopardizing investor access to index funds and retail investors are counting on those funds for retirements. Are you concerned about the potential negative impact on bank capital? Is this something that you guys have examined?

Mr. HSU. Thank you for the question. The issue recently came to the FDIC Board for a vote, and there was a very lively discussion of the issues. My view is that those issues warrant careful discussion, deliberation, particularly across the three agencies, to the extent that all three agencies are often involved in ownership issues with banks.

Mr. GARBARINO. So you all discussed the potential negative impact this would have on bank capital?

Mr. HSU. There are a range of views with regard to passivity, and I think that the liveliness of that discussion kind of highlighted how there is stuff we have to work through.

Mr. GARBARINO. Okay. Chairman Gruenberg, do you share those concerns as well?

Mr. GRUENBERG. As Comptroller Hsu indicated, there was a lively discussion at our Board meeting. No conclusion was reached. There were a variety of views, so this is something that I think the Board is going to have to continue to engage on.

Mr. GARBARINO. Back to Vice Chair Barr. I would like to move on to the Fed's proposal to adjust the G-SIB surcharge calculation.

In 2015, when the Fed first issued the surcharge, the Board acknowledged that a bank holding companies' method to score may be affected by economic growth that does not represent an increase in systemic risk. This fact, the Board said it will periodically review the coefficients and make adjustments as appropriate, but to my knowledge, I do not think it has done so yet. Why release a proposal for public comment that omits this important discussion for consideration in your latest proposed rule?

Mr. BARR. Pardon me. We did receive comment on the proposal that went to this question about how to calculate the coefficient. We are looking at that comment along with the other comments we received on the proposal. The proposal also addressed narrowing the buckets of the G-SIB surcharge and avoiding the problem of window dressing, as well as a number of technical adjustments to how we think about calculating the G-SIB surcharge. We are taking all of that comment on board. We are in the process of thinking through that now.

Mr. GARBARINO. So before you released the proposal for public comment, you all discussed the coefficients and whether adjustments would be appropriate?

Mr. BARR. I am sorry. Before we released the proposal?

Mr. GARBARINO. Before, yes. I am just wondering if this was all discussed before you opened it up for additional comment.

Mr. BARR. You know what? I do not think it would be appropriate to talk about internal conversations at the Federal Reserve. I am certainly aware of the issue.

Mr. GARBARINO. Okay. I appreciate that. I am going to run out of time, so I am just going to make a statement here. I would like to follow up with Chairman Gruenberg, and I am going to issue a more detailed question. Hopefully, you will respond to it on what appears to be the FDIC's hostile aggression toward banks who partner with fintechs. I have heard from several banks, and what they have shared with me and what we are witnessing is an overly adversarial regulatory environment that is using enforcement action to discourage banks from partnering with fintechs. I will say that I find this troubling, as I am sure a lot of my colleagues do, as the FDIC's posture will impact the development of what could be innovative products and services that benefit consumers and businesses, especially in New York and around the country. I would have more detailed question that I hope to get a response from you on, but with that, Chairman, I yield back.

Chairman MCHENRY. The gentleman yields back. The gentlelady from California, Mrs. Kim, is recognized for 5 minutes.

Mrs. KIM. Thank you, Mr. Chairman. I know it has been covered by both sides of the aisle, but I want to register my serious concerns with the FDIC's cultural, discriminatory, and moral issues laid out in the Cleary report. Mr. Gruenberg, having heard several of my colleagues already address this and taking that into consideration, I would like to ask you to reconsider and gracefully maybe resign to give the FDIC new respective leadership to enact much-needed internal reforms. You do not need to respond to that, but I want you to reconsider that seriously.

According to Chamber of Commerce letter from February signed by one of the Chamber of Commerce in my city, my district, Yorba

Linda, one of their surveys found that 68 percent of business owners believe that an increase in bank capital requirement would be damaging to their businesses and given the concerns that businesses have with a bank capital increase, I was bothered when I read the May 1 Bloomberg article that made a number of claims of the flaw the Basel III Endgame proposal. One of the claims is that key officials decided to adjust the original proposal rather than start over. Another claim says that you are planning to be done as soon as August. Mr. Barr, given the Fed statement to Bloomberg refuting claims, would it be fair to assume that it was not someone at the Fed leaking it to the reporter?

Mr. BARR. I have no idea why the reporter wrote that. We issued our statement to make it clear that we have made no decisions about procedure. We are very focused on the substance and making sure we get the substance right.

Mrs. KIM. Let me ask you, Mr. Hsu. Do you have any reason to believe it was someone at the OCC leaking the info?

Mr. HSU. No.

Mrs. KIM. What about you, Mr. Gruenberg? Are you aware of who was the source of the claims made in the article? It seems to me that whoever was leaking this information was trying to put pressure on other banking agencies. Is that a fair read?

Mr. GRUENBERG. I cannot speak to the motivations, but I am not aware of who is the source of the information.

Mrs. KIM. Mr. Gruenberg, the Fed is open and actively considering a full re-proposal of the Basel Endgame proposal. Just last month, Chair Powell testified right here in our committee that they are aware of the potential for significant negative economic impact. The Federal Trade Commission (FTC), however, is reluctant to consider a re-proposal and is pushing for it to be finalized. Do you think a re-proposal is appropriate, and where do you stand on the benefits of a re-proposal?

Mr. GRUENBERG. I think as Vice Chair Barr indicated, the three agencies right now are focused on trying to reach agreement on the substance of a rulemaking and the decision on process going forward. I think we will have to decide after we reach closure on the substance, so I think it is, candidly, an open question at this point.

Mrs. KIM. Well, I am going to switch to another topic here. What is the average time for issuing reports of examination following the date of the exit meeting, and how does this differ for those banks that are active in FinTech space? Question to you, Mr. Gruenberg.

Mr. GRUENBERG. I will be happy to get back to you on that question, Congresswoman. I just want to check on the particular record to give you accurate information. I am happy to do that.

Mrs. KIM. I am concerned by the disproportionate enforcement actions on fintechs and about what that can do to give the customers' opinions, options, and access to innovation, so I would urge regulatory parity for innovators. Mr. Barr, in your testimony, you mentioned that the Fed continues to work to improve the discount window tool. Can you give us some thoughts about how you are thinking about improving it?

Mr. BARR. Thank you very much for the question. Liquidity provision by the Federal Reserve has been an absolute bedrock for the financial system. Since the founding of the Federal Reserve, it did

provide the underpinning for the Bank Term Funding Program and discount window borrowing last spring, but what we have heard from a number of banks is that there are procedural issues and they are working with the discount window, that could be improved. We are going to get more systematic impact from banks about those issues. One of the areas that, for example, we are working on is that banks said it would be good to have an online portal. So we have started having an online portal to engage with the banks——

Mrs. KIM. We had this conversation when you came before our committee before too, right? I would ask you to look into the stigma that was associated with the use of the discount window and its limited operations with institutions working on the East Pacific Time Zone, like where I am from. Thank you, and my time is up. Thank you.

Chairman MCHENRY. The gentleman from Nebraska, Mr. Flood, is recognized for 5 minutes.

Mr. FLOOD. Thank you, Mr. Chairman. Acting Comptroller Hsu, you have spoken a few times in the last year about the separation of banking and commerce. From an activity's perspective, can you expound on where that line is? Specifically, I want to know from you, where do payment activities fall on the banking and commerce spectrum?

Mr. HSU. Sure. I think one way to think about it is banking consists of three services that are bundled together: facilitating payments, making loans, and taking deposits. Essentially, when banks are chartered, those are three activities that are bundled within the bank. When payments become unbundled from that on its own, that is commerce. That is not banking. What is happening sometimes is that those payment activities that get unbundled are sometimes being re-bundled outside of the bank perimeter that, to me, starts to approximate banking outside of the bank regulatory perimeter, and it warrants monitoring.

Mr. FLOOD. Can you give me an example of re-bundled?

Mr. HSU. Sure. So a payments company may start off providing payment services that are very narrowly defined as payment services, and then over time, it would say we can hold your cash as if it is a deposit and provide it with yield. Then we can also offer a loan, though that re-bundling of services looks awfully similar to banking.

Mr. FLOOD. Thank you very much. Let me pivot quickly to bank fintech partnerships. I am going to direct these questions to Chairman Gruenberg. I have stated in this committee previously that I feel bank fintech partnerships are important. I represent a rural state. We have mostly all community banks, very few regionals, very few—no G-SIBs. I mean, there are connections there, but I worry about these bank fintech partnerships not being available to community banks and only the largest banks in the Nation. I understand that sometimes a partnership with a fintech firm can introduce new risks, and I appreciate that there needs to be some framework for oversight of that. However, I have heard that in some cases, examiners are interpreting the new interagency guidance on this topic is more of a one-size-fits-all checklist.

So here is the question, Mr. Chairman. The broad application of regulations under the third-party risk guidance and Novel Activities Program has raised some concerns among stakeholders that regulators might be pushing to reduce or even dissolve existing bank fintech partnerships in favor of some more traditional banking operations. Is this a misinterpretation of the FDIC's intentions? If it is, would you please clarify what your intentions are and whether or not your agency supports banks partnering with financially sound and compliant financial technology companies?

Mr. GRUENBERG. Thank you, Congressman. Candidly, I think it is a misinterpretation. As I indicated in response to a previous question, most banks manage third-party relationships, including third-party relationships with fintechs, in an appropriate way. They have met risk management responsibilities. If that third party is undertaking services provided by the bank as well as consumer protection obligations, most banks manage those well and we are supportive of them. There are a few instances in which some banks have overreached, quite frankly, and gotten themselves into some difficulty, as you indicate, and then it becomes a matter of supervisory attention but as a general matter, we are supportive of those relationships as long as they are managed appropriately and take into account the guidance that you referenced.

Mr. FLOOD. Thank you. Chairman Gruenberg, on June 6, 2023, the Federal Reserve, the FDIC, and the OCC issued final guidance regarding risk management expectations for banks partnering with fintechs. While prior third-party risk management guidance included supplemental materials published close to the finalization date, there was a delay in issuing an aid specifically tailored to aid the community banks in complying with this June 2023 guidance. Can you explain the reasons for that delay?

Mr. GRUENBERG. Not offhand, Congressman. I will be glad to get back to you in regard to that.

Mr. FLOOD. Thank you very much.

Mr. FLOOD. With that, I yield back.

Chairman MCHENRY. The gentleman yields back. I would like to thank the panel for their testimony. I think there have been some notable calls, Mr. Gruenberg, for you to reappear before the committee from my Democrat colleagues. I will consult with the minority party on the committee about that and I want to thank all of you for your testimony today. These are important positions. The focus should not just be on cleaning up mismanagement, but it should be about the safety and soundness of our financial institution. I am glad that is of bipartisan concern.

Without objection, all members will have 5 legislative days within which to submit additional written questions for the witnesses to the chair. The questions will be forwarded to the witnesses for response. I ask our witnesses to respond no later than June 15.

[The information referred to can be found in the appendix.]

Chairman MCHENRY. Without objection, the committee is adjourned.

[Whereupon, at 1:32 p.m., the committee was adjourned.]

APPENDIX

MATERIALS SUBMITTED FOR THE RECORD

For Release on Delivery
10:00 a.m. Eastern
May 15, 2024

Statement for the Record by
The Honorable Todd M. Harper
Chairman, National Credit Union Administration
Before the U.S. House of Representatives
Committee on Financial Services

Oversight of Prudential Regulators

May 15, 2024

The NCUA protects credit union member-owners and the safety and soundness of the credit union system by managing risks to the National Credit Union Share Insurance Fund (Share Insurance Fund). In my testimony today, I will discuss the state of the credit union system, recent efforts by the agency to strengthen the system, and four legislative requests.

State of the Credit Union System

Credit union performance during 2023 was mixed due to increased market competition and rising interest rates. Large, complex credit unions (those with assets greater than $500 million) posted a decline in the aggregate return on average assets stemming from deposit competition and increased use of wholesale funding. In contrast, credit unions with assets less than or equal to $500 million in assets have a more stable deposit base, which mitigates the cost of funding increases. While these credit unions generally experienced some deposit decline, earnings remained stable. Both groups increased net interest margins by reacting to interest rate movements to benefit from higher yields on loans and investments.

In general, credit union liquidity appears to be stable, but the NCUA is seeing signs of stress linked to the current interest rate environment. This financial stress is reflected in the increasing number of credit unions with a composite CAMELS code rating of 3, 4, and 5.[1] Assets in institutions with a composite CAMELS 3 rating increased from December 2022 to December 2023, especially among large, complex credit unions with greater than $500 million in assets.[2] Credit unions with composite CAMELS 4 and 5 ratings remained relatively stable during 2023. Year over year, credit unions with a liquidity component rating of three nearly doubled. Just over three hundred credit unions experienced a decline in the liquidity component rating from a 1 or 2 to a 3, 4, or 5. Additionally, during 2023, the number of credit unions with a high liquidity risk rating tripled.

Credit Union System Performance

As of December 31, 2023, federally insured credit unions' aggregate net worth ratio was 10.95 percent, an increase of 17 basis points over the year. There was continued year-over-year growth in assets and lending, albeit at a slower pace, with the credit union system's total assets surpassing $2.2 trillion and total loans outstanding reaching more than $1.6 trillion. Insured shares and deposits increased slightly during 2023, ending the year almost 1.7 percent higher than one year earlier.

The growing financial strain on credit unions' balance sheets and consumer financial stress due to elevated interest rates and economic uncertainty were more noticeable in the fourth quarter. The delinquency rate for total loans and leases rose to 0.83 percent in the last quarter of 2023, the highest year-end rate in the previous seven years. The delinquency rate on credit cards and automobile loans rapidly increased during 2023, ending the year at 2.11 and 0.90 percent, respectively. It might be noted that the 2.11 percent rate for credit cards was higher than rates

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[1] The CAMELS rating system is based upon an evaluation of six critical elements of a credit union's operations: Capital adequacy, Asset quality, Management, Earnings, Liquidity and Sensitivity to market risk. The CAMELS rating system is designed to consider and reflect all significant financial, operational, and management factors examiners assess in their evaluation of a credit union's performance and risk profile.

[2] 86 FR 72784.

observed during the Great Recession. Additionally, the aggregate net charge-off rate on loans and leases has risen over the last year, climbing to 0.61 percent in the fourth quarter, reaching its highest point since June 2018.

Funding costs for credit unions have increased significantly in the rising interest rate environment. Credit unions have increased their issuances of time deposits, leading to total interest expenses growing substantially over the year. As a result, the industry's return on average assets has declined over the prior year but remains satisfactory at 0.69 percent. Additionally, the industry doubled its credit loss provision expense from $5.5 billion in 2022 to $11.3 billion in 2023. This shift was the combined result of the final implementation of the Current Expected Credit Loss accounting methodology and rising expectations of elevated problem loan levels. Despite the loan deterioration over the year, earnings, net worth, and reserves for credit losses indicate a resilient credit union industry.

External Factors Affecting the System

The NCUA is closely monitoring the economic landscape that credit unions and their member-owners face. Elevated prices and interest rates continue to negatively affect some household budgets, leading to a deterioration in loan performance and rising credit risk. In addition, the prevalence of hybrid work environments continues to strain commercial real estate lending. Overall, the credit union system has modest exposure to this type of lending; however, the NCUA is tracking specific credit unions with material exposure to such loans.

Elevated interest rates and the challenging shape of the yield curve continue to present liquidity and interest rate risks in the credit union system, including at several of the 432 federally insured credit unions with more than $1 billion in assets. Accordingly, the NCUA has emphasized the importance of liquidity risk management and contingency planning in its industry communications. The agency will continue to ensure credit unions conduct liquidity and asset-liability management planning to address current challenges and future uncertainties.

To mitigate potential risks and safeguard the Share Insurance Fund against possible losses, the NCUA will also remain vigilant in monitoring credit union performance through examinations, offsite monitoring, and supervision. Additionally, the NCUA will take necessary action to protect credit union member-owners and their deposits whenever required.

Artificial intelligence (AI), like every new technology, offers both promise and peril. The NCUA's goal is to maximize and deliver on the former while identifying and mitigating the risks of the latter. Consistent with the Executive Order on the Safe, Secure, and Trustworthy Development and Use of Artificial Intelligence, the NCUA is in the early stages of researching, assessing, and developing plans to address opportunities and risks associated with AI tools.[3]

In 2023, the NCUA issued guidance reminding credit unions of their obligation to comply with the Equal Credit Opportunity Act's nondiscrimination requirements in using automated underwriting systems. The NCUA also joined other federal financial regulators to issue a proposed rule about automated valuation models incorporating fair lending principles. While AI allows credit unions to automate certain functions like member communication, fraud detection,

[3] E.O. 14110 of Oct. 30, 2023.

and loan underwriting, it must be used to ensure fairness, transparency, privacy, and consumer protection.

Share Insurance Fund Performance

Backed by the full faith and credit of the United States, the Share Insurance Fund provides insurance coverage for individual accounts at federally insured credit unions of up to $250,000.[4] As of December 31, 2023, the Share Insurance Fund insured $1.7 trillion in share deposits. Notably, the Share Insurance Fund protects nearly 91.4 percent of total share deposits in the credit union system. In comparison, uninsured shares and deposits equaled nearly $161.4 billion at year-end 2023 or 8.6 percent of total share deposits.

The Share Insurance Fund continues to perform well, with no premiums currently expected. As of December 31, 2023, the Share Insurance Fund reported a year-to-date net income of $209.7 million, a net position of $21.2 billion, and an equity ratio of 1.30 percent,[5] which is sufficient but below the 1.33 percent normal operating level target set by the NCUA Board. Given the liquidity events in 2023, economic conditions, and the growing stress in the credit union system from liquidity and interest rate risks, the NCUA Board decided to build up the Share Insurance Fund's liquidity position. The current overnight balance is $5.6 billion. The NCUA Board continues to monitor liquidity in the Share Insurance Fund.

State of the Central Liquidity Facility

Inflationary pressures, elevated interest rates, and liquidity risk all underscore the importance of the NCUA's Central Liquidity Facility (CLF).[6] The CLF is an important tool that acts as a shock absorber when unexpected liquidity events occur.

Under the NCUA's regulations, federally insured credit unions with assets of $250 million or more must establish and document access to at least one contingent federal liquidity source for emergency liquidity as part of their contingency funding plans. This federal emergency liquidity backstop can be the CLF, the Federal Reserve's Discount Window, or both. Credit unions with less than $250 million in assets are not required to have membership with a contingent federal liquidity source; however, they must identify external sources as part of their liquidity policy or provide a written contingency funding plan that is commensurate with their complexity, risk profile, and scope of operations.[7]

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[4] 12 U.S.C. 1751(k) Insured Amounts Payable (3). Separately, a member's interests in all joint accounts at a federally insured credit union are combined and insured up to $250,000. The Share Insurance Fund also separately protects a member's Individual Retirement Accounts and Keogh retirement accounts up to $250,000. The fund is administered by the NCUA. See ncua.gov/files/publications/guides-manuals/NCUAHowYourAcctInsured.pdf.

[5] The equity ratio is the overall capitalization of the Share Insurance Fund to protect against unexpected losses from the failure of credit unions. When the equity ratio falls, or is projected within six months to fall, below 1.20 percent, the Federal Credit Union Act requires the NCUA Board to assess a premium or develop a restoration plan. When the equity ratio exceeds the normal operating level and available assets ratio at year-end, the Share Insurance Fund pays a distribution.

[6] Established by statute, the CLF is a mixed-ownership government corporation created to improve the general financial stability of credit unions by serving as a liquidity lender to credit unions experiencing unusual or unexpected liquidity shortfalls. Member credit unions, which may include both federally insured and non-federally insured credit unions, own the CLF, which exists within the NCUA. The CLF's president manages the facility under the oversight of the NCUA Board.

[7] 12 CFR Part 741.12.

As of December 31, 2023, the CLF had 407 consumer credit union members, providing $20.2 billion in lending capacity. These credit unions range in asset size from less than $50 million to more than $10 billion. The CLF helps protect approximately $370 billion in credit union assets. The more members the CLF has, the more effective it is as a liquidity facility. In December 2022, the CLF had a much greater total membership of 3,673 consumer credit unions with a combined $537 billion in member assets and a lending capacity of $27.5 billion. This rapid decline in membership followed the expiration of the temporary statutory enhancements that provided greater flexibility and affordability to corporate credit unions to serve as agent members of the CLF to cover their smaller credit union members, and that:

- Increased the CLF's maximum legal borrowing authority;
- Permitted access for corporate credit unions, as agent members, to borrow for their own needs; and
- Gave the NCUA Board the clarity and flexibility about the loans it could approve by removing the phrase, "the Board shall not approve an application for credit the intent of which is to expand credit union portfolios."

These enhancements expired on January 1, 2023, resulting in 3,322 credit unions with less than $250 million in assets losing access to the CLF.

To address this expiration and growing liquidity risks, the NCUA Board has unanimously requested that Congress allow corporate credit unions the flexibility to purchase capital stock in the CLF for a subset of their members, to provide their smaller credit union members with access to the facility. The Congressional Budget Office has scored this and the other CLF reforms at no cost to taxpayers.[8]

NCUA's Efforts to Protect and Strengthen the Credit Union System

In the past few months, the NCUA has taken actions to respond to cybersecurity risk; enhance consumer financial protection; support minority depository institutions; improve the credit union system's and the NCUA's diversity, equity, inclusion, and accessibility efforts; and has considered rulemaking activities that strengthen the system.

Enhancing Cybersecurity

Cybersecurity threats within the financial services industry are high and expected to remain so. To maintain vigilance against these threats, the NCUA is ensuring consistency, transparency, and accountability in its cybersecurity examination program and related activities.

The NCUA's recently implemented cyber incident reporting rule has proven helpful to the agency and credit union industry. The final rule requires a federally insured credit union to report a substantial cyber incident to the NCUA as soon as possible but no later than 72 hours after the credit union reasonably believes a reportable cyber incident has occurred. In the first 30 days after the rule became effective, the NCUA received 146 total incident reports, exceeding all previous reporting from the prior year. As of March 2024, the total number of incident reports is just under 1,000. The data collected has significantly improved our capacity to identify trends,

[8] S. 544, 118th Cong., 1st Sess. (2023).

vulnerabilities, and potential risks that could affect the entire sector's cybersecurity. This, in turn, has allowed us to develop strategies to enhance cyber resilience across the board. Moreover, this information will help us to evaluate the effectiveness of current cybersecurity practices among credit unions, leading to more informed regulatory guidance and better mitigation of future cyber risks. More than 70 percent of these incident reports involve third-party providers and credit union service organizations (CUSOs).

The NCUA also actively communicates with credit unions about the increased likelihood of cyberattacks resulting from geopolitical tensions and other cyber events. Credit unions of all sizes are a part of U.S. critical infrastructure and will likely remain consistent targets for certain criminals, as well as our nation's most capable foreign adversaries, and as such, should implement appropriate controls in the technology they use to deliver member services.

Maintaining Consumer Financial Protection

An essential part of the NCUA's mission is to examine credit unions with $10 billion or less in assets for compliance with consumer financial protection laws and regulations.[9] The agency's consumer compliance efforts are integral to ensuring the credit union system remains safe and sound.

In 2024, the agency's consumer financial protection supervisory priorities include overdraft programs, fair lending, and automobile lending, including assessing compliance with Truth in Lending Act requirements and reviewing credit unions' practices related to Guaranteed Asset Protection Insurance. This year, the NCUA is also focusing on credit union compliance with the Flood Disaster Protection Act, including its disclosure requirements.

In addition, the agency continues to review credit union overdraft programs and non-sufficient funds fee practices. Credit union member-owners and the public should have clear visibility into the income a credit union generates from overdraft and non-sufficient funds fees charged to its member-owners. Therefore, beginning with the 2024 first quarter Call Report, the NCUA required federally insured credit unions with more than $1 billion in assets to disclose, separately, income from overdraft and non-sufficient funds fees. These Call Report changes will allow credit unions to benchmark their overdraft programs against other financial institutions. The NCUA's supervision of these services aims to create a more equitable system that supports financial stability for credit union members, improves transparency, and advances the statutory mission of credit unions to meet the credit and savings needs of their members, especially those of modest means.

Furthermore, the NCUA is conducting targeted fair lending examinations at federal credit unions to assess compliance with federal fair lending laws and regulations. These reviews are critical to identifying discrimination and economic equity. In the fair lending examinations conducted in 2023, the NCUA identified pattern or practice of discrimination violations, illegal redlining, indirect lending pricing concerns, systemic Home Mortgage Disclosure Act violations, Regulation B notification and government monitoring information violations, and numerous instances of inadequate fair lending compliance management systems. In 2023, the NCUA referred six credit unions to the Department of Justice for discrimination based on age or marital

[9] 12 U.S.C. 5516(a).

status. These referrals impacted over 55,000 consumers, and associated remediation expenses exceeded $575,000.

In February, the NCUA joined the other Federal Financial Institution Examination Council agencies to issue a statement of examination principles related to valuation discrimination and bias in residential real estate lending. The principles will assess whether credit unions' compliance and risk management practices are sufficient to identify and mitigate discrimination or bias in their residential real estate valuation practices.

As part of its consumer financial protection efforts, the NCUA's Consumer Assistance Center resolves consumer complaints against federal credit unions with total assets of $10 billion or less and, in certain instances, federally insured, state-chartered credit unions. In 2023, the Consumer Assistance Center responded to 12,276 written complaints, 884 inquiries, 35,098 telephone calls, and recovered over $1.1 million in monetary benefits for complaints from consumers and credit unions concerning consumer financial protection regulations.

Finally, the NCUA regularly offers webinars promoting financial education and economic equity. Over the past year, the agency has hosted webinars on cybersecurity and identity protection, the IRS's Volunteer Income Tax Assistance program, appraisal bias, elder financial exploitation, and closing the racial wealth gap and increasing financial equity. The NCUA also released the *Money Basics Guides*, a series of learning tools developed to assist financial educators, credit unions, and other financial institutions with promoting financial literacy in their communities. The guides are also designed to provide consumers with practical skills to manage their money and increase their financial capability. The series includes guides on draft and share accounts, saving and budgeting, and building and maintaining credit. Lastly, the agency participates in national financial literacy initiatives, including the interagency Financial Literacy and Education Commission.

Supporting Minority Depository Institutions

Minority depository institutions (MDIs) play a crucial role in providing safe, fair and affordable financial services to people with modest means, especially minority individuals and communities that have traditionally been underserved by the financial services system. At the end of the fourth quarter of 2023, there were 492 MDI credit unions—about one in ten of all federally insured credit unions—serving more than 6.5 million members and holding assets of more than $88 billion. Although MDIs are typically smaller institutions, with average assets of approximately $181 million, they are solid performers with a return on average assets, net worth ratio, and net interest margin comparable to or exceeding those of credit unions overall.

The NCUA's MDI Preservation Program, in place since 2015, assists in cultivating and sustaining existing MDIs. In 2022, the NCUA launched the Small Credit Union and MDI Support Program to help MDIs with operational challenges such as staff training, examination concerns, and earnings improvement. For 2024, the NCUA is allocating 4,600 staff hours across its three regional offices to support and consult with MDIs.

In the 2023 grant round, 42 MDIs received over $1.4 million in technical assistance grants, a five-fold increase from the previous year. Earlier that year, Congress authorized all MDIs to be

eligible for Community Development Revolving Loan Fund grants and loans. Prior to 2023, MDIs had to meet the low-income credit union designation to qualify. This authorization was not extended in the recent appropriation, and I respectfully request that lawmakers reinstate CDRLF eligibility for all MDIs. MDIs are very small credit unions with average assets of $180 million and, in many circumstances, are supported by unpaid volunteer staff. Due to limited resources, CDRLF grants assist MDIs in remaining competitive by starting a new product or service such as ATMs, online banking, and other products consumers expect from a financial institution.

In addition, the NCUA hosted an MDI Awareness Month in 2023 to showcase the work of these credit unions. Similar efforts will continue in 2024. In October, the agency hosted an MDI Symposium that discussed how it could better serve MDIs, and the NCUA plans to hold a similar event again this year. The NCUA intends to use information from this outreach to further improve its MDI Preservation Program.

Advancing Diversity, Equity, Inclusion, and Accessibility

The NCUA is fully committed to fostering diversity, equity, inclusion, and accessibility (DEIA) within the agency and the credit union system. Through external initiatives like the agency's DEI Summit and internal efforts like employee resource groups, outreach to potential diverse suppliers, and hiring initiatives to promote a diverse pipeline of applicants, the NCUA advances important DEIA principles within the agency and across the credit union system. These efforts are outlined in the NCUA's *Diversity, Equity, Inclusion, and Accessibility Strategic Plan 2024–2026*, released earlier this year.[10] The four strategic goals in this plan will guide the NCUA's efforts and reinforce its commitment to DEIA as a business imperative for the agency and the credit union industry. In doing so, the agency and the broader credit union community will be well-positioned for significant, long-term, and sustainable progress.

As shown in the agency's Federal Employee Viewpoint Survey results, the NCUA draws strength from a broad range of talents and perspectives. The agency uses data from the U.S. Office of Personnel Management's Federal Employee Viewpoint Survey, including the Diversity, Equity, Inclusion, and Accessibility Index, to inform its data-driven DEIA strategies and activities.[11] In 2023, the DEIA index revealed that 77 percent of NCUA respondents reported positive perceptions of agency practices related to DEIA. The government-wide DEIA index average was 72 percent and 76 percent for medium-sized agencies in 2023.

The NCUA also supports workforce diversity, equity, inclusion, and accessibility through its training, outreach and recruitment, special emphasis programs, and employee resource groups (ERG). During fiscal year 2023, ERGs expanded their presence in the NCUA community—41.4 percent of NCUA employees are members of ERGs, putting the NCUA well above the industry-standard ERG membership goal of 10 percent of an organization's total workforce.

In addition, the NCUA routinely recruits employees with diverse backgrounds and seeks to ensure broad applicant pools for vacancies. These diversity recruitment efforts aim to attract and

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[10] NCUA, *Diversity, Equity, Inclusion, and Accessibility Strategic Plan 2024-2026*, https://ncua.gov/files/agenda-items/deia-strategic-plan-2024-2026-20240118.pdf.

[11] U.S. Office of Personnel Management, *Federal Employee Viewpoint Survey*, www.opm.gov/fevs/reports/data-reports/.

retain highly qualified individuals from historically underrepresented groups. The agency continues to build a pipeline of diverse talent in attracting, hiring, and retaining a diverse workforce. Since 2017, the NCUA has consistently exceeded the federal employment rate goals for employees with disabilities and employees with targeted disabilities, with 17.0 percent of individuals reporting disabilities and 4.7 percent reporting targeted disabilities.[12]

The NCUA supports accessibility through its hiring efforts, reasonable accommodations program, Disability Solutions Desk, and Section 508 compliance program. In GSA's 2023 report to Congress on compliance with Section 508 of the Rehabilitation Act of 1973, the NCUA had a maturity level of *Moderate* and a conformance level of *Very High*.[13] In 2024, training, human capital, culture, and leadership will be the agency's focus areas for further improvement in its compliance with Section 508.

The NCUA continues to build a diverse supplier network to obtain innovative solutions and the best value, particularly in technology and information technology solutions. The agency is committed to supporting minority- and women-owned businesses through our supplier diversity program. Diverse suppliers and vendors play a vital role in the economic success of small businesses and diverse communities, and in the success of the NCUA, by bringing in new perspectives and delivering innovation. By fiscal year-end 2023, the agency awarded 47.5 percent of reportable contract dollars to minority- or women-owned businesses. This performance represents a strong, sustained showing for the NCUA and places it among the top performers among federal financial regulatory agencies.

The NCUA also provides credit unions with a diversity self-assessment tool to help measure their progress in applying DEIA principles.[14] Credit unions may assess their DEIA policies and programs through this voluntary credit union diversity self-assessment offered annually. Credit union voluntary self-assessments have no bearing on CAMELS rating and examiners cannot access the data. The NCUA reports credit union diversity data only in the aggregate. The agency encourages credit unions to use this tool to support and evaluate their DEIA efforts and benchmark themselves with peer institutions. Credit unions can use the self-assessment to establish a baseline for action, such as committing to develop new products and services to address the needs of communities of color, increasing investment in underserved areas, and improving community marketing and outreach.

Finally, from July 9-11, the NCUA will host its annual Diversity, Equity, and Inclusion Summit in Minneapolis, Minnesota. This event provides a forum for hundreds of stakeholders to attend workshops, network, share best practices, and meet with leaders on ways to expand DEIA efforts.

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[12] The Office of Personnel Management defines "targeted disabilities" on Standard Form-256, Self-Identification of Disability.
[13] Robin Carnahan, *Message from the GSA Administrator*, U.S. General Services Administration, www.section508.gov/manage/section-508-assessment/2023/message-from-gsa-administrator/.
[14] The NCUA developed the voluntary Credit Union Diversity Self-Assessment in 2016 to comply with Section 342 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which requires certain agencies to assess the diversity and inclusion practices of their respective regulated entities (credit unions, in the NCUA's case).

Rulemaking Activities
In November, the NCUA Board unanimously approved a final rule that adds "war veterans' organizations" to the definition of a "qualified charity" that a federal credit union may contribute to using a charitable donation account. Specifically, the final rule adds a post or organization of past or present members of the Armed Forces of the United States, or an auxiliary unit or society of, or a trust or foundation for, any such post or organization recognized as exempt from taxation under section 501(c)(19) of the Internal Revenue Code to the definition of a "qualified charity" that a federal credit union may contribute to using a charitable donation account. With this final rule, the NCUA took an important step in honoring our nation's many veterans.

In March of this year, the NCUA Board finalized updates to the Interpretive Ruling and Policy Statement that governs the agency's Minority Depository Institution (MDI) Preservation Program for credit unions. MDIs play an important and unique role in promoting the economic viability of minority and underserved communities. Through its MDI Preservation Program, the NCUA engages in a range of efforts to preserve MDIs and foster their success. The MDI Preservation Program is designed to comply with section 308 of the Financial Institutions Reform, Recovery and Enforcement Act of 1989.

The updates included incorporating recent program initiatives, referencing examiner guidance, explaining how the NCUA will review an MDI's designation status during routine evaluations, and adding new subsections on engagement, technical assistance, MDI examinations, Community Development Revolving Loan Fund grants and loans, training and education, and MDI preservation. These changes to the structure and current administration of the MDI Program will better enable hundreds of MDI credit unions to meet the needs of their members and communities.

In addition, the NCUA has begun plans to review credit union records preservation requirements to understand how the agency can update its records preservation program regulations and accompanying guidelines. The NCUA will also be considering a rulemaking to address succession planning in federal credit unions.

Legislative Requests

Certain amendments to the Federal Credit Union Act would allow the NCUA to do its job more effectively and safeguard credit union member-owners, the Share Insurance Fund, and ultimately the taxpayers who back the Share Insurance Fund.

Restoration of Third-Party Vendor Examination Authority
The NCUA's lack of third-party vendor examination authority is a regulatory blind spot that *must* be addressed. Unlike the federal prudential banking regulators, the NCUA lacks the authority to examine credit union third-party vendors and CUSOs. Yet, the risks associated with credit union reliance on third-party services are expanding, increasing the potential for losses to the Share Insurance Fund.

The absence of third-party vendor examination authority limits the NCUA's ability to assess and mitigate potential risks associated with these vendors. Vendors typically decline requests or

refuse to implement recommended actions, exacerbating credit unions' exposure to operational, cybersecurity, and compliance risks that can arise from these relationships. Without the authority to supervise and enforce corrective actions and visibility into these entities, the NCUA cannot effectively protect credit unions and their member-owners.

This regulatory blindspot has already had a negative impact on the industry. Between 2008 and 2015, nine CUSOs contributed to material losses to the Share Insurance Fund, causing losses in 24 credit unions, some of which failed. According to NCUA staff calculations, at least 73 credit unions incurred losses between 2007 and 2020 as losses at CUSOs rolled onto credit union ledgers and led to liquidations.[15] And, last years' third-party core service provider disruption affecting 60 credit unions illuminated the NCUA's challenges as it tried to mitigate issues on behalf of impacted credit unions and their member-owners.

Independent entities such as the Government Accountability Office, the Financial Stability Oversight Council, and the NCUA's Office of Inspector General have identified this deficiency as a significant obstacle to the NCUA's mission to safeguard credit union members and the financial system. All of them have recommended that Congress provide the NCUA with this authority.

Moreover, this lack of vendor authority also impacts the nation's critical economic infrastructure and national security, as the interconnectedness of financial services expands with other industries and national infrastructure, making any exposure potentially perilous. Currently, one in three Americans use a credit union for basic financial services, and there are many credit unions with fields of membership that are tied to high-risk populations such as congressional staff, the U.S. military, the State Department, and members of the U.S. Intelligence Community. Many of these credit unions utilize third-party service providers to provide critical member services and a sophisticated cyberattack against a vendor can have measurable impacts on the personnel who are critical to government operations and national security. By current estimates, roughly 90 percent (or approximately $1.9 trillion) of industry assets are in some way touched or managed by unregulated third-party service providers.

If Congress grants the NCUA examination authority over credit union third-party vendors, risks would be considerably mitigated. Furthermore, credit unions would have access to NCUA examination summaries when conducting their own due diligence of vendors and there would be fewer requests from the NCUA to credit unions to intervene with vendors experiencing problems. If granted this authority, the NCUA would implement a risk-based examination program focusing on services that relate to safety and soundness, information security, cybersecurity, the Bank Secrecy Act and Anti-Money Laundering Act compliance, consumer financial protection, and areas posing significant financial risk for the Share Insurance Fund.

Central Liquidity Facility Reforms

The NCUA Board, as noted earlier, has unanimously supported a proposed statutory change that would restore the ability of corporate credit unions to serve as CLF agents on behalf of a subset of their member credit unions. In the first session of the 118th Congress, lawmakers introduced a

[15] Office of Inspector General, OIG-20-07, "Audit of the NCUA's Examination and Oversight Authority over Credit Union Service Organizations and Vendors" www.ncua.gov/files/audit-reports/oig-audit-cusos-vendors-2020.pdf.

bipartisan bill allowing corporate credit unions to buy CLF capital stock on behalf of a subset of their members. This bill enables corporate credit unions to contribute capital to provide coverage for smaller members with assets under $250 million. As liquidity risks within the credit union system continue to rise, prompt consideration of this bill would help protect the system from future liquidity events.

Additional Flexibility for Administering the Share Insurance Fund

Liquidity risks within the credit union system and rising interest rate risk highlight NCUA's need for flexibility. Therefore, NCUA urges Congress to amend the Federal Credit Union Act to remove limitations on the Share Insurance Fund's equity ratio and ability to assess premiums. This would provide parity with the Federal Deposit Insurance Corporation and enable better fund management.

Specifically, amendments should remove the limitations on assessing Share Insurance Fund premiums when the equity ratio of the fund is equal to or greater than 1.30 percent and if the premium charged exceeds the amount necessary to restore the equity ratio to 1.30 percent.[16] Further, a statutory change should remove the 1.50 percent ceiling for the Share Insurance Fund's equity ratio from the current statutory definition of "normal operating level," which limits the Board's ability to establish a higher normal operating level for the fund.

This approach would prevent credit unions from impairing their one percent contributed capital deposit or paying premiums during times of economic stress. Additionally, these amendments would enable the NCUA Board to proactively manage the Share Insurance Fund using a counter-cyclical approach, creating reserves during economic upswings and ensuring sufficient funds are available throughout economic downturns.

Increase Grant Assistance for the Community Development Revolving Loan Fund

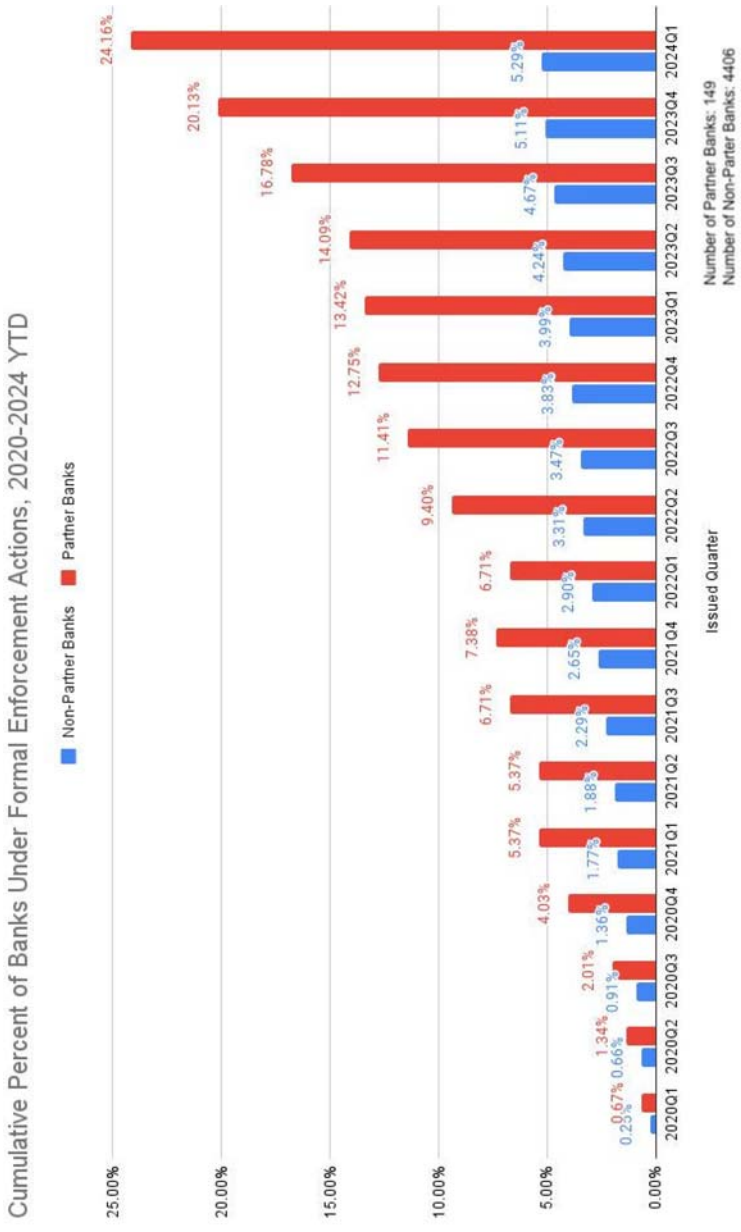
Congress created the CDRLF program to stimulate economic development in low-income communities served by credit unions. Through its stewardship of the CDRLF, the NCUA makes technical assistance grants to eligible credit unions for a variety of initiatives, including, but not limited to, expanding outreach to underserved populations, improving digital services and cybersecurity, staff training, and capacity-building programs. The NCUA requests Congress increase the appropriation for this vital program. Although relatively small in size, these grants make a big difference to low-income and minority credit unions working to provide more and better services to their members and communities. The NCUA does not use appropriated funds to administer the CDRLF program.

Conclusion

The NCUA is prepared to manage the effects of the credit union system's ever-changing economic and business landscape. The agency will continuously monitor credit union performance and collaborate with other federal financial institution regulators to ensure the stability and resilience of our nation's financial services system and economy and to ensure that consumers are protected.

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[16] See 12 U.S.C. 1782(c)(2)(C).



Source: Klaros Consulting (Konrad Alt)

LinkedIn posting

Jang, Jae

From: Bloomberg Government <alerts@bgov.com>
Sent: Wednesday, May 1, 2024 12:24 PM
To: Jang, Jae
Subject: Alert: US Discusses Finalizing Bank Capital Rules as Soon as August

Bloomberg Government

US Discusses Finalizing Bank Capital Rules as Soon as August

- Officials won't scrap draft plan and start over as some wanted
- Move may reduce impact of November elections on effort

By Katanga Johnson / May 1, 2024 12:20PM ET / Bloomberg Government

The Federal Reserve and other top US regulators are forging ahead with their landmark plan to make big banks hold more capital despite calls from some critics to scrap it.

Key officials have decided to adjust the original proposal rather than starting over, and some of them are pushing to finalize it as soon as August, according to people familiar with the matter, who asked not to be identified discussing the internal deliberations. Tossing out the plan released last July would have almost certainly delayed finalization until after the November US elections.

Speculation had been mounting that the Fed, Office of the Comptroller of the Currency and Federal Deposit Insurance Corp. would redo the proposal entirely. Several lawmakers and regulators have raised concerns, while Fed Chair Jerome Powell and Michael Barr, the central bank's top bank regulator, have said they expect "broad and material changes."

Representatives for the Fed, FDIC and OCC declined to comment. Officials at those agencies are still weighing the exact changes that will be made to last July's draft plan and no firm date has been agreed upon for final approval.

Read More: Fed's Powell Says Significant Changes to Capital Plan Likely

Barr, the Fed official who is a chief driver of the effort, said in March that criteria related to operational, market and credit risks could be adjusted. Those measures and others help determine how much capital banks would need to hold under the plan.

Recent Conversations

Recent conversations between senior officials at the Fed, FDIC and OCC have indicated some of the most meaningful changes to the proposal may come in how capital rules assess the level of risk related to a lender's trading, wealth management and investment-banking activities, said some of the people

familiar with the deliberations. Other areas might be addressed in the revised plan and become a focus for officials ahead of its release.

The US effort is tied to the Basel III international agreement that started more than a decade ago after the financial crisis. Supporters have also billed it as a fix for some of the issues exposed by the failures of Silicon Valley Bank and Signature Bank. But banks have argued they are already well-capitalized to withstand a crisis and that the proposed changes would ultimately hurt consumers.

Industry groups have spent months waging a fierce lobbying campaign that has featured appearances by chief executive officers testifying in Congress, television spots during sports games and a barrage of comments submitted against the plan.



Photographer: Anna Rose Layden/Bloomberg
Michael Barr, vice chair for supervision at the US Federal Reserve, left, and Martin Gruenberg, chairman of the Federal Deposit Insurance Corp.

Under the July 2023 proposal, the largest US banks would face about a 19% increase in how much capital they must hold to buffer against losses, with lenders between $100 billion and $250 billion in assets seeing as little as 5% more, according to government estimates.

Although officials are planning notable changes, US administrative law requires that they not depart too significantly from what was proposed. The decision to ultimately move ahead with a version to be based on the original proposal could reduce the impact of a potential consolidation of power in November by Republicans, many of whom have signaled support for the banking industry's arguments.

Fed Critics

Fed Governors Michelle Bowman and Christopher Waller are among the critics who have taken issue with how the original plan assessed various types of risks at banks. It's unclear whether the changes to the original proposal, some of which are still in flux, will allay their concerns.

Read More: Bowman Says Fed's Bank Capital Proposal Needs Big Changes

In a sign that regulators are advancing in their push to finalize the plan, officials are preparing to release as soon as next week a compilation of data from banks on how the changes could affect aspects of their businesses, according to some of the people. That so-called Quantitative Impact Study, which collected year-end 2023 data from the nation's eight largest banks, is supposed to help the Fed weigh the relative costs and benefits of each aspect of the proposed rule and the regulation as a whole.

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OPINION COMMENTARY Follow

The FDIC's Campaign Against Fintech Companies

With no authorization from Congress, the bank regulator tries to suppress these innovative firms.

By Jeb Hensarling

May 9, 2024 5:16 pm ET

Congress created the Federal Deposit Insurance Corp. during the Great Depression to protect Americans' hard-earned money and restore confidence in the financial system. Today the FDIC regulates more than 5,000 banks for safety and soundness, resolves failed banks, and provides standard deposit insurance on individual accounts up to $250,000. As if that isn't enough, its current leadership is attempting to expand its authority to target banks that work with financial-technology companies. The FDIC increasingly wants discretion in deciding where and under what circumstances consumers can obtain loans, financial products and other banking services. Arrogating such power to itself disregards the rule of law, innovation and consumer choice.

Financial-technology companies, or fintechs, are at the forefront of innovation in financial services. Consider Opendoor, which offers a new mobile-device platform to buy and sell homes with a cash offer. Whether such fintechs as Opendoor have built a better mousetrap should be a question for the public, not the government. Yet Washington bureaucrats typically don't welcome innovators, whose companies threaten their power.

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This dynamic doubtless obtains with the FDIC. The fintech business model relies on collaboration with enterprising banks. The FDIC's hostility toward such banks is laid bare by the agency's enforcement statistics. Since January 2023, according to the Klaros Group, more than 25% of the FDIC's formal enforcement actions against institutions have targeted banks with fintech partnerships—though they represent a much smaller percentage of all banks in the U.S.

Earlier this year it forced Lineage Bank of Franklin, Tenn., to terminate all "significant" partnerships with fintechs. The FDIC also determined that New York's Piermont Bank must get written approval from its board before adding new fintech partners. The message is clear: Any bank that goes into business with a fintech company will face the regulatory gauntlet.

It's difficult to read these statistics and conclude that the FDIC isn't trying to bully banks through consent orders and "cease and desist" demands. In doing so, the FDIC is engaged in de facto rulemaking while bypassing the notice and public comment period legally required under the Administrative Procedure Act.

The FDIC's assault on fintech isn't confined to enforcement. The agency in April took the unusual step of submitting a friend-of-the-court brief in a case interpreting Colorado state law. Fintech trade groups have sued Colorado over a law, set to take effect in July, that they say would reduce competition by capping interest rates on loans made by state-chartered banks based in the 49 other states. The law would hit banks with fintech partnerships especially hard because it targets products unique to their firms, such as short-term credit and buy-now-pay-later loans.

Leading the anti-fintech charge is FDIC Chairman Martin Gruenberg, who hasn't tried to conceal his contempt for the industry. In a recent speech, he referred to fintech firms as "shadow banks" while claiming that nonbank lenders fueled the 2008 financial crisis.

The agency's actions are déjà vu. During Mr. Gruenberg's stint leading the agency during the Obama administration, the FDIC joined the Justice Department in a program called Operation Choke Point. The agencies' goal was to deny banking services to businesses they deemed undesirable, such as payday

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effectively put their thumbs on the scale to say with whom banks could—and couldn't—do business.

After significant pushback, the FDIC and Justice Department claimed to have abandoned the program in August 2017. Considering the damage it did to their institutional reputations, one would think the FDIC wouldn't try a similar scheme again. If only.

Mr. Gruenberg hasn't enjoyed smooth sailing since returning to his post. The Journal revealed in a series of articles last fall that the agency has a toxic workplace, with widespread allegations of harassment, discrimination and other offenses. Members of the House Financial Services Committee in November launched an inquiry to evaluate the claims. On Tuesday an audit from the law firm Cleary Gottlieb Steen & Hamilton, commissioned by the FDIC, revealed that more than 500 people—mostly current employees—had reported "experiences of sexual harassment, discrimination, and other interpersonal misconduct" to the firm's hotline.

It isn't implausible that Mr. Gruenberg might be seeking to distract from the agency's scandals by announcing a slew of enforcement actions that please the far-left elements of the Democratic Party. He could use some allies in Congress. Sen. Sherrod Brown (D., Ohio), chairman of the Banking Committee, has been one of the loudest critics of fintechs, accusing the companies of putting "people's hard-earned money at risk" by acting like banks without offering the same level of "consumer protections and safeguards."

Regardless of the motivation, the FDIC's assault on fintechs is part of an alarming trend from the Biden administration. Whether it be the Federal Communication Commission's imposing net neutrality on broadband providers, the Consumer Financial Protection Bureau's imposing price caps on bank fees, or the Federal Trade Commission's banning almost every noncompete agreement in America, government agencies are granting themselves sweeping discretionary powers in constitutionally dubious ways. In so doing, they threaten the rule of law, suppress economic growth and limit consumer choice. That should worry all Americans.

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economics fellow at the Cato Institute.



PHOTO: MANUEL BALCE CENETA/ASSOCIATED PRESS

Appeared in the May 10, 2024, print edition as 'The FDIC's Campaign Against Fintech Companies'.

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FEDERAL DEPOSIT INSURANCE CORPORATION WASHINGTON, D.C. 20429

MARTIN J. GRUENBERG
CHAIRMAN

April 16, 2024

The Honorable Patrick McHenry
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Andy Barr
Chairman
Subcommittee on Financial Institutions
and Monetary Policy
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

The Honorable J. French Hill
Chairman
Subcommittee on Digital Assets, Financial
Technology and Inclusion
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman McHenry, Chairman Barr, and Chairman Hill:

Thank you for your letter of February 2, 2024, regarding the Federal Deposit Insurance Corporation's (FDIC) approach to supervision of institutions engaged in third-party relationships with financial technology (fintech) companies.

The FDIC's core mission is to maintain stability and public confidence in the United States' banking system. The FDIC carries out this mission by, among other things, supervising and examining financial institutions[1] for safety and soundness and consumer protection, insuring deposits, making large and complex financial institutions resolvable, and managing receiverships.

[1] The FDIC is the appropriate federal banking agency for state-chartered banks and savings associations that are not members of the Federal Reserve System and has backup examination authority over FDIC-insured banks and savings associations for which the Office of the Comptroller of the Currency (OCC) or the Board of Governors of the Federal Reserve System (FRB) are the primary federal regulator. 12 U.S.C. § 1813(q). The FDIC also has limited examination authority over affiliates and the provision of certain banking services by third-parties. *See, e.g.,* 12 U.S.C. §§ 1820(b)(4) and 1867(c).

The FDIC neither promotes nor discourages banks from pursuing any particular business lines; doing business with any particular type or class of customer; using any particular technology; or partnering with third parties, including fintech companies – provided that institutions operate in a safe and sound manner and in compliance with applicable laws and regulations.[2] The use of particular technologies or entering into arrangements with fintech companies are business decisions made by bank management based on each institution's unique business model, business needs, risk appetite, and risk management capabilities, among other business considerations. However, an institution's use of third parties does not diminish its responsibility to meet these requirements to the same extent as if its activities were performed by the banking organization in-house. To operate in a safe and sound manner, an institution establishes risk management practices to effectively manage the risks arising from its activities, including from third-party relationships.[3]

The enclosed document contains information prepared by FDIC staff that responds to the specific questions outlined in your letter. While there is no standard definition of the term "fintech company," the FDIC relied on the descriptions ascribed by the banks and companies with which they have relationships in compiling this information.

Your interest in this matter is appreciated. If you or your staff have questions, please contact me or Andy Jiminez, Director, Office of Legislative Affairs, at (202) 898-6761.

Sincerely,

Martin J. Gruenberg

Martin J. Gruenberg

Enclosure

[2] Pursuant to Section 39 of the Federal Deposit Insurance Act, the FDIC has established in Part 364 (including Appendices A and B) safety and soundness standards for all FDIC–supervised institutions.
[3] *See* 88 Fed. Reg. 37920 (June 9, 2023): Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management.

Enclosure: Information Responding To Questions From February 2, 2024 Letter From Chairman McHenry, Chairman Barr and Chairman Hill Regarding Innovation in the Financial Services Sector

1. **Starting in 2021, please provide the number of financial institutions, by year, that were issued a consent order, memo for board review, or subject to any other agreement involving the risk management of third-party relationships with fintech companies.**

The following list includes the number of financial institutions that were issued consent orders, memoranda of understanding, or civil money penalties by the FDIC, by year, and related to issues involving the risk management of third-party relationships.[1] The list also includes financial institutions with board resolutions,[2] which are informal commitments adopted by an institution's board of directors, as well as Section 39 plans,[3] in which bank management submits a Safety and Soundness Compliance Plan that must describe the steps the institution will take to correct deficiencies identified through the supervisory process. While the FDIC is not a party to board resolutions or Section 39 plans, the FDIC monitors bank actions to address the commitments. Data presented below reflect actions related to both safety and soundness and consumer compliance examinations.

Year Issued	Total # of Banks*
2021	1
2022	9
2023	10
2024 (through 1/31/24)	2
Total	**22**

**Eight institutions were subject to multiple enforcement actions during this timeframe; six of these institutions were issued multiple enforcement actions in the same year.*

a. **Please indicate whether the actions were related to the third-party's arrangement with subcontractors or other parties.**

Three of the actions issued by the FDIC address the banks' arrangements with a third party's subcontractors or other parties.

[1] *See* Chapters 2, 4, and 9, FDIC Formal and Information Enforcement Actions Manual. https://www.fdic.gov/regulations/examinations/enforcement-actions/.
[2] *See* Chapter 2, FDIC Formal and Information Enforcement Actions Manual. https://www.fdic.gov/regulations/examinations/enforcement-actions/.
[3] *See* Chapter 10, FDIC Formal and Information Enforcement Actions Manual. https://www.fdic.gov/regulations/examinations/enforcement-actions/.

Enclosure: Information Responding To Questions From February 2, 2024 Letter From Chairman McHenry, Chairman Barr and Chairman Hill Regarding Innovation in the Financial Services Sector

2. **For the financial institutions referenced in Question 1, please provide the following information:**

   a. **the date on which the examination of the financial institution began;**
   b. **the date on which the financial institution received the first copy of findings report; and**
   c. **the date on which the financial institution received a final consent order, memo for board review, or other agreement.**

	2.a. Exam Start Date	2.b. Date Report of Exam Mailed to Bank	2.c. Date Enforcement Action Issued
Bank 1	5/18/2020	7/30/2020	4/28/2021
Bank 2	7/12/2021	12/3/2021	2/24/2022
	10/31/2022	11/28/2023	1/16/2024
Bank 3	8/30/2021	2/16/2022	4/5/2022
Bank 4	11/29/2021	4/7/2022	4/25/2022
Bank 5	9/13/2021	3/9/2022	5/6/2022*
	10/3/2022	6/6/2023	9/20/2023
Bank 6	11/15/2021	5/6/2022	6/6/2022*
Bank 7	3/21/2022	7/26/2022	7/25/2022
Bank 8	10/12/2021	9/30/2022	11/2/2022
	5/3/2021	9/14/2022	3/8/2023
	n/a	n/a	5/11/2023
Bank 9	12/17/2020	10/15/2021	11/14/2022
Bank 10	4/13/2022	11/29/2022	1/23/2023
	4/13/2022	11/29/2022	10/4/2023
Bank 11	4/1/2021	2/15/2023	3/3/2023
Bank 12	10/11/2022	6/9/2023	7/14/2023
Bank 13	2/27/2023	6/30/2023	8/10/2023
	10/18/2021	4/27/2022	4/27/2022
Bank 14	9/14/2022	4/10/2023	4/26/2023
	6/5/2023	9/19/2023	12/18/2023*
Bank 15	3/21/2022	3/17/2023	11/21/2023
Bank 16	6/26/2023	11/17/2023	12/20/2023
Bank 17	4/17/2023	10/27/2023	12/28/2023
Bank 18	1/23/2023	11/21/2023	1/30/2024*

**Two enforcement actions issued.*

Enclosure: Information Responding To Questions From February 2, 2024 Letter From Chairman McHenry, Chairman Barr and Chairman Hill Regarding Innovation in the Financial Services Sector

3. **Please describe how a financial institution's growth impacts the FDIC's decision to begin a board review of the bank.**

The frequency of safety and soundness examinations is governed by law.[4] Examiners review a bank's risk management practices and controls over growth as part of the onsite examination process and consider these factors in rating the bank under the Uniform Financial Institutions Rating System (UFIRS).[5] For example, under UFIRS, capital adequacy is rated, in part, on the prospects and plans for growth, as well as prior experience in managing growth. Further, earnings are rated, in part, on their ability to fully support operations and provide for the accretion of capital and allowance levels in relation to the institution's overall condition, growth, and other factors affecting the quality, quantity, and trend of earnings. Examiners also consider an institution's conformance with the Interagency Guidelines Establishing Standards for Safety and Soundness, Appendix A to Part 364 of the FDIC Rules and Regulations,[6] which also address growth. The Guidelines state, in part, that an institution's asset growth should be prudent and consider: the source, volatility and use of the funds that support asset growth; any increase in credit risk or interest rate risk as a result of growth; and the effect of growth on the institution's capital.

Rapid growth can change an institution's risk profile; institutions that experienced rapid growth have had higher-than-average incidences of failure.[7] The FDIC maintains an offsite review program to track rapid growth and other risk indicators in between examination cycles. Institutions that are flagged by the offsite review program indicators receive follow up reviews, which could, in some instances, result in a supervisory event, such as a visitation or acceleration of a scheduled examination.

The frequency of consumer compliance examinations is governed by FDIC policy. Consumer compliance examination reviews start with a top-down, risk-focused process to comprehensively analyze and review an institution's compliance management system (CMS), which is comprised of two components: Board and Management Oversight; and Compliance Program. These components are evaluated at every consumer compliance examination, regardless of the size of the institution. While the CMS will vary greatly among institutions, the FDIC expects the Board and management of each institution to have a system in place to effectively manage its compliance risk, consistent with the size and complexity of its products,

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[4] Section 10(d) to the Federal Deposit Insurance Act sets forth the requirements for on-site examinations of all insured depository institutions. In general, the appropriate Federal banking agency shall, not less than once during each 12-month period, conduct a full-scope, on-site examination of each insured depository institution. The Federal banking agency may accept a state examination in alternate 12-month periods if the agency determines that the state examination carries out the purpose of Section 10(d). Further, the 12-month timeframe can be extended to 18 months for certain small institutions under $3 billion in total assets that are well capitalized and well managed.

[5] *See* https://www.fdic.gov/news/financial-institution-letters/1996/fil96105.html.

[6] *See* https://www.ecfr.gov/current/title-12/chapter-III/subchapter-B/part-364.

[7] *See* Chapter 1, page 75, History of the Eighties—Lessons for the Future. https://www.fdic.gov/bank/historical/history/3_85.pdf. *See* Chapter 4, pages 119-121, Crisis and Response. https://www.fdic.gov/resources/publications/crisis-response/book/crisis-response-chapter-4.pdf.

services, and markets. Therefore, institutions that experience growth in asset size are expected to implement more robust Board and management oversight to effectively manage increased compliance risk.[8]

An institution's asset size directly impacts the frequency in which the FDIC conducts compliance examinations. Other factors are also considered. Broadly, institutions are subject to more frequent compliance examinations when total assets exceed $350 million as of December 31 for two consecutive calendar years.[9]

Finally, for certain institutions that exhibit elevated or unique risks of consumer harm, the Division of Depositor and Consumer Protection (DCP) implemented a Complex Bank Supervision Program (Program) that employs a continuous supervisory strategy. These institutions often have complex business models, offer nontraditional products or services, and/or rely heavily on third-party relationships. Generally, institutions with assets of $10 billion or more fall within this Program, but the level of supervisory oversight is still dependent on the complexity of the bank's business model.[10]

4. **Please provide all the information disseminated from FDIC Headquarters to the various regional offices regarding the risk management of third-party relationships with fintech companies from 2021.**

The FDIC's Divisions of Risk Management Supervision (RMS) and DCP routinely have discussions with staff regarding industry guidance and emerging issues. For example, in regular staff calls, RMS staff have provided general overviews of the Interagency Third-Party Risk Management Guidance and shared specific observations from examinations of banks' implementation of third-party deposit program relationships and crypto-related activities. In July 2023, as part of a management meeting, RMS provided an overview of an institution's weak risk management implementation of a third-party deposit fintech relationship. In addition, RMS provided training to examiners in October 2023 on the newly issued Interagency Third-Party Risk Management Guidance,[11] including a case study on third-party relationships related to fintechs.

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[8] *See* Section II-1 of the Consumer Compliance Examination Manual, Compliance Examinations – Overview of Compliance Examinations, https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/2/ii-1-1.pdf.

[9] *See* Section II-12 of the Consumer Compliance Examination Manual, Compliance Examinations – Examination and Visitation Frequency, https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/2/ii-12-1.pdf.

[10] *See* Section II-12 of the Consumer Compliance Examination Manual, Compliance Examinations – Complex Bank Supervision Program, https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/2/ii-15-1.pdf.

[11] *See* 88 Fed. Reg. 37920 (June 9, 2023): Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management.

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DCP distributes internal bulletins that provide brief, summarized information to DCP staff regarding the availability of new information, resources, or tools. Since 2021, bulletins issued regarding the risk management of third-party relationships with fintech companies have included: announcements related to all public Financial Institution Letters (FILs), and accompanying interagency guidance and joint statements, as applicable; internal examination resources; and internal webinars; among others.

5. **Please describe how the FDIC enforced infractions related to third-party risk management prior to 2020, and what changes have been made since then and why.**

The FDIC enforced infractions related to third-party risk management in the same way before and after 2020. Infractions related to a bank's risk management of a third-party relationship are enforced in the same manner as if the infractions were incurred directly by the bank.

Since 2008, the FDIC has had outstanding industry guidance making clear that "An institution's board of directors and senior management are ultimately responsible for managing activities conducted through third-party relationships, and identifying and controlling the risks arising from such relationships, to the same extent as if the activity were handled within the institution." The 2008 guidance described that, "The FDIC reviews a financial institution's risk management program and the overall effect of its third-party relationships as a component of its normal examination process. As noted, the FDIC evaluates activities conducted through third-party relationships as though the activities were performed by the institution itself. In that regard, it must be noted that while an institution may properly seek to mitigate the risks of third-party relationships through the use of indemnity agreements with third parties, such agreements do not insulate the institution from its ultimate responsibility to conduct banking and related activities in a safe and sound manner and in compliance with law."[12] The 2023 Interagency Guidance on Third-Party Relationships: Risk Management repeats this messaging, stating, "Whether activities are performed internally or via a third party, banking organizations are required to operate in a safe and sound manner and in compliance with applicable laws and regulations. A banking organization's use of third parties does not diminish its responsibility to meet these requirements to the same extent as if its activities were performed by the banking organization in-house. To operate in a safe and sound manner, a banking organization establishes risk management practices to effectively manage the risks arising from its activities, including from third-party relationships."[13]

[12] *See* Inactive FIL-44-2008, Guidance for Managing Third-Party Risk. https://www.fdic.gov/news/inactive-financial-institution-letters/2008/fil08044a.html.

[13] *See* 88 Fed. Reg. 37920 (June 9, 2023): Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management.

Enclosure: Information Responding To Questions From February 2, 2024 Letter From Chairman McHenry, Chairman Barr and Chairman Hill Regarding Innovation in the Financial Services Sector

6. **Please describe how the FDIC ensures that financial institutions have an independent, fair, and consistent appeals review related to third-party risk management practices.**

Federal statute requires each of the federal banking agencies, including the FDIC, to establish an independent intra-agency appellate process to review material supervisory determinations.[14] The FDIC has issued Guidelines for Appeals of Material Supervisory Determinations (Guidelines) through notice and comment that describe the types of determinations that are eligible for review and the process by which appeals will be considered and decided by the Supervision Appeals Review Committee (SARC).[15] This process allows supervised institutions to obtain review of supervisory determinations by senior-level staff who were not involved in the determinations being challenged, including determinations relating to third-party risk management practices.

The SARC is composed of FDIC Board members or their deputies, which promotes accountability for supervisory decisions. The SARC also includes (as non-voting members) the General Counsel and the Ombudsman, who has a long-standing role as a neutral advocate for a fair process. The FDIC's approach is generally consistent with that of the other federal banking agencies.

7. **Although the FDIC does not have a dedicated innovation office that conducts external outreach, the FDIC has maintained that it still engages with industry participants. Please describe the nature of these engagements, the frequency of them, as well as the FDIC divisions and offices, including positions by title who engage with industry participants regarding specific third-party relationships with fintech companies.**

To ensure the FDIC understands the potential benefits and risks of financial technology and is prepared to address the associated issues that can arise, the FDIC routinely engages with industry stakeholders through a number of channels. For example, the FDIC issues periodic Requests for Information regarding insured financial institutions' current and potential activities involving modern technologies, such as digital assets and artificial intelligence; publishes proposed policy statements and industry guidance for public comment, including the Interagency Guidance on Third-Party Relationships: Risk Management, (issued for public comment in *July 2021*[16] and which, as noted above, was finalized in June 2023) and coordinates with other

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[14] *See* Section 309(a) of the Riegle Community Development and Regulatory Improvement Act of 1994 (Public Law No. 103-325, 108 Stat. 2160).

[15] *See* FIL-53-2022: Guidelines for Appeals of Material Supervisory Determinations, December 13, 2022, https://www.fdic.gov/resources/regulations/appeals-of-material-supervisory-determination/index.html.

[16] *See* 86 Fed. Reg. 38182 (July 19, 2021): Proposed Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2021/07/19/2021-15308/proposed-interagency-guidance-on-third-party-relationships-risk-management; *see also* 88 Fed. Reg. 37920 (June 9, 2023): Interagency Guidance

Federal and state regulatory agencies on financial technology issues. The FDIC has also sponsored financial technology-related conferences and periodically participated jointly with other federal agencies in panel discussions, presentations and meetings with industry representatives.

FDIC staff engages regularly with supervised institutions, which can be through a range of supervisory processes, such as examinations or regular communications between bank management and the FDIC's local field office, regional office, and in some circumstances, the Washington office staff and management, with representation from RMS, DCP, and the Legal Division. Also, the FDIC accommodates ad hoc meeting requests from entities that are not supervised institutions as they may seek to discuss developments, innovations, and technologies in financial services or to better understand the banking regulatory framework. FDIC participants in these meetings range from staff level up through Division Directors, as well as meetings with Board members. The divisions generally represented during these meetings include RMS, DCP, and the Legal Division; however, additional divisional and office representatives may attend as interested or specifically requested.

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on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management..

December 11, 2023

The Honorable Michael S. Barr
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20499

Mr. Michael J. Hsu
Acting Comptroller of the Currency
The Office of the Comptroller of the Currency
400 7th Street, SW
Washington, DC 20219

Re: Comments on Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity, Docket ID OCC–2023–0008, Fed: Docket No. R–1813, RIN 7100–AG64, FDIC: RIN 3064–AF29, 88 Fed. Reg. 64028 (2023) and Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15), Docket No. R–1814, 88 Fed. Reg. 60385 (2023)

Dear Vice Chair Barr, Chairman Gruenberg, and Acting Comptroller Hsu:

Well-functioning derivatives markets are critical for hedging price risks in the agricultural supply chain. We are concerned that recent bank capital proposals will have unintended consequences for the health of US derivatives markets and make hedging significantly more expensive for all market participants. We urge you to reconsider the proposal and avoid taking actions that will harm end-users in the real economy.

Farmers, ranchers and other agricultural producers use derivatives such as futures and options to make sure that they cover their costs of production. On the other side of the market, companies that process agricultural products into food, fiber and biofuels use derivatives to protect their profit margins from a steep increase in their input costs. Both sides depend on well-functioning derivatives markets to hedge their risks.

Central clearing is a core component of derivatives markets. Central clearing reduces counterparty risk and allows end-users to trade these contracts without fear of loss if their counterparty defaults. Central clearing has been a mainstay of the agricultural futures markets for more than a century, and its importance to financial stability and market functioning was validated by the G20 leaders in the aftermath of the financial crisis of 2008.

The strength of central clearing depends, however, on the participation of banks and other institutions as members of clearinghouses. They provide the majority of the financial resources that support the clearing system, and they guarantee the performance of the trades they clear. This is an expensive business, and we are concerned that two recent capital proposals will make it even more expensive.

For agricultural end-users, hedging is like insurance – it is a cost they are willing to pay for protection against price volatility. But not at any price. If the cost of using cleared derivatives rises too high, they will switch to using uncleared derivatives, or simply abandon hedging. Furthermore, there is already a shortage of firms available to provide clearing services to agricultural end-users, and these proposals could reduce the number even more.

According to data from the Commodity Futures Trading Commission, the number of futures commission merchants that clear exchange-traded derivatives for clients has fallen by 50% over the past 20 years. We see a similar trend in the more specialized business of clearing interest rate swaps and other over-the-counter derivatives. In 2014, there were 22 firms clearing these contracts for clients. Today there are 12.

The two recent capital proposals -- the US Federal Reserve GSIB Surcharge Proposal and the US Basel III Endgame Proposal – are likely to have a significant impact on the availability of clearing services in the US. Although the proposals only affect banking organizations – and there are some non-bank financial institutions that provide clearing services – the majority of the clearing firms in the US are banks. According to CFTC data, two thirds of all customer funds in the US clearing system are held by US banks.

There are many types of commercial entities that use derivatives, including asset managers, pension funds, insurance companies, energy producers and auto manufacturers. We are very concerned that any contraction in the availability of clearing services will have a disproportionate impact on agricultural end-users that are far outside the major financial centers, especially smaller entities such as grain elevators and family farms. We urge you to modify the proposals so that they do not disincentivize banks from providing this important service to their customers.

Sincerely,

National Council of Farmer Cooperatives
Commodity Markets Council
National Cattlemen's Beef Association
National Grain and Feed Association
American Farm Bureau Federation
National Milk Producers Federation
National Pork Producers Council
American Cotton Shippers Association
Farm Credit Council

December 11, 2023

The Honorable Michael S. Barr
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
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Mr. Michael J. Hsu
Acting Comptroller of the Currency
The Office of the Comptroller of the Currency
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Washington, DC 20219

Re: Comments on Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity, Docket ID OCC–2023–0008, Fed: Docket No. R–1813, RIN 7100–AG64, FDIC: RIN 3064–AF29, 88 Fed. Reg. 64028 (2023) and Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15), Docket No. R–1814, 88 Fed. Reg. 60385 (2023)

Dear Vice Chair Barr, Chairman Gruenberg, and Acting Comptroller Hsu:

The US economy benefits from having one of the most efficient and productive energy industries in the world. Well-functioning derivatives markets contribute to that success by providing energy producers, refiners, suppliers, and utilities with highly effective tools for managing price risk. This contribution could be threatened, however, by recent proposals to increase bank capital requirements. Those proposals include several provisions that will make it much more expensive for banks to clear derivatives for their clients. We are concerned that this increase in costs will negatively impact our ability to use derivatives to manage our risks.

Energy markets are among the most volatile of all markets in the world. Both supply and demand are subject to sudden shocks, and prices can swing violently from one extreme to another. To protect themselves from this volatility, entities throughout the energy value chain, from oil and gas producers to utilities, participate in the derivatives market to mitigate commercial risk. For producers, a hedging strategy can ensure cost recovery even if prices decline. Moreover, utilities are encouraged to hedge by state and local public utility commissions and boards in order to limit commodity price volatility and protect consumers. Utilities use these hedging strategies to keep the lights and heat on, while maintaining affordability. Similar hedging strategies are employed by manufacturing and transportation companies that use derivatives to protect themselves from volatility in case power or fuel prices suddenly rise.

Futures, options and swaps are the building blocks for this type of risk management. They allow end-users to manage price risk on a wide range of energy commodities, including crude oil, gasoline, heating oil, jet fuel, natural gas and electricity. Most of the risk in the energy derivatives markets is channeled into clearinghouses, also known as central counterparties, through the use of central clearing. But even when an end-user opts out of central clearing, the dealers on the other side of the trade rely on the

centrally cleared markets to hedge their risks. In effect, central clearing provides the foundation for risk transfer in the energy derivatives markets, and by extension, the hedging strategies used by energy producers, refiners and suppliers to protect their businesses from price volatility.

The US Federal Reserve GSIB Surcharge Proposal and the US Basel III Endgame Proposal (collectively, "US Bank Capital Proposals") will make it more expensive for banks to offer clearing to their customers. Although these proposals are not aimed directly at end-users, we believe that the indirect effects will be substantial. This could make hedging unaffordable for many energy end-users, which would expose them to higher risks. Alternatively, if end-users decide to pay more to hedge, the costs will flow through to their customers in the form of higher energy prices.

The increased costs of client clearing also has the potential to harm end-users by reducing the number of banks willing to provide clearing services to end-users in the energy industry. According to data published by the Commodity Futures Trading Commission, the number of firms that provide clearing for exchange-traded futures and options has fallen by 50% during the past twenty years. Of the 47 firms that currently provide clearing for those products, the majority are banks. The proposed increase in capital requirements for these banks seems likely to lead to further consolidation and fewer choices for end users.

The situation is even more dire in the clearing of over-the-counter derivatives. In 2014, there were twenty-two firms that cleared OTC derivatives for clients. Today, there are only twelve, and the top six in terms of market share are US banks that will be directly affected by the proposed increase in capital requirements. Any proposal that puts further pressure on these firms runs the risk of decreasing the availability of clearing services for derivatives, which will negatively impact end-users.

In short, this is already a fragile ecosystem that's necessary to manage customer bills. Current hedging activity shifts the financial risk away from the customer and onto commercial participants that can manage that risk utilizing the hedging tools described above. If the US Bank Capital Proposals are implemented, the result will be a decrease in entities offering clearing services, a decrease in liquidity (which will increase volatility), a decrease in hedging, and an increase in costs to customers, who ultimately bear these costs. We urge the US prudential regulators to consider these concerns before finalizing any significant changes to the capital framework.

Sincerely,

Energy Trading Institute
Electric Power Supply Association
American Gas Association
American Public Gas Association
Commodity Markets Council

The Honorable Michael S. Barr
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

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Dear Vice Chair Barr, Chairman Gruenberg, and Acting Comptroller Hsu:

The American Public Power Association (APPA) and National Rural Electric Cooperative Association ("NRECA") (hereafter "Joint Associations") respectfully submit these comments in response to the Notice of Proposed Rulemaking on Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity (Proposed Rule).

APPA is the voice of not-for-profit, community-owned utilities that power 2,000 towns and cities nationwide. We represent public power before the federal government to protect the interests of the more than 49 million people that public power utilities serve, and the 96,000 people they employ. Public power utilities include utilities owned or authorized by a state, utilities owned by a political subdivision of a state (such as a municipality or utility district), and joint action agencies, joint powers agencies, and similar entities formed to collectively serve other public power utilities.

Public power utilities are load-serving entities with the primary goal of providing the communities they serve with safe, reliable electric service at the lowest reasonable cost, consistent with good environmental stewardship. This orientation aligns the interests of the utilities with the long-term interests of the residents and businesses in their communities.

The National Rural Electric Cooperative Association (NRECA) is the national trade association representing nearly 900 local electric cooperatives and other rural electric utilities. America's electric cooperatives are owned by the people that they serve and comprise a unique sector of the electric industry. From suburbs to remote farming communities, electric cooperatives power one in eight Americans and serve as engines of economic development for 42 million Americans across 56 percent of the nation's landscape. America's electric cooperatives serve 92 percent of all persistent poverty counties in the United States.

Electric cooperatives operate at cost and without a profit incentive. NRECA's member cooperatives include 63 generation and transmission (G&T) cooperatives and 832 distribution cooperatives. The G&Ts generate and transmit power to distribution cooperatives that then provide it to the end of line co-op consumer-members. Collectively, cooperative G&Ts generate and transmit power to nearly 80 percent of the distribution cooperatives in the nation. The remaining distribution cooperatives receive power directly from other generation sources within the electric utility sector. Both distribution and G&T cooperatives share an obligation to serve their members by providing safe, reliable, and affordable electric service.

The Joint Associations have been active participants in previous rulemakings implementing the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). Specifically, NRECA commented on rulemakings related to Capital Requirements of Swap Dealers and Major Swap Participants RIN 3038-AD54 and both APPA and NRECA commented on the Standardized Approach for Calculating the Exposure Amount of Derivative Contracts Docket R-1629 and RIN 7100–AF22; Docket ID OCC–2018–0030; RIN 3064-AE80.

The Joint Associations have members that utilize commodity markets and rely on bilateral physical power and natural gas contracts, and enter energy commodity swaps, options, and futures contracts to hedge commodity supply and price risks. Our members enter these commodity instruments as commercial "end users" seeking to hedge supply risks and minimize price variability, not for purposes of speculation.

Under the Proposed Rule, for an entity entering such a transaction with a large bank to receive a favorable risk weight, the entity must be: (1) investment grade; and (2) publicly traded or the parent entity that controls a company that is publicly traded. Rule makers argued that this would provide "a simple, objective criterion that would provide a degree of consistency across banking organizations." In addition, the proposal states that "publicly traded corporate entities are subject to enhanced transparency and market discipline as a result of being listed publicly on an exchange."

However, we are concerned that the Proposed Rule will make effective risk management more difficult and more expensive for commercial end-users in the energy industry, including our members, without materially improving risk management for the banking sector. Specifically, we believe that the Proposed Rule as drafted will have serious consequences for our members' ability to find regulated counterparties for the forward contracts, commodity trade options, and energy commodity swaps needed to hedge price and supply risks.

Specifically, because our members are not publicly traded, large bank counterparties would face increased capital requirements for such transactions—transactions that we believe do not create more risk to large banks, simply because the bank's counterparty happens to be a cooperative or a government-owned entity. In turn, large banks will be less willing to participate in such transactions or, at a minimum, increase the charges for participating in such transactions to cover the additional costs imposed by the more stringent capital requirements.

Specifically, we believe the Proposed Rule's two-pronged approach to receive a lower 65 percent risk weight for derivatives transactions is flawed and should be removed or reworked substantially. The criteria for publicly traded companies included it the Proposed Rule is a far more restrictive capital requirement than that of the EU and UK capital frameworks, and places American banks – and their customers – at a material competitive disadvantage. We believe this provision should be removed or revised significantly.

In addition, the proposal states that "publicly traded corporate entities are subject to enhanced transparency and market discipline as a result of being listed publicly on an exchange." We believe this too is a flawed argument. The Joint Associations members are community-owned and governed by

democratically elected officials who are required to operate transparently and in the public's best interest and must abide by laws and regulations instituted by multiple layers of government.

We call into question, the suggestion that, as non-publicly traded entities, co-ops, and government-owned entities are fundamentally more of a credit risk due to their ownership structure. Because co-ops are consumer-owned and operate at cost, it is in the best interests of the co-op to fulfill its financial obligations in the most cost-efficient, risk-averse manner possible. Public power providers operate in a similar vein and are accountable to the communities they serve. There is a reason why more than half of all public power utilities have been in operation for a century or longer – and more than three-quarters have been in operation since World War II.

On the other hand, publicly traded companies operate to maximize shareholder return and it can be argued that this type of ownership structure is vulnerable to the short-term interests of shareholders and shareholder returns at the expense of the firm's long-term financial viability and operation.

If the proposal's bias against non-public traded companies, cooperatives, and government-owned entities is left intact, we believe it will severely and needlessly disrupt the ability of our Joint Association members to participate in risk management hedging transactions with large banks. Adopting precedents in federal law that cooperatives, government-owned entities, and other non-publicly traded companies are less creditworthy and more risky than publicly traded companies is also dangerous and unwarranted.

We ask for you to consider the comments above and revise the Proposed Rule accordingly so that our members can continue to manage commodity risks by using hedging instruments without undue cost or complexity. If the Proposed Rule is adopted as drafted, we fear that there will be a decrease in hedging, increased costs to our consumer members, and increased market volatility in the energy sector, which is already facing many uncontrolled externalities. We urge the US prudential regulators to consider these concerns before finalizing any significant changes to the capital framework.

John Godfrey
Senior Government Relations Director
2451 Crystal Drive, Suite 1000,
Arlington VA 22202

Paul Gutierrez
Legislative Affairs Director
4301 Wilson Blvd
Arlington, VA 22203

February 28, 2024

The President
The White House
Washington, DC 20050

Dear Mr. President:

The undersigned chambers of commerce and businesses across the United States are concerned about the proposed rule known as the "Basel III Endgame" that would substantially increase capital requirements on covered U.S. banks and make capital and credit more expensive for businesses of all shapes and sizes. Small and mid-size businesses, who are the drivers of economic growth, are more reliant on bank financing than other sectors of the economy. If enacted, the Basel III Endgame rule would make financing prohibitively expensive for businesses in the midst of an already challenging environment.

We ask that you urge federal banking regulators to study the costs of and then repropose the Basel III Endgame rule given it stands to hamstring access to capital and credit, the essential lifeblood that fuels the vitality of every business.

A recent Chamber survey of 300 treasurers and financial decision-makers revealed that **68%** of business owners believe that a net increase in bank capital requirements could be detrimental to their business. Furthermore, the survey found that an alarming **87%** of businesses have been negatively impacted by cost increases resulting from financial regulation, including **46%** of companies that have delayed or canceled planned investments or capital expenditures due to financial regulations.[1]

Small businesses could see the most adverse impacts under the Basel III Endgame rule. Notably, companies that are not publicly traded are disproportionately affected through higher assigned risk weights relative to publicly traded competitors, despite similarly strong credit quality, requiring banks to hold additional capital on the loans made to small businesses. Approximately 99 percent of all U.S. companies are privately held and employ roughly half of all private sector employees. One of the main reasons small businesses take on loans is to hire and retain workers. Higher capital requirements will likely lead to increased borrowing rates for privately held businesses, hurting their ability to hire workers and make investments. These costs could in turn be passed on to consumers and put downward pressure on economic growth and employment. Other parts of the rule, particularly the capital requirement for operational risk, will also have adverse downstream impacts on small businesses' ability to access credit and wealth management services.

Policymakers must carefully consider the potential adverse effects of the Basel III Endgame rule, especially for the small business customers of banks. We implore policymakers to refrain from advancing a rule that will further constrain small businesses and further complicate an already challenging economic environment.

Thank you for your consideration and we stand ready to discuss these issues in greater detail.

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[1] U.S. Chamber of Commerce, How Business Views Financial Challenges: Basel III & Beyond (October 2023), https://www.uschamber.com/assets/documents/CCMC_Survey-FinancialChallenges_Fall2023.pdf

Sincerely,

National

The U.S. Chamber of Commerce

Alabama

Business Council of Alabama

Arizona

Apache Junction Area Chamber of Commerce
Arizona Chamber of Commerce & Industry
Chandler Chamber of Commerce
Greater Flagstaff Chamber of Commerce
Greater Phoenix Chamber
Lake Havasu Area Chamber of Commerce
Mesa Chamber of Commerce
Nogales-Santa Cruz County Chamber of Commerce
Queen Creek Chamber of Commerce
Tucson Metro Chamber

California

Antelope Valley Chambers of Commerce
Buellton Chamber of Commerce
California Business Roundtable
Carlsbad Chamber of Commerce
La Verne Chamber of Commerce
LA Area Chamber of Commerce
Long Beach Area Chamber of Commerce
Murrieta/Wildomar Chamber of Commerce
Oceanside Chamber of Commerce
Palos Verdes Peninsula Chamber of Commerce
San Francisco Chamber of Commerce
Silicon Valley Leadership Group
Simi Valley Chamber of Commerce
Torrance Area Chamber of Commerce
Yorba Linda Chamber of Commerce

Colorado

Vail Valley Partnership

Delaware

Delaware State Chamber of Commerce
The New Castle County Chamber of Commerce (Delaware)

District of Columbia

DC Chamber of Commerce
Independent Petroleum Association of America

Florida

Florida Chamber of Commerce

Georgia

Georgia Chamber of Commerce
Metro Atlanta Chamber

Idaho

Boise Metro Chamber of Commerce
Jerome Chamber of Commerce

Illinois

Chamber630
Edwardsville/Glen Carbon Chamber of Commerce
Greater Rockford Chamber of Commerce
Joliet Region Chamber of Commerce & Industry
The Greater Springfield Chamber of Commerce
West Suburban Chamber of Commerce & Industry

Indiana

Indiana Chamber of Commerce
South Bend Regional Chamber

Iowa

Quad Cities Chamber of Commerce

Kansas

Greater Topeka Chamber

Kentucky

Greater Louisville Inc. - The Metro Chamber of Commerce
Kentucky Chamber of Commerce

Maine

Barry County Chamber and Economic Development Alliance

Maryland

Harford County Chamber of Commerce
Maryland Chamber of Commerce

Michigan

Battle Creek Area Chamber of Commerce
Detroit Regional Chamber
Michigan Chamber of Commerce
Oscoda AuSable Chamber of Commerce

Minnesota

Minneapolis Regional Chamber
Minnesota Chamber of Commerce
St. Paul Area Chamber

Montana

Helena Area Chamber of Commerce
Montana Chamber of Commerce

Nevada

Henderson Chamber of Commerce
Vegas Chamber

New Jersey

New Jersey State Chamber of Commerce

New York

Brooklyn Chamber of Commerce
Capital Region Chamber
Manhattan Chamber of Commerce
The Business Council of New York State

North Carolina

NC Chamber

North Dakota

Greater North Dakota Chamber

Ohio

Ohio Chamber of Commerce
Willard Area Chamber of Commerce

Oregon

Canby Area Chamber of Commerce
Gresham Area Chamber of Commerce
Keizer Chamber of Commerce
Lake County Chamber of Commerce
Lincoln City Chamber of Commerce
Oregon Business & Industry
Portland Metro Chamber
Roseburg Area Chamber of Commerce

Pennsylvania

Greater Latrobe Laurel-Valley Regional Chamber of Commerce
Hanover Area Chamber of Commerce
Huntingdon County Chamber of Commerce
Mercer Area Chamber of Commerce

Pennsylvania Chamber of Business and Industry
Schuylkill Chamber of Commerce

Texas

Coppell Chamber of Commerce

Virginia

Virginia Chamber of Commerce

Washington

Association of Washington Business
Burlington Chamber of Commerce
Greater Spokane Valley Chamber of Commerce
La Conner Chamber of Commerce
Mercer Island Chamber of Commerce
Moses Lake Chamber of Commerce
Puyallup Sumner Chamber
Shelton-Mason County Chamber of Commerce

Wisconsin

Wisconsin Manufacturers & Commerce

Wyoming

Campbell County Chamber of Commerce
Casper Area Chamber of Commerce
Earth Work Solutions
Riverton Chamber and Visitors Center
Spotted Dog Bed and Breakfast
Wyoming State Chamber of Commerce

Additional

National US India Chamber of Commerce

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Andy Barr
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 1-6 and 11-21 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. Responses to your remaining questions will be forthcoming.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Andy Barr:

1. **In March, regarding the Basel III Endgame proposal, Chairman Powell testified that he was "confident that the final product will be one that has broad support at the Fed and in the broader world." Likewise, you have said you "expect to have a set of broad, material changes to the rule that allow [the Fed] to have a broad consensus."**

    a. **Do you remain committed to achieving broad consensus before finalizing any rule?**
    b. **Do you think the Federal Reserve could suffer serious reputational harm if it sought to finalize the proposal without broad support amongst the Governors?**

As I said in my testimony, given the comments we received, I expect we will have a set of broad and material changes to the proposal. We are currently focused on the substance of the proposed rule and, once that work is complete, we will then determine the appropriate process moving forward.

2. **The comment period for the Basel III Endgame proposal closed on January 16 2024, and on that same day, the Fed concluded its data collection to gather more information from the banks that will be affected by the proposal. The Fed's announcement regarding the data collection noted that "summaries [are] to be made public." Conceivably, those summaries will be of the data itself and of the Fed's analyses of that data.**

    a. **When can we expect to see these summaries?**

    b. **Will you commit to releasing these summaries before taking any further action on the proposal?**

    c. **Do you commit to waiting to take further action on the proposal until after you have received and incorporated comments on the results of the QIS?**

We included impact analysis in the proposal, and then also asked for and received updated data to better evaluate the capital proposal. Doing so allowed us to gather additional, updated data specific to what was being proposed and further evaluate the proposal's impact. We conducted this additional exercise voluntarily to ensure a thoughtful and transparent approach to this proposal. We are closely analyzing this data and are planning to make it available to the public, with an opportunity for comment.

3. **There have been rumors that the Federal banking agencies will soon propose new liquidity regulations, including a requirement that banks preposition some collateral at the discount window. Although some have argued that pre-positioning can ward off bank runs, it would require a substantial reworking of other liquidity rules, such as the**

liquidity coverage ratio, and can have serious implications for the wider wholesale financial market.

a. Can you comment on whether the Federal Reserve is considering introducing a collateral pre-positioning requirement?

b. Will the Federal Reserve commit to providing an economic analysis that considers the impacts that such a requirement would have on wholesale financial markets and explain what steps it would take to mitigate those impacts?

To address the lessons about liquidity learned last spring, we are exploring targeted adjustments to our current liquidity framework. Over the last year, many firms have taken steps to improve their liquidity resilience, and the regulatory adjustments we are considering would ensure that all large banks maintain better liquidity risk management practices going forward.

As part of this work, we are exploring a requirement that banks over a certain size maintain a minimum amount of readily available liquidity with a pool of reserves and pre-positioned collateral at the discount window, based on a fraction of their uninsured deposits. It is vital that depositors have confidence that their funds will be readily available, if needed, and this confidence would be enhanced by a requirement that large banks have readily available liquidity. In developing proposed rules, we carefully consider the potential impact. Any changes to our liquidity rules would be subject to the public notice and comment process required by the Administrative Procedure Act (APA).

4. Regarding potential new liquidity rules:

a. To the extent that Federal banking agencies are actively working on regulatory proposals to update bank liquidity rules, precisely what is being considered and will the Fed discuss what is under consideration with Congress?

b. What is the specific timeline for rulemaking, if any, related to bank liquidity rules.

c. Will the Fed undertake rigorous analysis of the impacts that changes in liquidity rules may have on stability in the market for U.S. Treasury securities?

d. If new rules and regulations concerning liquidity requirements are being contemplated, will the Fed first work with Congress and stakeholders to examine possible effects, or will we see another iteration of the opaque process that was used with the underdeveloped and under-analyzed Basel III Endgame proposal?

To address the lessons about liquidity learned last spring, we are exploring targeted adjustments to our current liquidity framework. Over the last year, many firms have taken steps to improve their liquidity resilience, and the regulatory adjustments we are considering would ensure that all

large banks maintain better liquidity risk management practices going forward. They would also complement the capital requirements by improving banks' ability to respond to funding shocks.

First, we are exploring a requirement that banks over a certain size maintain a minimum amount of readily available liquidity with a pool of reserves and pre-positioned collateral at the discount window, based on a fraction of their uninsured deposits. It is vital that uninsured depositors have confidence that their funds will be readily available, if needed, and this confidence would be enhanced by a requirement that large banks have readily available liquidity.

Incorporating the discount window into a readiness requirement would also re-emphasize that supervisors and examiners view use of the discount window as appropriate and unexceptional under both normal and stressed market conditions. Given the important role of the discount window, we are also actively working to improve its functionality. As part of these efforts, we are seeking feedback from banks, and this feedback will help us to further prioritize operational improvements.

Second, we are considering a restriction on the extent of reliance on held to maturity assets in large banks' liquidity buffers, such as those held under the liquidity coverage ratio and the internal liquidity stress test requirements, to address the known challenges with their monetization in stress conditions.

Third, we are reviewing the treatment of a handful of types of deposits in the current liquidity framework. Observed deposit withdrawals from high-net-worth individuals and companies associated with venture capital or crypto-asset-related businesses suggest the need to recalibrate deposit outflow assumptions in our rules for these types of depositors. As we saw during the stress of a year ago, these types of deposits can flee banks much more quickly than previously anticipated. Finally, we are revisiting the details of the application of our current liquidity framework for large banks. In developing proposed rules, we carefully consider the potential impact. Any changes to our liquidity rules would be subject to the public notice and comment process required by the APA.

5. Regarding Federal Reserve consideration of merger applications:

a. Do you believe the Federal Reserve conducts a meaningful and careful analysis of bank merger applications before approving them?

b. Do you think it is fair to describe the Fed's merger review process as simply "rubber-stamping," as some on the other side of the aisle have characterized it?

The Federal Reserve Board (Board) takes seriously its responsibility to review bank merger proposals under the relevant statutory factors set forth in the Bank Holding Company Act of 1956, the Home Owners' Loan Act, and the Bank Merger Act. These factors include the financial and managerial resources of the organizations involved and of the proposed combined institution; the convenience and needs of the communities to be served by the resulting institution; the Community Reinvestment Act performance of the involved depository

institutions; the effectiveness of the parties in combatting money laundering; and the effects of the proposal on competition and financial stability.[2]

6. Recently, your counterparts at the FDIC and OCC have proposed significant changes to their bank merger review processes.

a. Does the Fed have any concerns about increased divergence between its own merger review process and those of its fellow bank regulators?

b. Do you believe that greater divergence between the Federal banking agencies in their merger review processes will create greater uncertainty for banks seeking to merge?

c. Does this disincentive to merge potentially create concerns that banks that would benefit from a merger, for instance, a weaker bank being acquired by a strong bank, create potential risks to financial stability that could otherwise be avoided?

The Federal Reserve is reviewing its bank merger framework to determine whether any adjustments would be appropriate to improve our merger analysis. This includes a review of each of the statutory factors that the Federal Reserve must consider in evaluating merger proposals. As part of this process, Board staff have been engaging in discussions with staff of the other federal banking agencies regarding our bank merger frameworks, and with staff of the U.S. Department of Justice regarding its ongoing review of the joint bank merger guidelines.

11. The Federal Reserve extended loans of approximately $180 billion to the SVB and Signature bridge banks. Chairman Gruenberg has said those loans began to accrue a penalty interest rate when the bridge banks went into receivership because they were considered in "technical default." But the Federal Reserve has said these loans were collateralized and protected by an FDIC guarantee.

a. Why would a "technical default" warrant a 100-basis point penalty when the loan was collateralized and had a government guarantee?

b. What economic factors support that result?

c. The transaction looks like a loan from the government to the government, with a penalty rate of interest, that the government passed on to other banks and their customers who had nothing to do with the bank failures. Do you agree?

The Federal Reserve Banks did not make any loans to the Federal Deposit Insurance Corporation (FDIC). In 2023, the Federal Reserve extended loans under its ordinary discount window

[2] *See* 12 U.S.C. § 1842(c).

lending authority (section 10B of the Federal Reserve Act), as well as, in one instance, under its emergency lending authority through the Bank Term Funding Program (BTFP) (established under section 13(3) of the Federal Reserve Act), to depository institutions that were later placed into FDIC receivership. Discount window loans were extended to Silicon Valley Bank, Signature Bank, and First Republic Bank, and BTFP loans were extended to First Republic Bank, in each case, before the depository institutions were placed into receivership. In addition, new discount window loans were extended to Signature Bridge Bank, N.A. and Silicon Valley Bridge Bank, N.A., both OCC-chartered insured depository institutions that were eligible discount window borrowers under the Federal Reserve Act. Upon the two bridge depository institutions and First Republic Bank being placed into receivership, the discount window and BTFP loans were not assumed by the acquiring depository institutions. In each case, the outstanding discount window and BTFP loans have been repaid in full as of November 30, 2023. The outstanding loans accrued interest at 100 basis points above the applicable discount window or BTFP rate until they were repaid in full.

12. The Basel III Endgame proposal is fundamentally flawed, and, at best, a re-proposal is necessary. As proposed, the Basel III Endgame would likely raise capital requirements for U.S. financial institutions by more than 20%. There are suggestions that the EU and UK are supportive of implementing the Basel III Endgame proposal at a lower calibration – closer to a 5 to 7% increase.

a. What does proposed additional gold plating on U.S. firms mean for our international competitiveness?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on U.S. banks, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

13. Can you explain the timeline and process at the Federal Reserve for processing and examining, in detail, the more than 400 comments on the Basel III Endgame proposal issued last July, the vast majority of which are critical of the proposal, coming from constituents across the ideological, geographical, and sectoral spectrums?

a. While I understand that staff will do the hard work of reading and analyzing each comment, what steps will you take to ensure that each of your fellow Board Members is fully briefed on the issues raised by the voluminous comments?

b. What steps will you take to ensure that each of your fellow Board Members has equal access to the staff's assistance in understanding and evaluating the comments?

c. Will each of your fellow Board Members be given the opportunity to weigh in on how each issue raised by the comments should be addressed?

Every member of the Board received extensive information related to the proposal before a vote was taken. As part of this ongoing process, Board members will continue to receive information, including briefings from Board staff, as we work to evaluate the policy changes and process forward for this proposal.

14. A recent Oliver Wyman study found that $35 billion of the revenue lost among U.S. banks would be taken up by either European banks or the nonbank sector. Has this type of migration of financial services activity to U.S. competitors or the less regulated nonbank space be contemplated as you consider making changes to the proposal? If so, how and to what extent?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on U.S. banks, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

15. After the financial crisis many banks were encouraged to diversify into service-oriented bank businesses like wealth management to offset their financial risks through steady fee revenue. Now, under the Basel III capital proposal, these fee-oriented businesses that don't take significant financial risk will be considered much riskier due to an operational risk charge. This operational risk charge, however, is based on financial measures of size that bear no substantive relation to actual risks. Creating a measure of operational risk that is overly dependent on revenue seems conceptually flawed, and it ignores the capturing of that risk in the Fed's stress tests. Most of the increase in capital in the Basel III Endgame proposal comes from this new measure of operational risk. Is there some hole that you see in the existing stress testing and models approach, which accounts for operational losses, that warrants the double counting of risks?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding operational risk, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

16. Recently, Bill Dudley, former president of the Federal Reserve Bank of New York, called for regulators to undertake a detailed study of any potential liquidity proposals before such proposals are circulated to ensure that regulators and the public have a solid understanding of the impact of any such proposals. Do you agree that studying

this issue before and not after a proposal is issued would be best for regulators, the banking sector, and the public?

a. Do you commit to issuing an advanced notice of proposed rulemaking (ANPR) on any potential liquidity requirements before any firm proposals are made?

Any changes to our liquidity rules would be subject to the public notice and comment process required by the APA.

17. In October of last year, some of my colleagues and I sent a letter to you and the other prudential regulators voicing our concerns about the impact that the Basel III Endgame proposal would have on America's agriculture industry. Since then, agriculture industry groups, such as the National Grain and Feed Association, National Council of Farmer Cooperatives, in addition to Farmer Mac and the Farm Credit System, have written their own comment letters on the proposal. Specifically, a letter from the Farm Bureau, Pork, Milk, and Beef producers, and others notes that they: "are very concerned that any contraction in the availability of [derivatives] clearing services will have a disproportionate impact on agricultural end-users that are far outside the major financial centers, especially smaller entities such as grain elevators and family farms." Derivatives transactions are critical risk management tools for our agricultural industry. It is evident that while the letter of this proposal may only directly regulate the largest banks, it will affect industries well beyond the financial sector. How has the Fed analyzed the impacts to industries beyond the banking sector?

a. How will comments like this from an important economic industry for our country be considered and what changes will be made as a result?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on the agricultural sector, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

18. A number of your fellow Fed board members and FDIC board members, along with numerous organizations across the political spectrum – the Urban Institute, National Housing Conference and the Urban League, to name a few – have voiced concerns about the impacts Basel III Endgame will have on homeownership, especially minority and first-time homebuyers. In their comment letter, the National Housing Conference said: "At a time when banks around the country are making efforts to address the homeownership gap, and Special Purpose Credit Programs are being adopted to improve racial equity by financial institutions, requiring an unprecedented and unnecessary level of capital for high LTV mortgage loans risks moving the entire industry in the wrong direction by limiting credit access for borrowers of color." It is

alarming to hear that the mortgage piece of your Basel III proposal goes above and beyond what was agreed to in the 2017 Basel III Framework and beyond what other jurisdictions like the EU and UK are implementing. Is there an American bank-specific deficiency, or a deficiency in the Basel III agreement that necessitates gold plated regulations which will make homeownership more difficult for everyone, particularly minority and first-time homeowners?

a. While an adjustment to the mortgage RWA aspect of the Basel proposal would be welcome, fixing one piece does not address the broad operational risk component of the proposal which comprises the majority of the capital increase and touches every aspect of a bank's business. By not fixing the operational risk piece of the proposal, how will LMI communities, small businesses, and other everyday consumers feel the impact of this proposal?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on credit availability, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

19. As public officials, we are stewards of taxpayer dollars, as are our counterparts in our state and local governments. Taxpayer dollars fund infrastructure like schools, hospitals, roads, and other critical projects, and we should strive to continue investing in our infrastructure without unnecessary cost to our constituents. The Basel III Endgame proposal will force us to spend more money to finance the same infrastructure projects. As the Government Finance Officers Association and other organizations across the municipal debt market wrote in a comment letter: "Our U.S. State and local government issuers and conduit nonprofit borrowers rely on access to affordable credit, primarily through the issuance of municipal bonds and direct loans from financial institutions, to finance our nation's infrastructure assets and critical public services. These borrowing opportunities are often made more affordable by the tax-advantaged treatment of qualified bonds and relationships built between local lenders and borrowers. Increases in debt service costs for municipal issuers and conduit borrowers will result in declined investment in infrastructure, public safety, education, and numerous other social services." When America's infrastructure investment is falling behind and we are trying to incentivize it at the federal level, what are the consequences of the Basel proposal on financing schools, roads, or other infrastructure projects?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on state and municipal financing, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of

broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

20. I am concerned that the Basel III Endgame proposal would negatively impact every American's ability to save for retirement. As they wrote to you in their comment letter, the American Benefits Council notes "the proposal would significantly increase banks' capital requirements for derivatives and SFTs (securities financing transactions), among other transactions. These costs would be passed on to end users (such as [retirement] plans), increasing the cost and reducing the availability of these products. The loss of these products at a reasonable price – or the unavailability of these products – will result in some plans managing risks in less effective ways, which will undoubtedly lead to higher costs (again at the expense of participants and beneficiaries) and more harmful volatility. The specter of higher costs and increased volatility will in turn result in more employers terminating their plans, again hurting participants." This sounds like a lose-lose-lose situation which stands to hurt retirement savers. Do you disagree with this logic?

a. At a time when Americans are already dealing with heightened inflation, why are we making it harder and more expensive to save for retirement?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on retirement savers, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

21. Chairman Powell has repeatedly said that there would be broad and material changes to the Basel III Endgame proposal based on the comments received. I have called for these rules to be withdrawn and re-proposed, particularly in light of the volume and breadth of comments submitted from individuals and institutions across U.S. markets, political spectrum, and geography. Notably, the comments reveal particular downsides of the proposal for the availability and cost of credit for small and medium-sized businesses.

a. In finalizing any Basel-related rules under consideration, specifically as they relate to credit risk calculations, will due consideration be given to the call for continuing flexibility to recognize the value of for highly liquid non-financial collateral, such as accounts receivable and inventory?

b. Does the special data collection referenced in your comments include the data drawn from the agencies' direct oversight (and which informs current regulatory guidance), which support the distinction among different types of loan structures and has been provided by commenters for review?

c. Will consideration be given to the impact of the rules on the amount of capital required to support a swingline loan structure and the disincentives it will pose, particularly when fronting exposure is mitigated by reimbursement obligations owing from highly secure investment grade financial institutions?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on small businesses, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable Andy Barr
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 7 and 9 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. Responses to your remaining questions will be forthcoming.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 1-6 and 11-21 were sent to your office and the Committee on June 27, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Andy Barr:

7. **The larger and more complex a banking organization is, the more rules around capital, liquidity, and supervision that banking organization must adhere to. For example, global systemically important banks (GSIBs) are subject to an additional capital requirement known as the GSIB surcharge.**

    a. **Given these enhanced standards for larger banks, is it possible that a merger or acquisition could improve financial stability by subjecting more bank assets in the system to heightened standards?**

    b. **If this is not the case, then what is the purpose of all these heightened standards for banking organizations with more than $100 billion in assets?**

The Dodd-Frank Wall Street Reform and Consumer Protection Act amended the Bank Holding Company Act of 1956 (BHC Act), to require the Federal Reserve Board (Board) to take into consideration "the extent to which a proposed acquisition, merger, or consolidation would result in greater or more concentrated risks to the stability of the United States banking or financial system" when evaluating bank acquisitions by bank holding companies.[1] In response, the Board developed a comprehensive, multi-faceted framework for evaluating how a particular proposed merger may affect financial stability risks. Under the framework, the Board analyzes five key factors: (i) the size of the resulting firm; (ii) the availability of substitute providers for any critical products or services offered by the resulting firm; (iii) the interconnectedness of the resulting firm with the banking or financial system; (iv) the extent to which the resulting firm contributes to the complexity of the financial system; and (v) the extent of the cross-border activities of the resulting firm. These metrics are intended to capture the systemic importance of the combined organization and the incremental effect of the transaction on the systemic footprint of the acquiring institution. The Board also considers qualitative factors indicative of the relative degree of difficulty of resolving the resulting firm, such as the opaqueness and complexity of a firm's internal organization. Further, the Board considers the resulting firm's global systemically important bank score and factors that may mitigate the effect of a proposed transaction on financial stability; however, the Board has been clear that these factors are not exhaustive or dispositive, and that any analysis under the financial stability factor is holistic.

Heightened regulatory requirements are one of many considerations in evaluating the financial stability risks posed by a firm's larger size, or increased interconnectedness and complexity. Each merger or acquisition is evaluated based on the specific facts presented.

9. **In 2020, the Board unanimously approved new rules to provide clarity on bank control. Consumer Financial Protection Director Chopra recently stated at an FDIC board meeting that these changes, "sent a clear message that the Federal Reserve would be**

[1] 12 U.S.C. § 1842(c)(7). The Board is also required to consider whether the "risk to the stability of the United States banking or financial system" presented by acquisitions of non-banks by bank holding companies and weighing such risks against any expected public benefits (12 U.S.C. § 1843(j)(2)(A)).

lenient when it came to enforcing Congressional prohibitions and limitations on ownership of banks."

a. Do you agree with Director Chopra that the Board's determinations of control are too lenient and allow for manipulation?

b. At the same FDIC Board meeting, Director Chopra also suggested the only reason a bank would become a member of the Federal Reserve System is to evade FDIC oversight. Can you touch on the reasons that a bank would want to join the Federal Reserve System and respond to his inference that there are material differences between the Federal banking agencies' ability to supervise and regulate banks?

Under the BHC Act and Home Owners' Loan Act (HOLA), it is generally unlawful for any company to acquire "control" of a bank or bank holding company, or of a savings association or savings and loan holding company (collectively, regulated banking entities), without the prior approval of the Board. The Board's review of applications for such prior approval is governed by specific criteria set forth in the respective statutes. Control is defined under the BHC Act as having 25 percent or more of a class of voting securities of a company, having the power to select a majority of the directors of a company, or having the ability to exercise a "controlling influence" over the management or policies of a company.[2] The Board has a long history of interpreting the "controlling influence" standard with respect to the wide variety of relationships between banks and other companies.

In 2020, the Board amended its regulations related to control under the BHC Act and HOLA to clarify and make more transparent the Board's views and practices around control.[3] The core of the 2020 amendments was a framework of presumptions of control and non-control based on particular objective metrics. The 2020 amendments did not constitute a material change to the Board's substantive positions on control; the presumptions were designed to be generally consistent with the Board's historical practice and precedents. In addition, the presumptions were meant to provide clarity and transparency around the Board's general considerations, but the Board retains the ability to determine control based on the facts and circumstances presented by any given case.

The Board can and does monitor relationships between banking organizations and other companies under its control framework through the supervisory process. For example, every parent bank holding company and savings and loan holding company is required to file annual reports with the Board that list each person that owns, controls, or holds with the power to vote 5 percent or more of any class of voting securities of the holding company as of its fiscal year-end.[4] Furthermore, during an examination of a banking organization, examiners review and

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[2] 12 U.S.C. § 1841(a)(2). The definition of control in HOLA is substantially similar to the definition in the BHC Act. *See* 12 U.S.C. 1467a(a)(2).

[3] 85 FR 12398 (March 2, 2020). *See* 12 CFR Part 225, Subpart D; Part 238, Subpart C.

[4] *See* Instructions for the Preparation of the Annual Report of Holding Companies, Reporting Form FR Y-6, Report Item 3: Securities Holders, GEN-9 (Effective December 2022), *available at* https://www.federalreserve.gov/apps/reportingforms/Download/DownloadAttachment?guid=63605a60-09b7-4bf5-b0cc-c931beb9b0b1.

discuss the composition and strategy of the firm's board of directors and management with the firm's management. The examination provides supervisors some visibility into whether there are any control or undue influence issues.

We work within the mandate and structure for bank supervision and regulation that Congress has given us, which includes having three federal agencies that oversee banks. The Federal Reserve shares responsibility for ensuring financial institutions operate safely and soundly, and we have a long history of working collaboratively with the other federal and state banking regulators, including the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and state banking regulators around the country, to ensure that supervision and regulation of financial institutions are effective, efficient, and consistent. For example, it is standard practice to consult with other interested banking regulators when reviewing expansionary proposals from banking organizations.

The federal banking agencies have long recognized the risk that could be presented by a banking organization seeking to change its primary regulator and have developed a policy to protect against such risks by ensuring coordination among regulators.[5] At the same time, the Board recognizes that there are often appropriate reasons for a banking organization to change its charter from federal to state or vice versa or for a state bank to obtain or relinquish its Federal Reserve membership. Importantly, Congress has established a wide variety of common prohibitions and requirements across all bank charter types, which have the effect of substantially reducing divergences across the regulatory frameworks of the federal banking agencies.[6] Consistent with the statutory framework, the federal banking agencies work to align their regulatory and supervisory policies.

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[5] *See* Federal Financial Institutions Examination Council, "Statement on Regulation Conversions" (2009), *available at* ffiec.gov/pdf/pr070109_statement.pdf.

[6] *See, e.g.*, Pub. Law 111-203, § 612, 124 Stat. 1612–14 (July 21, 2010); 12 U.S.C. § 214d. *See also* Supervision and Regulation (SR) Letter 12-16, *available at*: The Fed - Supervisory Letter SR 12-16 / CA 12-12 on Interagency Statement on Restrictions on Conversions of Troubled Banks -- November 26, 2012 (federalreserve.gov).

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

October 1, 2024

The Honorable Andy Barr
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 8 and 10 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. This concludes my responses to your questions.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 1-6 and 11-21 were sent to your office and the Committee on June 27, 2024. Responses to questions 7 and 9 were sent to your office and the Committee on August 7, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Andy Barr:

8. Recently, the Fed proposed changes to its FR Y-3 and FR Y-4 forms that are required to be completed by prospective or current bank holding companies that are seeking to acquire a bank or another bank holding company. Significantly, these proposed changes include requiring an acquiring bank to provide an "integration plan to merge the operations of the combined organization." For larger bank holding companies, this change would likely be marginal, but, for smaller bank holding companies seeking to acquire another bank or bank holding company, the change could present significant increases in upfront costs and increased compliance costs for banks preparing and submitting a merger application for approval. Do these proposed changes, in fact, represent a substantive change in the Fed's merger review process?

The changes to the FR Y-3 and FR Y-4 forms aim to give the Federal Reserve a better understanding of merger proposals at the outset of the application process and do not affect the Federal Reserve's review of applications consistent with the relevant statutory factors. Prior to implementing these changes, the Federal Reserve frequently requested this information when considering bank merger proposals and the changes to these forms would formalize that practice. The revised forms and instructions are available on the Federal Reserve Board's (Board) public website.[1]

10. In 2016, the Fed unanimously approved a joint agency notice of proposed rulemaking to implement incentive compensation provisions of section 956 of Dodd-Frank. Then-Governor Powell voted for this proposal. In the years since, there have obviously been developments around incentive-based compensation. Sensibly, Chair Powell has said that any rulemaking on incentive compensation must be updated to reflect a decade of changes; going so far as to say, "I would like to understand the problem we're solving, and then I would like to see a proposal that addresses that problem." Yet the FDIC, OCC, and FHFA simply re-proposed the 2016 rule. Do you agree with Chair Powell that any section 956 rulemaking on incentive-based compensation should reflect updated knowledge on how the industry works today, as opposed to how it worked in 2016?

Incentive compensation practices before the global financial crisis were flawed and an important post-crisis lesson was that compensation programs should provide incentives for employees to act in the long-term interest of the firm. Senior management should be held accountable for managing risks in a manner consistent with the long-term health of the organization. To this end, the Board, among other federal banking agencies, provided robust supervisory guidance for banks on incentive compensation to assist them in improving their compensation practices.

Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act requires six agencies—the Board, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, the National Credit Union

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[1] For the FR Y-3, *see* https://www.federalreserve.gov/apps/reportingforms/Report/Index/FR_Y-3. For the FR Y-4, *see* https://www.federalreserve.gov/apps/reportingforms/Report/Index/FR_Y-4.

Administration, and the Securities and Exchange Commission—to jointly issue regulations or guidelines implementing prohibitions on certain incentive compensation arrangements at supervised financial institutions and requiring firms to disclose relevant information related to incentive compensation arrangements. The Board is committed to implementing section 956. However, further work on this issue should be based on updated analysis to reflect current banking conditions and practices. We are focused on conducting this analysis to determine the best path forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Joyce Beatty
House of Representatives
Washington, D.C. 20515

Dear Congresswoman:

Enclosed is my response to the question you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Question for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Joyce Beatty:

1. **Vice Chair Barr, I'd like to follow up on a letter I sent you in January with many of my colleagues regarding Basel III and access to credit for low-and-moderate income and underserved communities, first time homebuyers, and small business owners. I appreciate your acknowledgement of my letter, and I understand that you're still working through the hundreds of letters, opinions, and impact statements that were submitted during the comment period.**

   Many stakeholders in my district have brought this issue to my attention and expressed concern about the potential impacts of the rule. The capital requirements proposal is sweeping and complex, so we want to make sure we get this right for consumers and small businesses in Ohio and across the nation.

   How are you incorporating the feedback you've received from consumers and stakeholders?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on credit availability, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable Scott Fitzgerald
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Scott Fitzgerald:

1. **As the Board is not required by statute or regulation to revisit Reg II, why does the Board feel that now is the right time to revisit the regulation, particularly because the Board is currently in the process of collecting data from debit card issuers for 2023, which would not reflect pandemic idiosyncrasies, and may better account for the effect of recent regulatory mandates that have only recently gone into effect, such as the Board's dual routing requirement for card not present transactions?**

Section 1693o–2 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) requires the Federal Reserve Board (Board) to prescribe standards for assessing whether the amount any interchange fee received by a debit card issuer is reasonable and proportional to specific costs incurred by the issuer with respect to the transaction. The Board fulfilled this statutory mandate in 2011 when it adopted the interchange fee cap in Regulation II.

Regulation II's current interchange fee cap is based on the costs incurred by large debit card issuers with respect to transactions performed in 2009. Since that time, the Board has continued to collect data from large debit card issuers on a biennial basis, as required by section 1693o–2. These data show that that the costs incurred by large debit card issuers have changed significantly since 2009. As a result, the current interchange fee cap may no longer be effective for assessing whether the amount of any interchange fee is reasonable and proportional to the cost incurred by the issuer with respect to the transaction, as required by statute.

Last year, the Board proposed to update the interchange fee cap based on the latest data reported to the Board by large debit card issuers concerning transactions performed in 2021. In addition, the Board proposed to update the interchange fee cap every other year going forward by directly linking the interchange fee cap to data from the Board's biennial survey of large debit card issuers. Under the proposed approach, any changes in the costs incurred by large debit card issuers would be reflected in the interchange fee capon a regular basis.

The Board requested comment on all aspects of the proposal. The public comment period closed on May 12, 2024, and the Board is currently in the process of reviewing the public feedback received.

2. **Data related to Cardholder Inquiry Costs and NSF Handling Costs weren't included back in 2011 because that data wasn't readily available at the time. However, now that this information is being collected and is available to the Fed. Did the Fed consider this data in the Reg II proposal and if not, why?**

In prescribing interchange fee standards, section 1693o–2 of the Dodd-Frank Act requires the Board to consider the incremental cost incurred by a debit card issuer for the role of the issuer in the authorization, clearance, or settlement of a particular debit card transaction. The statute prohibits the Board from considering other costs incurred by a debit card issuer that are not specific to a particular transaction. The statute is silent with respect to a third category of costs: costs other than the above-mentioned costs that the Board is required to consider, but that are

specific to a particular transaction. Within this third category of costs, the Board has discretion to consider or not consider particular types of costs, consistent with the statute. The Board is also required to consider the functional similarity between debit card transactions and checking transactions that are required within the Federal Reserve System to clear at par.

Cardholder inquiry costs and non-sufficient funds (NSF) handling costs fall within this third category of costs. When the Board first adopted the interchange fee cap in Regulation II, the Board noted that many cardholder inquiry costs do not relate to specific transactions and that, while some customer service inquiries do relate to particular transactions, fielding these inquiries is partly a cost of a service required by regulatory and network rule requirements and partly a cost of managing the customer relationship.[1] With respect to NSF handling costs, the Board reasoned that these costs are largely, although not always, within the issuer's control. The Board also contrasted cardholder inquiry costs and NSF handling costs with relevant types of costs associated with check transactions. For these reasons, the Board exercised discretion not to include cardholder inquiry costs and NSF handling costs in the interchange fee cap.

In the proposal issued last year, the Board did not propose to change the categories of costs incurred by debit card issuers on which the interchange fee cap is based. The Board reviewed its construction of the statue and prior analysis and stated that it believes that this prior analysis remains sound.

3. Has the Board done an analysis on how the Reg II proposal would affect small banks and credit unions in terms of their ability to recover a reasonable rate of return on the services they provide?

Section 1693o–2 of the Dodd-Frank Act exempts debit card issuers with consolidated assets of less than $10 billion from the interchange fee standards. Regulation II implements this provision through the "small issuer exemption." The Board's proposal to update the interchange fee cap would similarly not apply to small debit card issuers. The Board's proposal includes a statutorily required analysis of the economic impact of the proposal on various parties, including small debit card issuers. This analysis concludes that the proposal would not directly or indirectly affect small issuers. That conclusion is based on two premises:

- First, when the Board adopted the original interchange fee cap, there was concern that the small issuer exemption may not be effective; that is, that networks might not distinguish between small issuers exempt from the interchange fee cap and large issuers subject to the interchange fee cap. However, all networks adopted pricing structures with different interchange fees for large and small issuers.

- Second, data collected by the Board from payment card networks on an annual basis, and published on the Board's website, demonstrate that average per-transaction interchange fees for small issuers across all payment card networks did not decline after the interchange fee cap was adopted in 2011, have not declined since, and have remained

[1] The Board collects data on cardholder inquiry costs related to possible fraudulent debit card transactions, and those costs are included in the interchange fee cap's fraud-prevention adjustment.

substantially higher than average per-transaction interchange fees for large issuers subject to the interchange fee cap.

Although the Board believes that the small issuer exemption has been and will remain effective, the Board requested comment on all aspects of the proposal, including the economic impact of the proposal on small issuers. The Board is currently in the process of reviewing this public feedback.

4. **The Reg II proposal contains an automatic reset provision that would allow the Board to reset, automatically and on a biennial basis, components of the Interchange Fee Cap without providing the public an opportunity to participate in the changes through the notice-and-comment process. Why does the Board believe the automatic adjustment qualifies for the "good cause exception" to the Administrative Procedure Act's notice and comment requirement?**

The Board proposed to update the interchange fee cap every other year going forward by directly linking the interchange fee cap to data from the Board's biennial survey of large debit card issuers. Under the proposed approach, any changes in the costs incurred by large debit card issuers would be reflected in the interchange fee cap on a regular basis. This approach is designed to ensure that the interchange fee cap will be effective going forward for assessing whether the amount of any interchange fee received by a debit card issuer is reasonable and proportional to the cost incurred by the issuer with respect to the transaction, as required by statute.

The Board's proposal includes the specific formulas the Board would use to compute each component of the interchange fee cap going forward. Thus, if the approach were adopted by the Board as proposed, updating the interchange fee cap would be a matter of applying the latest data collected by the Board to the formulas previously adopted following notice and comment.

The Board stated in the proposal that these updates qualify for the "good cause" exception from notice and comment under the Administrative Procedure Act because they would involve the application of existing formulas, and the Board would not be exercising any discretion. In this way, such updates would be similar to inflation adjustments to regulatory thresholds, which do not require notice and comment. However, any changes to the formulas themselves would require a new round of notice and comment.

As stated previously, the Board requested comment on all aspects of the proposal, including the proposal to update the interchange fee cap every other year without notice and comment. The Board is currently in the process of reviewing this public feedback.

5. **Has the Board analyzed how the Reg II proposal would affect low-and-moderate income (LMI) consumers in terms of current services like free checking accounts, pathways for unbanked and underbanked individuals to enter or re-enter the financial mainstream with safe and appropriate accounts such as Bank On, and other affordable banking products?**

The Board's proposal to update the interchange fee cap includes a statutorily required analysis of the economic impact of the proposal on various parties, including consumers. This analysis concludes that the net effect of the proposal on consumers, both individually and in the aggregate, will depend on which of two effects predominates:

- First, the proposal would lower merchants' costs of accepting debit card transactions. Merchants may pass through some or all of these savings to consumers in the form of lower prices, foregone future price increases, or improvements in product or service quality. These responses by merchants may benefit consumers.

- Second, the proposal would lower the interchange revenue earned by large debit card issuers on debit card transactions. Large issuers may seek to offset these losses by increasing fees on debit cards or checking accounts, or making other adjustments that make these products less attractive to consumers. These responses by large issuers may harm consumers and may make banking services less accessible for low-and-moderate income consumers in particular.

The Board noted that which of these two effects predominates will depend on many factors and is thus difficult to predict. As stated previously, the Board requested comment on all aspects of the proposal, including the economic impact of the proposal on consumers. The Board is currently in the process of reviewing this public feedback.

6. Private mortgage insurance is one of the best tools we have to help first-time homebuyers who don't have the savings to make a traditional 20 percent down payment. You seemed to acknowledge this last November when you testified that "private mortgage insurance can be a factor that contributes to a mortgage being considered prudently underwritten."

a. Can you confirm that under any new rule private mortgage insurance would continue to be gating criteria for low down payment mortgages to receive risk weights less than 100%?

b. Have the agencies considered the FHFA's Enterprise Regulatory Capital Framework (ERCF) as a basis for providing capital relief to low down payment mortgages with private mortgage insurance coverage?

Under the current capital framework and in the capital proposal, mortgage insurers are not considered eligible guarantors, meaning that mortgage insurance cannot, in isolation, reduce the capital requirement for a mortgage loan. This is due to the concern that private mortgage insurers tend to be less financially sound during periods of housing market stress, including during the global financial crisis of 2007-09.

However, consistent with the current rule, private mortgage insurance would continue to be one of several factors in a banking organization's assessment of whether a mortgage is prudently underwritten and thus may qualify for beneficial risk-weight treatment. We are reviewing public comments on the proposal.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Bill Foster
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Bill Foster:

Basel III Endgame Quantitative Impact Study

Thank you for your decision to conduct a quantitative impact study (QIS) on the impact of the Basel III Endgame proposal. I believe it is an important exercise that will help our committee and the public better understand the real impact of what is being proposed on the U.S. economy. I think it is important for the findings of the QIS to be made public and allow for public engagement on the findings as you continue working to reach consensus on the proposal.

1. **Vice Chair Barr, do you intend to release the QIS results for public comment and use public comments on the results to inform next steps on the rule?**

    a. **What is the path forward for the Basel III Endgame QIS and final rule. Can you share any additional information regarding process, timing, and substance?**

We included impact analysis in the proposal, and then also asked for and received updated data to better evaluate the capital proposal. Doing so allowed us to gather additional, updated data specific to what was being proposed and further evaluate the proposal's impact. We conducted this additional exercise voluntarily to ensure a thoughtful and transparent approach to this proposal. We are closely analyzing this data and are planning to make it available to the public, with an opportunity for comment. As I said in my testimony, given the comments we received, I expect we will have a set of broad and material changes to the proposal. We are currently focused on the substance of the proposed rule and, once that work is complete, we will then determine the appropriate process moving forward.

Liquidity Proposal/Process

Your agencies have indicated that you are working on a liquidity proposal. I would urge you all to conduct a well-informed, data driven, public process as you develop a proposal. Engaging with industry experts, academics and consumer advocates will ensure that the proposal hits the mark and is well calibrated for today's banking system. As we saw with the failure of Silicon Valley Bank, bank runs powered by social media and modern technology can be more rapid than previously thought.

2. **Vice Chair Barr, how are you engaging with the banking community and business and consumer advocates as you develop the upcoming liquidity proposal? What information would be helpful as you draft the proposal?**

To address the lessons about liquidity learned last spring, we are exploring targeted adjustments to our current liquidity framework. Over the last year, many firms have taken steps to improve their liquidity resilience, and the regulatory adjustments we are considering would ensure that all large banks maintain better liquidity risk management practices going forward. They would also complement the capital requirements by improving banks' ability to respond to funding shocks.

First, we are exploring a requirement that banks over a certain size maintain a minimum amount of readily available liquidity with a pool of reserves and pre-positioned collateral at the discount window, based on a fraction of their uninsured deposits. It is vital that uninsured depositors have confidence that their funds will be readily available, if needed, and this confidence would be enhanced by a requirement that large banks have readily available liquidity.

Incorporating the discount window into a readiness requirement would also re-emphasize that supervisors and examiners view use of the discount window as appropriate and unexceptional under both normal and stressed market conditions. Given the important role of the discount window, we are also actively working to improve its functionality. As part of these efforts, we are seeking feedback from banks, and this feedback will help us to further prioritize operational improvements.

Second, we are considering a restriction on the extent of reliance on held to maturity assets in large banks' liquidity buffers, such as those held under the liquidity coverage ratio and the internal liquidity stress test requirements, to address the known challenges with their monetization in stress conditions.

Third, we are reviewing the treatment of a handful of types of deposits in the current liquidity framework. Observed deposit withdrawals from high-net-worth individuals and companies associated with venture capital or crypto-asset-related businesses suggest the need to recalibrate deposit outflow assumptions in our rules for these types of depositors. As we saw during the stress of a year ago, these types of deposits can flee banks much more quickly than previously anticipated. Finally, we are revisiting the details of the application of our current liquidity framework for large banks. In developing proposed rules, we carefully consider the potential impact. Any changes to our liquidity rules would be subject to the public notice and comment process required by the Administrative Procedure Act.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable Andrew Garbarino
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Andrew Garbarino:

1. **The FHFA issued its FHLBank System at 100 Report late last year. Did the FHFA coordinate with any of the prudential regulations in the conducting and scheduling of its series of fact-finding roundtables and townhall meetings across the country? Were any of the prudential regulators involved in the drafting and publication of the report?**

The Federal Housing Finance Agency published its report independently. The Federal Reserve was not involved in the drafting or publication of this report.

2. **Since the release of the FHFA's FHLBank System at 100 Report, numerous officials from FHFA have acknowledged that the FHLBanks play an important role in providing liquidity to financial institutions. However, they have also said that the FHLBanks cannot be the "Lender of Last Resort" and that the Federal Reserve should have the responsibility to lend to troubled financial institutions.**

    a. **Acknowledging that your regulated entities, and the FHLBanks that lend to them, need regulatory clarity and certainty, is there a regulatory definition of a "troubled" (or "weak") institution that all of the prudential regulators and FHFA use for purposes of determining whether FHLBanks should continue lending to financial institutions?**

    b. **If so, what regulatory body is responsible for determining if a financial institution is "troubled" (or "weak")?**

    c. **Have the prudential regulators and the FHFA given clear direction or guidance as to when a FHLBank should designate and report a "troubled" (or "weak") bank to the Federal Reserve?**

    d. **If the prudential regulators and the FHFA have not provided that guidance yet, when will that guidance or direction be published so that financial institutions and FHLBanks are clear on the availability of liquidity from the FHLBanks to financial institutions that are at risk of being deemed "troubled" or "weak"?**

    e. **How do the prudential regulators otherwise evaluate whether a financial institution has experienced a decline in financial condition such that the prudential regulators would raise concerns related to that financial institution's creditworthiness with the relevant FHLBanks? Have the prudential regulators given clear direction or guidance as to when they will raise such concerns with the FHLBanks? What would be the implications of a material decline in a financial institution's financial condition for accessing FHLBank liquidity? Have the prudential regulators and the FHFA provided, or do they plan to provide, guidance clarifying such implications?**

The Federal Reserve does not dictate Federal Home Loan Bank (FHLB) credit decisions A wide range of banks are FHLB members and many of them consider FHLB advances a normal part of their funding mix. The Federal Reserve System has good coordination with FHLBs.

The Federal Reserve may share supervisory information regarding a specific financial institution's financial condition with the FHLB upon request. This is consistent with a memorandum of understanding we have in place that references Title 12 of the United States Code, section 1442. This law directs the Federal Reserve along with other bank regulators to make available to any FHLB "such reports, records, or other information as may be available, relating to the condition of any member bank for any FHLB or institution to which such Bank has had or contemplates having transactions."

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Josh Gottheimer
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Josh Gottheimer:

1. **The U.S. economy and our capital markets are the envy of the world. To maintain that status, we must remain competitive with other nations in balancing the interests of stability with the interests of liquidity. Vice Chair Barr, can you give me some examples of how you are balancing those interests when implementing Basel III, to ensure our markets remain globally competitive?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on U.S. capital markets, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

2. **Vice Chair Barr, the entire point of Basel III Endgame was to level capital requirements across jurisdictions, not for the U.S. to raise our requirements and impair our own economic growth. Will the Fed, FDIC, and OCC commit to releasing the study for public feedback under a notice and comment period, and will you do so before re-proposing or finalizing Basel III Endgame?**

We included impact analysis in the proposal, and then also asked for and received updated data to better evaluate the capital proposal. Doing so allowed us to gather additional, updated data specific to what was being proposed and further evaluate the proposal's impact. We conducted this additional exercise voluntarily to ensure a thoughtful and transparent approach to this proposal. We are closely analyzing this data and are planning to make it available to the public, with an opportunity for comment. As I said in my testimony, given the comments we received, I expect we will have a set of broad and material changes to the proposal. We are currently focused on the substance of the proposed rule and, once that work is complete, we will then determine the appropriate process moving forward.

3. **Vice Chair Barr, it seems premature to finalize the long-term debt (LTD) rules without fully understanding the impacts of Basel III Endgame. It is made clear in the LTD proposal that the specific calibrations of the rule were determined using the current capital framework that the Basel III Endgame seeks to amend, making an accurate assessment of the LTD proposal impossible. While I continue to believe that the Basel III Endgame proposed rule should be withdrawn and reissued, would you agree that the agencies should not finalize the LTD proposal until banks have a better understanding of the capital requirements they will face under Basel III?**

I am committed to maintaining the strength and diversity of the banking system, so that it can continue to provide financial services and access to credit for households and businesses. Community and regional banks serve important sectors of the economy that are often not the focus of many other financial institutions, including small businesses, middle market businesses,

and consumers in rural communities. I am attentive to making sure we retain this diversity, and that our regulation and supervision reflect the size and risks associated with different firms.

The long-term debt (LTD) proposal only applies to firms over $100 billion and preserves significant regulatory differences among the firms that would be subject to the rule and global systemically important banks (GSIBs). For example, the firms subject to the proposal would be required to hold a lower level of LTD than GSIBs. In addition, the firms subject to the proposal would have no total loss-absorbing capacity minimum requirements. The calibration of the proposed LTD requirement also increases in stringency based on the size and risk profile of the assets held by a bank that would be subject to the proposal. All else equal, institutions are required to issue more LTD when they increase in size or their assets become riskier.

The proposal invited the public to comment on the Federal Reserve Board's (Board) proposed differentiation of the LTD requirements, and whether the Board should adjust the proposed application and scope of the rule. The Board is carefully reviewing feedback from the public on these issues.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable French Hill
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to question 1 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. This concludes my responses to your questions.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 2 and 3 were sent to your office and the Committee on June 27, 2024.

Question for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative French Hill:

1. **The Fed has been public about how many institutions have signed up for its real-time payment system, FedNow, but not how much it is being used. Please tell me the dollar amount sent vs. received through FedNow. This information should be from when FedNow went live on July 20, 2023, to the present date of May 15, 2024.**

A diverse group of banks and credit unions across the country have adopted the FedNow® Service. These institutions are in the early stages of implementing new instant payment services for their customers and adjusting to round-the-clock operations. Accordingly, the number of transactions and dollar amounts sent on the FedNow Service since July 2023 is modest, which is in line with what we expected for a new service. Our intention is to publish volume and value information in the future for the FedNow Service as we do for our other payment services. From a longer-term perspective, we expect transaction volumes will follow the typical trajectory of a new payment service and grow steadily over time.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable French Hill
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 2 and 3 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. A response to your remaining question will be forthcoming.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative French Hill:

2. **The Basel III Endgame proposal's treatment for inter-affiliate transactions is punitive and it could better capture the risk of such transactions. In particular, the proposed treatment does not consider the unique relationship between a foreign bank and its affiliates, and this could discourage the prudent management of internal funding, liquidity, and capital. What is the justification for treating a transaction between affiliates the same as transactions to unaffiliated third parties?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on foreign banks, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

3. **Have your agencies taken responsibility for assessing the Basel proposal's impact on the municipal bond market? What type of interaction has your agency had with the SEC or the MSRB on the topic of municipal bonds? Furthermore, how does the government plan to address the identified risks, particularly the projected increase in the cost of capital for holding municipal bonds and its potential adverse effects on borrowing costs for municipalities nationwide?**

As I noted above, as part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on state and municipal financing, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Michael V. Lawler
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 1 through 3 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. A response to your remaining question will be forthcoming.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Michael V. Lawler:

1. **The market risk component of the Basel III Endgame proposal is highly complex and would increase capital requirements on critical market making activities by over 70%. For example, the Business Roundtable stated in their comment letter that "the new framework for market risk and the new additive requirements for derivative transactions (CVA) would significantly raise the costs for U.S. public companies to hedge business and operating risks." Derivatives are a critical risk management tool and without them, risk both inside the financial system and across the broader economy will increase. Considering that the aim of the Basel III Endgame proposal is to mitigate risk, please explain what steps you will take to ensure that the proposal does not make it more difficult for American businesses to manage risk?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on derivatives transactions, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

2. **The National Association of Manufacturers notes in its comment letter; "the Proposed Rule's substantial increase in capital requirements for banks' trading books through the Fundamental Review of the Trading Book will significantly increase the costs of critical risk management tools for U.S. manufacturers." They go on to say that "by making it less affordable and more complex for manufacturers and other non-bank entities to manage risks, the Proposed Rule will ultimately make the U.S. economy less resilient and more vulnerable to financial shocks." The market risk components of the Basel III Endgame proposal stand to undermine the goal of reducing risk in the financial system. Have you had conversations with the Manufacturers or other industries who would be subject to much higher hedging costs?**

    a. **Do you disagree with the diverse range of commenters who note that the market risk component of the proposal would make the economy less resilient?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the market risk components of the proposal, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

3. **Vice Chair Barr, your Federal Reserve colleagues, including Governor Cook last week, have expressed some concern about commercial real estate (CRE) exposures in smaller banks, particularly around concentration risk. We're aware of the challenging**

environment for CRE, and that borrowers will need access to credit as loans mature during this period of higher interest rates and high inflations.

a. **Have you studied the Basel Endgame proposal's impact on availability of credit for CRE? If so, what is that impact?**

b. **If CRE risk weights are lower, but other provisions raise overall bank capital, what is the end result? Does this mean these banks will make more CRE loans than they currently do?**

c. **If small banks have too many CRE loans and you raise costs on large banks, where should borrowers turn for a CRE mortgage?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on commercial real estate, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable Michael V. Lawler
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to question 4 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. This concludes my responses to your questions.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 1-3 were sent to your office and the Committee on June 27, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Michael V. Lawler:

4. **John Williams, president of the Federal Reserve Bank of New York, recently spoke at a member symposium hosted by the FHLBank of New York. In his comments, Mr. Williams stated that "the Federal Home Loan Bank of New York and the New York Fed share a commitment to supporting economic strength in communities and households in our region." He also went on to note that he and his staff had regular contact with the CEO and Management Team of FHLBNY. He later stated that the FRBNY and FHLBNY had complimentary roles in providing needed liquidity to banks and other lenders in their footprint. Would you agree that the liquidity roles of the FHLBank System and the Fed's discount window are separate and complimentary to one another, and do not conflict?**

Federal Reserve lending to depository institutions through the discount window plays an important role in supporting the liquidity and stability of the banking system and the effective implementation of monetary policy. By providing ready access to funding, the discount window helps depository institutions manage their liquidity risks efficiently and avoid actions that have negative consequences for their customers, such as withdrawing credit during times of market stress. Thus, the discount window supports the smooth flow of credit to households and businesses. Providing liquidity in this way is one of the original purposes of the Federal Reserve System and other central banks around the world.

Congress chartered the Federal Home Loan Banks (FHLB) to support mortgage lending. A wide range of banks are FHLB members and many of them consider FHLB advances a normal part of their funding mix.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Barry Loudermilk
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Barry Loudermilk:

1. **Vice Chairman Barr, you've received more than 400 comments on the Basel III Endgame proposal issued last July, the vast majority of which I'll note are negative. Could you explain the process and timeline, in detail, for examining all 400 of these comments?**

The Federal Reserve has received numerous and meaningful comments on the capital proposal, as well as additional information from a special data collection. As I said in my testimony, given the comments we received, I expect we will have a set of broad and material changes to the proposal. We are currently focused on the substance of the proposed rule and, once that work is complete, we will then determine the appropriate process moving forward.

2. **Chairman Powell has previously indicated that there would be "broad and material changes" to the Basel III Endgame proposal and left open the possibility of a re-proposal before it is finalized. In his remarks he stated that he expects any final rule to have broad support from the Board. I understand that your staff will do the hard work reading and analyzing each comment, but how will you personally ensure that your fellow Board Members are all sufficiently briefed on the substantive issues raised in the public comments?**

Every member of the Federal Reserve Board (Board) received extensive information related to the proposal before a vote was taken. As part of this ongoing process, Board members will continue to receive information, including briefings from Board staff, as we work to evaluate the policy changes and process forward for this proposal.

3. **Will each board member have access to staff assistance to understand concerns raised in the public comments?**

Please see my response to question 2.

4. **Will all board members have the opportunity to weigh in on issues raised in the comments?**

Please see my response to question 2.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Zach Nunn
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to the question you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Question for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Zach Nunn:

1. **Mr. Barr, Under the Basel III Endgame proposal, the proposed credit conversion factor applied to off-balance sheet items like unused credit card lines would apply to undrawn funds, reflecting the amount that could become an on-balance sheet exposure. The associated capital implications could incentivize financial institutions to lower their off-balance sheet exposure in part by reducing or closing dormant credit lines. This credit contraction could disproportionately impact military credit cardholders. Servicemembers tend to exhibit different credit usage patterns compared to their civilian counterparts, including longer periods of inactivity or decreased usage. Are the agencies considering unintended impacts on servicemembers, and will the broad and material changes underway include adjustments to this aspect of the proposal?**

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on unused credit lines, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

JEROME H. POWELL
CHAIR

October 1, 2024

The Honorable John Rose
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to question 1 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. This concludes my responses to your questions.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 2 through 4 were sent to your office and the Committee on June 27, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative John Rose:

1. **Vice Chairman Barr, with the increased prevalence of remote work, the Committee is concerned about potential incidents of accidental disclosure or misuse of confidential Federal Reserve data by employees. Please discuss with your team and provide a written response for the record on the following:**

   Have there been any documented incidents of accidental disclosure or misuse of confidential Federal Reserve data by employees working remotely in the past five years?

   If so, please provide details regarding the nature of the incidents, including:

   - **Date range of the incidents.**
   - **Type of data involved (e.g., customer information, financial data).**
   - **Actions taken by the Federal Reserve to address the incidents and prevent future occurrences.**

The Federal Reserve Board (Board) takes safeguarding confidential Federal Reserve data very seriously. Over the past five years, the Board has not experienced any accidental disclosure or misuse of confidential data that was related to an employee working remotely. We have thorough policies and procedures to safeguard all confidential data and to monitor for its accidental disclosure or misuse no matter from where or how it is accessed. Furthermore, all access to data by employees is monitored for accidental disclosure or misuse.

A foundational component of our approach to protecting confidential data is the requirement for all employees to access Federal Reserve data through the same mechanisms and controls whether they are working from a Board facility or remotely.

The Board is continuously enhancing our controls and all methods of access and provides employees with regular data handling training that is modified over time to address emerging threats and risks.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable John Rose
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 2 through 4 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. A response to your remaining question will be forthcoming.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative John Rose:

2. Vice Chairman Barr, did the Fed think through how businesses' access to credit will potentially be impeded by the likely/potential for further consolidation in the banking market due to higher capital level?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on access to credit, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

3. Vice Chair Barr, what are your plans regarding artificial intelligence?

The Federal Reserve is taking a deliberate approach to supervising banks' use of artificial intelligence (AI) and seeking a wide range of input on AI's benefits and risks and potential regulatory gaps. Our goal is to create guardrails that can support innovation that benefits consumers and the financial system broadly. We are closely monitoring how banks are using AI and confirming that proper controls are in place in addition to referring to existing laws, regulations, and guidance that have applicability to AI—such as IT handbooks, model risk management guidance, third-party risk management guidance, and consumer laws and regulations. Additionally, Federal Reserve staff work closely with staff of other regulatory agencies to track and learn more about emerging practices regarding banks' use of AI and related risk management.

4. Vice Chair Barr, has the Fed assessed the implications and potential unintended consequences of the Ops Risk calculation?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding operational risk, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

June 27, 2024

The Honorable Brad Sherman
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed are my responses to questions 1 and 3-5 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. A response to your remaining question will be forthcoming.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Questions for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Brad Sherman:

1. **Consequences of Prepositioning**

   During our exchange at the hearing, I inquired about the Federal Reserve's reported proposal on prepositioning of Discount Window collateral to cover a portion of uninsured deposits, and on the need for community lenders to serve small businesses when considering such proposal.

   How could requiring prepositioning of collateral in proportion to uninsured deposits affect a financial institution's overall ability to manage their balance sheet and net income, given that this collateral would be tied to only short-term borrowing from the Fed?

   To provide small business loans or first-time homebuyers with mortgages, a financial institution must have the flexibility to borrow an optimal mix of both long-term (i.e., years) and short-term (i.e., days) liquidity. With the Federal Reserve's Discount Window limited to 90-day terms, how might a financial institution's own lending operations be affected by prepositioning significant amounts of collateral *exclusively for* short-term borrowing?

To address the lessons about liquidity learned last spring, we are exploring targeted adjustments to our current liquidity framework. Over the last year, many firms have taken steps to improve their liquidity resilience, and the regulatory adjustments we are considering would ensure that all large banks maintain better liquidity risk management practices going forward.

As part of this work, we are exploring a requirement that banks over a certain size maintain a minimum amount of readily available liquidity with a pool of reserves and pre-positioned collateral at the discount window, based on a fraction of their uninsured deposits. It is vital that depositors have confidence that their funds will be readily available, if needed, and this confidence would be enhanced by a requirement that large banks have readily available liquidity. In developing proposed rules, we carefully consider the potential impact. Any changes to our liquidity rules would be subject to the public notice and comment process required by the Administrative Procedure Act.

3. **Domestic Manufacturing Competitiveness**

   The National Association of Manufacturers highlighted in its comment letter that the Basel III Endgame proposal could "significantly increase the costs of critical risk management tools for U.S. manufacturers" given increased capital requirements associated with banks' market-making activities with respect to – for example – commodity derivatives for price fluctuations in raw materials, cross-currency swaps for international currency variations, and interest rate swaps for interest rate changes on long-term liabilities. Moreover, manufacturers say that the capital increases associated with banks' capital markets activities may hurt America's ability to outpace foreign

competitors, "thus impairing the ability of U.S. manufacturers to compete on price, capture market share, and lead the world in innovation." What are your agencies' assessments of the consequences that the Basel III Endgame proposal will have for the international competitiveness of American manufacturers – and for end-users more-generally – that want to hedge their risks?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the market risk components of the proposal, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

4. Municipal Underwriting & Infrastructure

Congress pushed through substantial legislation to encourage investments in our infrastructure like the building of roads, schools, bridges, and hospitals across the country. As we pursue these infrastructure projects, we must be mindful not to undermine these critical investments and make municipal financing more expensive. As the Government Finance Officers Association pointed out in response to Basel III Endgame: "Increases in debt service costs for municipal issuers and conduit borrowers will result in declined investment in infrastructure, public safety, education, and numerous other social services." What do your agencies anticipate are the consequences of the Basel III Endgame proposal on financing schools, roads, or other infrastructure projects?

As part of the public comment process, we received numerous and meaningful comments on the proposal, as well as additional data from a special data collection. We are aware of the concerns that commenters have raised regarding the impact of the proposal on state and municipal financing, and we are in the process of reviewing and assessing the data and the comments received on these issues and other aspects of the proposed rule. I expect we will have a set of broad, material changes to the proposal that allow us to have a broad consensus in moving the proposal forward.

5. Private Mortgage Insurance

Can you confirm that the Basel III Endgame proposal would continue the current practice of including private mortgage insurance as one of the credit enhancement factors required for low down payment mortgages with a loan-to-value ratio of above 90 percent to satisfy the definition of "regulatory residential real estate exposure"? If yes, would you consider explicitly stating as such in the final rule – that private mortgage insurance will continue to be considered a factor for credit enhancement?

Under the current capital framework and in the capital proposal, mortgage insurers are not considered eligible guarantors, meaning that mortgage insurance cannot, in isolation, reduce the capital requirement for a mortgage loan. This is due to the concern that private mortgage

insurers tend to be less financially sound during periods of housing market stress, including during the global financial crisis of 2007-09.

However, consistent with the current rule, private mortgage insurance would continue to be one of several factors in a banking organization's assessment of whether a mortgage is prudently underwritten and thus may qualify for beneficial risk-weight treatment. We are reviewing public comments on the proposal.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

MICHAEL S. BARR
VICE CHAIR FOR SUPERVISION

August 9, 2024

The Honorable Brad Sherman
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to question 2 that you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record. This concludes my responses to your questions.[2]

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.
[2] Responses to questions 1 and 3-5 were sent to your office and the Committee on June 27, 2024.

Question for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative Brad Sherman:

2. Coordination with Federal Home Loan Banks

Having liquidity options is critical. The prudential regulators have made it a priority to ensure that your regulated entities can access the Federal Reserve's Discount Window if necessary. What percentage of the banks under your supervision have accessed the Window this calendar year? Are all banks under your supervision ready to tap the facility if they need contingent liquidity right now?

It is my understanding that the Federal Home Loan Banks have worked to establish intercreditor agreements with the various Federal Reserve Banks, which allow a lender to access both the Discount Window and FHLBanks. How does (or doesn't) utilization of these agreements ensure in moments of economic stress, lenders have the necessary means to sufficient liquidity?

Federal Reserve lending to depository institutions through the discount window plays an important role in supporting the liquidity and stability of the banking system and the effective implementation of monetary policy. By providing ready access to funding, the discount window helps depository institutions manage their liquidity risks efficiently and avoid actions that have negative consequences for their customers, such as withdrawing credit during times of market stress. Thus, the discount window supports the smooth flow of credit to households and businesses. Providing liquidity in this way is one of the original purposes of the Federal Reserve System and other central banks around the world.

The Federal Reserve, along with the other federal banking agencies, have encouraged depository institutions to incorporate the discount window as part of their contingency funding plans. By the end of 2023, about 3,900 banks, or 80 percent of all banks, had completed the legal documentation to borrow. Of those, nearly 2,000 banks pledged collateral totaling $2.6 trillion. These figures are substantially above their levels at the end of 2022.

Both the Federal Reserve Banks and the Federal Home Loan Banks (FHLB) make advances on a secured basis. The Federal Reserve Banks and FHLBs coordinate to ensure that advances to the same borrower are not secured by the same collateral. Such coordination can assist in the smooth transfer of collateral between the FHLBs and Reserve Banks if the need arises.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

JEROME H. POWELL
CHAIR

October 4, 2024

The Honorable William Timmons
House of Representatives
Washington, D.C. 20515

Dear Congressman:

Enclosed is my response to the questions you submitted following the May 15, 2024,[1] hearing before the Committee on Financial Services. A copy also has been forwarded to the Committee for inclusion in the hearing record.

Please let me know if I may be of further assistance.

Sincerely,

Enclosure

[1] Questions for the record related to this hearing were received on May 24, 2024.

Question for The Honorable Michael Barr, Vice Chair for Supervision, Board of Governors of the Federal Reserve System, from Representative William Timmons:

1. **Duplicate Check Fraud**
   Thank you for your thoughtful answer to my question on whether the Federal Reserve has explored technological solutions to enable real-time fraud detection to address rising rates of check fraud, particularly duplicate presentment fraud. You answered that the Federal Reserve is "looking at various technological ways that [it] can help" combat this growing problem. I was hoping you could expand on these efforts.

   a. **What specific technological solutions is the Federal Reserve currently exploring to address increasing check fraud rates, including in response to heightened instances of duplicate presentment fraud?**

   b. **Would these efforts enable real-time fraud detection across all check-processing organizations?**

   c. **If these efforts include operationalizing the Federal Reserve's Duplicate Check Notifier Service, what is the timeline for enabling money services businesses to access this system?**

The Federal Reserve is committed to advancing the safety of payment services and that includes providing fraud mitigation products and services. Our FedDetect® Duplicate Treasury Check Notifier Service (FedDetect) offers the bank where the check was deposited early notice of potential duplicate Treasury checks. While checks do not clear in real time, FedDetect aims to provide fraud notifications to financial institutions at the earliest and most effective point in the check clearing process. Additionally, checks deposited through money services businesses may be screened but only if their bank clears the checks through the Federal Reserve Banks and chooses to use FedDetect. The Federal Reserve continues to explore opportunities that could further help banks mitigate payments fraud.

FDIC
Federal Deposit Insurance Corporation
550 17th Street NW, Washington, DC 20429
Office of Legislative Affairs

November 15, 2024

The Honorable Patrick McHenry
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman McHenry:

Thank you for your letter enclosing Questions for the Record from members subsequent to the testimony by Martin Gruenberg, Chairman, Federal Deposit Insurance Corporation, at the Committee's March 15, 2024, hearing entitled "Oversight of Prudential Regulators." Enclosed are Chairman Gruenberg's responses.

If you have any questions regarding these responses, please contact the Office of Legislative Affairs at (202) 898-7055.

Sincerely,

M. Andy Jiminez
Director
Office of Legislative Affairs

Enclosure

Questions for the Record from Representative Andy Barr for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **It appears that the FDIC chose not to coordinate or in any way align its proposed bank merger policy statement with the OCC or Federal Reserve. This can create uncertainty for banks because the merger review processes are different based on their primary regulator and different again for their bank holding company if they have one. Please explain why the FDIC chose not to coordinate with the other federal banking agencies to ensure a consistent approach to merger reviews.**

Response:

On September 17, 2024, the FDIC's Board approved a final Statement of Policy on Bank Merger Transactions (Final SOP). The Final SOP is generally consistent with merger application evaluations performed by the OCC and Federal Reserve and was guided by comments received from the public as well as discussions with the other federal banking agencies and the U.S. Department of Justice.

The FDIC will continue to coordinate with the federal prudential bank regulators as well as with the U.S. Department of Justice regarding interagency efforts to review of the existing laws, regulations, guidance, and processes used by the federal banking agencies under the Bank Merger Act.

2. **In his statement accompanying his vote against issuing the proposed bank merger policy for comment, Director McKernan stated, "I have not been persuaded that there is a basis in law for an expectation that the post-merger bank do 'better' on the convenience and needs factor." Please point to and explain the statute on which the FDIC is relying on to adopt a new expectation "that a merger between IDIs will enable the resulting IDI to better meet the convenience and the needs of the community to be served than would occur absent the merger?"**

Response:

When evaluating a merger transaction, the Bank Merger Act requires the responsible agency to consider a number of factors set forth in the Bank Merger Act[1], as amended by the USA Patriot Act[2] and the Dodd-Frank Wall Street Reform and Consumer Protection Act.[3] Among these is the convenience and needs of the community to be served.[4] As such, the FDIC Board retains authority to evaluate any merger transaction for which one or more of the statutory factors are not favorably resolved. To that end, the Final Statement of Policy provides greater detail and

[1] See Bank Merger Act of 1960, Pub. L. No. 86-463 (May 13, 1960) subsequently amended by Bank Merger Act of 1966, Pub. L. No. 89-356 (Feb. 21, 1966). See also
[2] See USA PATRIOT Act, Pub. L. No. 107-56, § 327(b) (Oct. 26, 2001).
[3] See Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 604(f) (July 21, 2010).
[4] 12 U.S.C. § 1828(c)(5).

transparency on how the FDIC will evaluate that factor by emphasizing the FDIC's expectation that a merger between IDIs will better meet the convenience and needs of the community in order for staff to find favorably on this factor.

3. **Earlier this month, the FDIC issued a joint proposed rulemaking on incentive-based compensation agreements for public comment with only the OCC and FHFA joining. Vice Chairman Hill gave pause, saying "It is extremely odd to issue this proposal without all the relevant agencies participating.**

    a. **Should commenters invest time and resources to respond to this proposal, or wait until all the relevant agencies are in agreement?**

Response:

On May 3, 2024, the FDIC Board of Directors approved a Notice of Proposed Rulemaking (NPR) and request for comment entitled Incentive-Based Compensation Arrangements, a rule to implement Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).[5] In this NPR, the FDIC, the Office of Comptroller of the Currency (OCC), the National Credit Union Administration (NCUA), and the Federal Housing Finance Agency (FHFA) (collectively the "Agencies" for purposes of the NPR) re-proposed the regulatory text previously proposed in June 2016, along with certain alternatives and questions, for public comment.[6] The NPR would provide a consistent set of enforceable standards and help safeguard covered financial institutions from certain types and features of incentive-based compensation arrangements that encourage inappropriate risks by providing excessive compensation or that could lead to material financial loss to the institution.

Until this proposed rulemaking is published in the Federal Register, comments on the proposed rule and alternatives in the preamble can be sent to IncentiveCompProposal2024@fdic.gov and will be posted on the FDIC website at https://www.fdic.gov/regulations/laws/publiccomments/.

    b. **Why did the FDIC issue for comment a rulemaking that does not include all the agencies required to participate by law?**

Response:

In considering earlier legislation that formed the basis for section 956, the majority members of

[5] See Incentive-Based Compensation Arrangements, FIL-21-2024 (May 6, 2024) available at https://www.fdic.gov/news/financial-institution-letters/2024/incentive-based-compensation-arrangements.
[6] See Incentive-Based Compensation Arrangements, 81 Fed. Reg. 37670 (proposed June 10, 2016) (to be codified at 12 C.F.R. pt. 372) available at https://www.govinfo.gov/content/pkg/FR-2016-06-10/pdf/2016-11788.pdf.

the Committee on Financial Services of the House of Representatives found that "a broad consensus has developed that executive and financial institution compensation structures relate directly to both the safety and soundness of individual financial institutions and the health of the broader financial system."[7] The FDIC agrees that misaligned compensation incentives are a serious safety and soundness concern and issued the proposal because experience shows that this area continues to present a safety and soundness risk. When poor compensation practices involve the largest financial institutions, the negative impacts of inappropriate risk-taking can have broader consequences for the financial system.

Material Loss Reviews of failed institutions issued by the Inspectors General for the three federal banking agencies between 2007-2010 found that, in a number of instances, poor compensation practices were a contributing factor to the institution's failure
More recent supervisory experience continues to demonstrate the potential negative impact of misaligned incentive-based compensation arrangements on financial institutions. For example, the bank failures in March 2023 highlighted the importance of a financial institution's risk management practices and governance arrangements, including the incentives provided by senior management compensation schemes. A report on the failure of Silicon Valley Bank noted that compensation packages of senior management through 2022 were tied to short-term earnings and equity returns and did not include risk metrics.[8] As such, the report concluded that managers had a financial incentive to focus on short-term profit over sound risk management.

4. **Under FDIC receivership, the SVB and Signature bridge banks borrowed upwards of $180 billion from the Federal Reserve. You previously told us when the bridge banks went into receiverships, those loans were considered in "technical default" and began to accrue a penalty interest rate.**

    a. **When were those loans repaid?**

Response:

Both Silicon Valley Bridge Bank, National Association (SVBBB.) and Signature Bridge Bank, National Association (SBB) were federally-chartered, full-service banks which possessed the same powers as any national bank, including the ability to borrow from the Federal Reserve. The Federal Reserve Board borrowings of both SVBBB and SBB were subsequently inherited by the FDIC as receiver, and were required to be repaid over time from the inception of the receiverships until they were fully repaid (for SVBBB on 11/30/2023 and for SBB on 10/10/2023). Proceeds from the sales of assets of the failed firms were used to repay Fed borrowings over time to continually lower the balances.

[7] See H.R. Rep. No. 111-236, at 6 (July 30, 2009).
[8] See Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank (April 28, 2023) available at https://www.federalreserve.gov/publications/files/svb-review-20230428.pdf.

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The Honorable Martin J. Gruenberg
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b. **When did the FDIC begin to consider refinancing these loans?**

Response:

The Federal Reserve borrowings of SVBBB and SBB inherited by the FDIC as receiver were not refinanced. They were repaid through the sale of assets of the failed firms. See the response to Question 4.a (*supra*).

c. **Did politics or the optics of turning to Treasury affect the decision not to seek alternative funding sooner?**

Response:

Neither SVBBB nor SBB sought alternative funding during the period of time in which the bridge institutions were operating. Throughout the bridge period, however, the FDIC continually evaluated the options for meeting the liquidity and funding needs of the bridge institutions while also ensuring adequate liquidity was preserved for potential additional bank failures.

5. **A recent report states that 38% of FDIC staff were considering leaving within the next year, more than double that of 2020. And examiner retention was one issue cited in your very own report on the stability-threatening failure of Signature Bank.**

a. **How do you expect to guard against threats to systemic stability and oversee the safety and soundness of the banking system with staff retention threats this large**

Response:

Developing and maintaining a strong workforce has been, and remains, a top strategic priority for the FDIC,[9] as has been managing the challenges associated with a highly tenured workforce.[10] More recently, the report of the FDIC Chief Risk Officer evaluating the FDIC's supervision of Signature Bank from 2017 until its failure in March 2023, resource challenges with examination staff was identified as one of the challenges that affected the timeliness and quality of Signature Bank examinations.[11] These challenges were the result of a number of factors.

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[9] See FDIC 2022-2026 Strategic Plan (December 14, 2021) available at https://www.fdic.gov/strategic-plans/fdic-2022-2026-strategic-plan.
[10] *Id.* See also, FDIC OIG Audit, *The FDIC's Management of Employee Talent*, AEC Memorandum No. 21-002 (September 2021) available at https://www.fdicoig.gov/sites/default/files/reports/2022-08/AEC-Memorandum-21-002.pdf.
[11] See *FDIC's Supervision of Signature Bank* (April 28, 2023), available at https://www.fdic.gov/news/press-releases/2023/pr23033a.pdf.

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Nearly every employee in the FDIC's Division of Risk Management Supervision is a commissioned examiner. Examiners are highly specialized with a high level of expertise, requiring four years of intensive training to earn a basic examiner commission. Examiners for largest, most complex banks generally have many more years of experience.

Like other agencies and private employers, the FDIC experienced a higher-than-normal level of separations in 2021 and 2022, primarily among pre-commissioned examiners. In response, the FDIC took steps to redirect and supplement examiner resources, implementing contingency operating measures allowing for temporary reassignment of qualified employees across the agency to assist with examinations; leave buybacks, leave rollover, and overtime to expand hours available for examination work; use of rehired annuitants; hiring of industry experts to assist with examination work; and pursuit of contracted assistance.

More recently, the FDIC has taken a number of actions to address examiner retention. Throughout 2023, examiner attrition returned to nearly historical levels from the heightened levels seen in 2021 and 2022.

The FDIC experienced an unwillingness of staff to relocate to the New York City area during the COVID-19 pandemic. Another more widespread challenge has been filling dedicated examiner positions in high-cost areas, New York, NY in particular. In response to this challenge, the FDIC has taken a number of actions to enhance the attractiveness of the dedicated examiner position, including adding a corporate expert level examiner-in-charge, adding six deputy examiners-in-charge, increasing the grade of 21 examiner-in-charge positions, and instituting an incentive payment for dedicated examination team leaders; taken steps to address the high cost of living in San Francisco, New York, Seattle, and Los Angeles by adding a payment supplement to address the gap between the cost of labor and the cost of living; offered eligible examiners and case managers indicating their intent to retire before year-end a retention payment to stay for one or two additional years; and increased the career ladder for a journeyman examiner from CG 7 – CG 12, to CG 7 – CG 13 in recognition of increases in the complexity of the workload.

More broadly, the FDIC has implemented a number of initiatives to develop and maintain an expert and experienced workforce. The FDIC engages in regular hiring of new examiner candidates and has enjoyed large applicant pools and strong rosters. The FDIC also offers employees highly competitive compensation, a generous benefits program, and extensive career development opportunities. The FDIC continues to enhance data collection and analysis efforts to inform development and implementation of succession management strategies over the next several years. These efforts include specific recruitment and development strategies to support a high performing workforce that reflects the communities we serve by optimizing experiences throughout an employee's career.

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6. **According to the recent report, FDIC staff who felt FDIC management maintained "high standards of honesty and integrity" is down 56 percent since 2020, at the very low rate of 18 percent. And only 52 percent of staff expressed a high level of respect for your leadership. This is a widespread problem that impedes the agency's ability to supervise, regulate, and resolve banks. How can you continue to serve in your capacity when this is what the data show?**

Response:

The FDIC has implemented a number of strategies to strengthen its workplace culture and enable employees to elevate concerns to the most senior levels of leadership. This includes the Workplace Excellence (WE) Program[12], the FDIC Labor Management Forum (LMF)[13], the FDIC Employee Resource Group (ERG)[14] Program, as well as the Chairman's Diversity Advisory Council (CDAC).[15] More recently, the FDIC has implemented a comprehensive agency-wide Plan for cultural transformation, which includes initiatives aimed at strengthening leadership accountability.[16] The plan was prepared at my request by FDIC senior leadership and staff. The Plan reflects comments and suggestions received during listening sessions held with FDIC employees in November. The Plan also reflects input from a range of FDIC stakeholders, including the Diversity and Inclusion Executive Advisory Council, personnel in the Office of Minority and Women Inclusion, and the employee resource groups. Strengthening the agency workplace culture and ensuring strong leadership has, and will remain, a top priority and will require the commitment and attention of the agency Board and senior leadership.

7. **Sections 521 through 523 of the Depository Institutions Deregulation and Monetary Control Act of 1980 (DIDMCA) were enacted in response to a 1978 U.S. Supreme Court. These sections authorize state chartered insured depository institutions (and certain other banks) the authority to authority to export interest rates permitted by their home state to provide a level playing field and prevent discrimination. Section**

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[12] The WE Program provides a forum where diverse employees across various organizations, share their perspectives on the FDIC work environment and collaborate on workplace improvements. In previous years, the successful launch of this program led to 10 Division/Office WE Councils and actively engaged 75% of all FDIC employees through WE employee engagement activities and accomplished over 80 WE Steering Committee and Council Projects and initiatives.

[13] The LMF is a mechanism to provide NTEU with pre-decisional input on workplace matters to the fullest extent practicable, without regard to whether those matters are negotiable subjects of bargaining. Together with the Workplace Excellence Program, the LMF strives to enhance communications, employee input and morale throughout FDIC.

[14] ERGs are FDIC-recognized networks of employees with common goals, interests, or experiences which are established to foster and encourage equality of opportunity, respect, and fair treatment for all.

[15] The mission of the Chairman's Diversity Advisory Councils (CDACs) is to provide advice to the FDIC Chairman, through the Office of Minority and Women Inclusion (OMWI) Director, on diversity and inclusion (D&I) issues and concerns.

[16] See FDIC Action Plan for a Safe, Fair, and Inclusive Work Environment, available at https://www.fdic.gov/action-plan.

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525 permits states to opt-out of this regime for loans made in those states. On June 5, 2023, Colorado passed a law that would exclude consumer loans made in Colorado from section 521 of the DIDMCA. Three consumer financial services industry trade groups brought suit in Federal court, requesting a declaratory judgment holding that this Colorado law is invalid as to loans that are not "made in" Colorado.

The FDIC took the unusual step to file an amicus brief in this litigation, arguing that Colorado can legally impose an interest rate cap on loans made by state-chartered banks that are headquartered in any state other than Colorado.

a. **Please explain whether the position taken by the FDIC in the amicus brief is consistent with prior positions taken by the FDIC in determining where a loan is made?**

Response:

The positions expressed in the amicus brief are consistent with prior FDIC statements regarding Sections 521 and 525 of DIDMCA. The FDIC submitted its amicus to brief to underscore that the FDIC General Counsel's Opinion 11[17] (Opinion 11) is inapplicable to the opt-out issue in the above-referenced litigation. Plaintiffs have suggested Opinion 11 provides the relevant framework for determining the scope of loans covered by Section 525's opt-out provision. However, as the FDIC's amicus brief explains, Opinion 11 only addresses where a bank is "located" for purposes of Section 521 and does not address Section 525 or states opt-out rights. The FDIC felt it was important to clarify to the court its interpretation of Opinion 11.[18]

b. **Please explain whether the FDIC believes that states still have authority to opt out of the DIDMCA despite subsequent legislative developments?**

Response:

States retain opt-out rights under Section 525 of DIDMCA despite subsequent legislative developments.

Section 521 of DIDMCA allowed state-chartered insured banks, like their national bank counterparts, to charge interest at the rates allowed at the "federal" rate authorized under the

[17] See General Counsel's Opinion No. 11.: Interest charges by interstate state banks, 63 Fed. Reg. 27282 (May 18, 1998), available at https://archive.fdic.gov/view/fdic/5180.
[18] See Federal Deposit Insurance Corporation's Unopposed Motion for Leave to File an Amicus Curiae Brief in Support of Defendants National Association of Industrial Bankers, American Financial Services Association, and American Fintech Council v. Philip J. Weiser, Attorney General of the State of Colorado, and Martha Fulford, Administrator of the Colorado Uniform Consumer Credit Code, Civil Action No. 1:24-cv-812-DDD-KAS (April 23, 2024).

National Bank Act or the state where the bank is located. Sections 522 and 523 respectively provided similar rights to savings and loan institutions ("S&L institutions") and credit unions.

Section 525 of DIDMCA permits states to enact "opt-out" legislation overriding the provisions in "sections 521 through 523." When incorporating Section 525 into Title 12 of the U.S. Code, the Office of the Law Revision Counsel included the provision's text in various notes following the interest-rate authorities to which they correspond.[19]

The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), effective August 9, 1989, repealed Title 4 of the National Housing Act (12 U.S.C. § 1724 *et seq.),* which included § 1730g note and the opt-out language corresponding to S&L institutions.[20] FIRREA did not purport to repeal Section 525 of DIDMCA. In addition, nothing in FIRREA purported to repeal anything in § 1785 note (applicable to credit unions) or § 1831d note (applicable to state-chartered insured depository institutions) neither of which was part of the National Housing Act.

Given the targeted scope of this repeal, the FDIC believes that Section 525's opt-out provision remains in force to the extent that DIDMCA's interest-rate authorities apply to state-chartered insured depository institutions.[21]

c. **Please explain whether the FDIC believes that Colorado's law will discourage banks from choosing a state, rather than national, charter?**

Response:

Section 525 permits a state to opt out of Section 521's interest-rate regime with respect to loans "*made in*" that state. To effect this opt-out, Section 525 instructs a state to enact a law providing "*explicitly and by its terms*" that it does not want Section 521 to apply to loans "*made in such State.*" But a state can revisit an earlier opt-out decision by repealing or rescinding any such state-enacted law. For example, seven states and Puerto Rico exercised their opt-out right under Section 525 shortly after DIDMCA's passage. Since then, six of these states have repealed or

[19] *See* 12 U.S.C. §§ 1730g note (S&L institutions subject to Section 522), 1785 note (credit unions subject to Section 523), 1831d note (state-chartered insured depository institutions subject to Section 521). "[W]hether . . . a provision is . . . set out as a section or a statutory note[] does not in any way affect the provision's meaning or validity." OFFICE OF THE LAW REVISION COUNSEL, About Classification of Laws to the United States Code, https://uscode.house.gov/about_classification.xhtml. The classification decision instead reflects an "editorial judgment." *Id.* Therefore, statutory notes are binding law. *E.g.*, *SEC v. Hallam*, 42 F.4th 316, 335 n.76 (5th Cir. 2022).

[20] *See* Financial Institutions Reform, Recovery and Enforcement Act of 1989, § 407, Pub. L. No. 101-73, 103 Stat. 183, 363 (1989) ("Title 4 of the National Housing Act (1724 et seq.) is hereby repealed.").

[21] This view is consistent with the position expressed in the FDIC's Federal Interest Rate Authority Rulemaking. *See* 85 Fed. Reg. at 44,147 n.17 (citing 12 U.S.C. § 1831d note to describe states' opt-out authority under DIDMCA).

rescinded their opt-out statutes and reentered Section 521's interest-rate regime. Both Iowa and Puerto Rico, however, have not repealed or rescinded their opt-out statutes since both states passed these laws in 1980.

The FDIC observes that a robust dual banking system has endured throughout DIDMCA's existence and that banks have readily continued to seek state charters. The dual banking system has also withstood various states' decisions to opt out of Section 521's interest-rate regime. To that end, Iowa and Puerto Rico's historical experience suggests that state banking systems successfully operate under the opt-out regime.[22] Therefore, the FDIC believes that the Colorado law will not significantly impact banks' chartering decisions.

8. **Chairman Powell has repeatedly said that there would be broad and material changes to the Basel III Endgame proposal based on the comments received. In light of the volume and breadth of comments submitted from individuals and institutions across U.S. markets, political spectrum, and geography, it is clear that this proposal should be withdrawn and re- proposed. The comments reveal particular downsides of the proposal for the availability and cost of credit for small and medium-sized businesses.**
    a. **In finalizing any Basel-related rules under consideration, specifically as they relate to credit risk calculations, will due consideration be given to the call for continuing flexibility to recognize the value of for highly liquid non-financial collateral, such as accounts receivable and inventory?**

    b. **Does the special data collection referenced in your comments include the data drawn from the agencies' direct oversight (and which informs current regulatory guidance), which support the distinction among different types of loan structures and has been provided by commenters for review?**

    c. **Will consideration be given to the impact of the rules on the amount of capital required to support a swingline loan structure and the disincentives it will pose, particularly when fronting exposure is mitigated by reimbursement obligations owing from highly secure investment grade financial institutions?**

Response:

[22] Other states have operated both within and outside Section 521's interest-rate regime for significant time periods. For example, Colorado was one of the seven states that originally opted out under Section 525, 1981 Colo. Sess. Laws, ch. 73, § 1, and operated under an opt-out regime for thirteen years, 1994 Colo. Sess. Laws, ch. 272, § 12.

Questions for the Record from Representative Andy Barr for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
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The Federal Reserve, OCC, and the FDIC have worked cooperatively on the Basel III proposal.[23] The Federal banking agencies have received over 400 unique comment letters relating to the Basel III Endgame proposal and have also met with interested parties over 50 times. The FDIC greatly values all feedback received on the proposal and is carefully considering all comments received including those comments concerning the availability and cost of credit for small and medium-sized businesses.

The Federal Reserve Board launched a special data collection in October 2023[24] to gather more information from the banks affected by the Basel III Endgame proposal. Per the Federal Reserve website, the additional data will further clarify the estimated effects of the proposal and inform any final rule, with summaries to be made public. The submission deadline for the data collection was January 16, 2024.

On September 10, 2024, Federal Reserve Vice Chair Barr outlined a number of potential changes to the 2023 proposed rule that are responsive to commenters' concerns relating to credit risk, operational risk, and market risk.[25] I look forward to the agencies working together to bring Basel III to a conclusion that will strengthen bank capital and bolster financial system resilience and stability in light of the experience during the 2008 global financial crisis.

[23] See Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64018 (September 18, 2023) available at https://www.fdic.gov/sites/default/files/2024-03/2023-07-27-notice-dis-a-fr.pdf.
[24] See https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231020b.htm
[25] See *The Next Steps on Capital*, Vice Chair for Supervision Michael S. Barr at the Brookings Institution, Washington, D.C. (September 10, 2024) available at https://www.federalreserve.gov/newsevents/speech/barr20240910a.htm.

Questions for the Record from Representative Bill Huizenga for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **In your testimony before the Committee, you stated that four FDIC employees who engaged in misconduct this year have been separated from the agency.[26] Please provide the following information for each employee that was separated:**
    a. **Each employee's position;**
    b. **Whether the employee received a termination notice or was informed of disciplinary action;**
    c. **The date the employee received a termination notice or was informed of disciplinary action;**
    d. **The date the employee was separated;**
    e. **Whether the employee left the agency or retired.**

Response:

Employee #1 was a Senior Risk Examiner. On November 16, 2023, the Employee was informed that his conduct would be investigated. Subsequently, on that same day, the Employee communicated his intent to retire. The employee retired effective November 30, 2023.

Employee #2 was a Field Supervisor. The FDIC proposed the Employee's removal on January 24, 2024. On April 15, 2024, the FDIC amended the proposal to include additional charges of misconduct that surfaced subsequent to the issuance of the initial proposal. The FDIC removed the employee on May 14, 2024.

Employee #3 was a Senior Examination Analyst. The FDIC proposed the Employee's removal on March 27, 2024. The employee retired effective April 5, 2024.

Employee #4 was a Financial Institution Specialist still in the initial trial period. On April 19, 2024, the Employee was informed that he would be removed effective April 23, 2024. the Employee resigned from the FDIC on April 22, 2024.

2. **To better understand the FDIC's response to addressing misconduct in the workplace, please provide the following:**
    a. **The number of employees that have received termination notices or been informed of disciplinary action since November 13, 2023;**
    b. **The number of employees that have received termination notices or been informed of disciplinary action since May 7, 2024.**

[26] *Oversight of Prudential Regulators: Hearing before the H. Comm. on Financial Services* 118th Cong. (May 15, 2024), 84.

Questions for the Record from Representative Bill Huizenga for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

Response:

Since November 13, 2023, twenty-five employees have been disciplined, informed of disciplinary action, or counseled in writing in connection with harassment or similar interpersonal misconduct. Of this number, fifteen employees have been disciplined, informed of disciplinary action, or counseled in writing since May 7, 2024.

Questions for the Record from Representative Jim Himes for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **Last month, the FDIC considered two proposals related to asset managers' investments in banks. Both proposals would have addressed situations in which an asset manager's funds collectively own more than 10% of a particular bank. In your remarks, you stressed that all three banking regulators need to be coordinated on this issue, because all three agencies have equities here. Can you expand on why the agencies need to coordinate on this particular issue?**

   a. **Chairman Gruenberg – do you agree that it's important for the regulators to address this issue on an interagency basis?**

Response:

The FDIC has observed a growth in passive investment funds and fund complexes along with developments in the equity markets that may be contributing to elevated risk of excessive indirect control and concentration of ownership in FDIC-supervised institutions. As the primary federal regulator of state non-member banks, it is important that the FDIC closely reviews who is exercising direct or indirect control over its supervised institutions.

The proposed rule to amend the FDIC's regulations under the Change in Bank Control Act was published in the *Federal Register* on August 19, 2024. Comments closed on October 18, 2024, following a 60-day comment period. The FDIC engaged with the staff of the OCC and the Federal Reserve Board in connection with this proposal. The FDIC requested comment on all aspects of the proposed rule and asked multiple questions, such as what steps should be taken on an interagency basis to ensure the appropriate review of transactions involving an indirect acquisition of control of an institution. The FDIC will consider all comments carefully before finalizing the rule.

The FDIC is committed to developing an interagency approach to change in control notices and will continue to engage in dialogue and coordination with the other Federal banking agencies.

Questions for the Record from Representative Bill Foster for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **Thank you for your decision to conduct a quantitative impact study (QIS) on the impact of the Basel III Endgame proposal. I believe it is an important exercise that will help our committee and the public better understand the real impact of what is being proposed on the U.S. economy. I think it is important for the findings of the QIS to be made public and allow for public engagement on the findings as you continue working to reach consensus on the proposal.**

    a. **Chair Gruenberg, do you intend to release the QIS results for public comment and use public comments on the results to inform next steps on the rule?**

    b. **What is the path forward for the Basel III Endgame QIS and final rule. Can you share any additional information regarding process, timing, and substance?**

Response:

The Federal Reserve Board launched a special data collection in October 2023[27] to gather more information from the banks affected by the Basel III Endgame proposal. Per the Federal Reserve website, the additional data will further clarify the estimated effects of the proposal and inform any final rule, with summaries to be made public. The submission deadline for the data collection was January 16, 2024. Questions related to the release of the QIS results should be directed to the Federal Reserve.

The Federal Reserve, OCC, and the FDIC have worked cooperatively on the Basel III proposal.[28] The Federal banking agencies have received over 400 unique comment letters relating to the Basel III Endgame proposal and have also met with interested parties over 50 times. The FDIC greatly values all feedback received on the proposal and is carefully considering all comments received including those comments concerning the availability and cost of credit for small and medium-sized businesses

On September 10, 2024, Federal Reserve Vice Chair Barr outlined a number of potential changes to the 2023 proposed rule that are responsive to commenters' concerns relating to credit risk, operational risk, and market risk.[29] I look forward to the agencies working together to bring Basel III to a conclusion that will strengthen bank capital and bolster financial system resilience and stability in light of the experience during the 2008 global financial crisis.

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[27] See https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231020b.htm
[28] See Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64018 (September 18, 2023) available at https://www.fdic.gov/sites/default/files/2024-03/2023-07-27-notice-dis-a-fr.pdf.
[29] See *The Next Steps on Capital*, Vice Chair for Supervision Michael S. Barr at the Brookings Institution, Washington, D.C. (September 10, 2024) available at https://www.federalreserve.gov/newsevents/speech/barr20240910a.htm.

Questions for the Record from Representative William Timmons for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **Over the last four years how often has the Regional Office or Washington changed the exam ratings recommended by the examiners?**

Response:

During the time period of 2020 – 2023, the Division of Risk Management Supervision has processed 11,524 examinations. The component and/or composite ratings have been adjusted in 1.21 percent of total examinations (140 / 11,524). Specifically, ratings were upgraded at 0.37 percent (43) and downgraded at 0.84 percent (97) of total examinations.

Over the four-year period, the Division of Depositor and Consumer Protection processed 3,951 examinations. Of these, the Division of Depositor and Consumer Protection Regional Offices or Washington Office has changed the Community Reinvestment Act and consumer compliance composite ratings at 0.48 percent of total examinations (19/3,951). Specifically, there have been eight upgrades and four downgrades to the consumer compliance composite ratings, and two upgrades and five downgrades to the Community Reinvestment Act composite ratings.

2. **In the past 4 years, what percentage of banks added to the Problem Bank List are those active in the fintech (third-party relationships) space?**

Response:

Within the past four years (January 2020 – May 2024), 12 percent of the FDIC-supervised banks added to the problem bank list were active in the fintech (third-party relationship) space.

3. **In the past 4 years, what percentage of examinations start prior to issuance of a Report of Exam from the prior exam and/or issuance of a Supervisory Letter from the prior visitation?**

Response:

The Division of Risk Management Supervision conducts two types of examinations: point-in-time examinations and continuous examinations. Certain supervisory procedures and processes for large state non-member banks are distinct from those of community banks. Due to the size and complexity of these institutions, the FDIC generally assigns dedicated staff and employs a continuous examination process, which differs significantly from point-in-time examinations typically conducted in community banks.

All continuous safety and soundness examinations will begin prior to the issuance of the previous Report of Examination, unless an institution is moving from a point-in-time examination approach to the continuous examination approach. The continuous examination

cycle is twelve months, and the Report of Examination is issued within 120 days of the conclusion of the examination cycle.

Generally, point-in-time examinations will not begin prior to the issuance of the previous Report of Examination. Over the past four years (January 2020 through May 2024) less than one percent of point-in-time examinations started before the previous examination was mailed. More than 5,800 examinations were conducted during this period and 8 started before the prior examination was mailed.

Typically, another compliance examination would not begin prior to the issuance of a Report of Examination of a prior examination for the Division of Depositor and Consumer Protection (DCP). As for Supervisory Letters, those are issued for our continuing exam banks throughout the exam cycle and then taken into the overall exam report when issued. DCP would have Supervisory Letters in process for the next exam cycle while we wrap up the current exam as we have an examination plan for each year that we implement.

4. **Does FDIC agree with the recent GAO's statement that FDIC policy requires that all supervisory concerns must be communicated in writing?**

Response:

Yes. The July 2016 Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations states[30]: "*Communicate Concerns Clearly and in Writing*. Supervisory recommendations must be made in writing in either a Report of Examination or other official FDIC communication. Supervisory recommendations may not be solely verbal, but should be discussed with, and explained to, bank management. FDIC personnel should present information in a fact-based, diplomatic, and objective manner that clearly and concisely supports all recommendations. Comments should describe the deficient practices, operations, or financial condition and how it deviates from sound governance, internal controls, or risk management or consumer protection principles, or legal requirements, as well as how the continuation of the deficiency could adversely affect the bank's financial condition or operations, cause consumer harm, or result in further supervisory action in the future.

5. **To what extent does FDIC hold banks to corrective or remedial actions which are not communicated in writing? Please provide a copy of the 8/29/2023 FDIC Memorandum to its regional directors regarding such communication of supervisory concerns.**

[30] See Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations at https://www.fdic.gov/resources/supervision-and-examinations/statement-on-recommendations.html

Questions for the Record from Representative William Timmons for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
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Response:

The FDIC does not hold banks to corrective or remedial actions that are not communicated in writing. As required by the July 2016 Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations, [31] corrective or remedial actions for Supervisory Recommendations, including Matters Requiring Board Attention must be made in writing and communicated through the Report of Examination, Supervisory Letter, or other written communication on official FDIC letterhead. Supervisory Recommendations, including Matters Requiring Board Attention, are followed up on as part of interim supervisory activities and/or at subsequent examinations or reviews.

The primary directive regarding communication of supervisory concerns is the July 2016 Board Statement that also describes the purpose of informal communications: "*Appropriate use of Informal Communication*. The FDIC Board of Directors recognizes that informal communication promotes an ongoing dialogue and remains a vital part of a sound, effective, and efficient supervision program. Informal communication occurs in many forms. For example, examiners may make verbal suggestions to address minor issues identified during an examination. In addition, bankers routinely ask examiners, without attribution, to describe effective practices observed at other institutions. FDIC encourages these types of communication but does not consider these conversations to be a supervisory recommendation. Accordingly, informal communications should not be used to convey expectations of action by bank management and will not be tracked as part of the FDIC's examination follow-up supervisory activities or at subsequent examinations."

The August 29, 2023, Regional Director Memorandum regarding supervisory recommendations including matters requiring board attention and progressive supervisory response is an internal procedure that implements instruction in the FDIC's Formal and Informal Enforcement Actions Manual[32]. Those instructions are found under the heading, Considerations for Appropriate Action, in Chapter 1 of the Manual, Overview and Administrative Matters, and state:

"When actionable misconduct is detected early, staff should bring these matters to the attention of insured depository institutions (IDI) management and engage in discussions regarding the problem areas and potential remedial steps. The ability for staff and management to engage in discussions is a vital and longstanding part of the examination process, and often results in the type of early intervention that is necessary to correct problems before they become serious. If management is able to correct deficiencies within a reasonable

19 See Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations at https://www.fdic.gov/resources/supervision-and-examinations/statement-on-recommendations.html
32 See Formal and Informal Enforcement Actions Manual at https://www.fdic.gov/system/files/2024-07/ch-01.pdf

timeframe, then supervisory recommendations[33] for corrective action in the Report of Examination could be a sufficient supervisory response, subject to appropriate follow-up during an interim contact, on-site visitation, or the next examination.

If this process does not achieve the desired result, an informal or even formal corrective action may be warranted. Additionally, certain forms of misconduct require enforcement by law, including the assessment of civil money penalties for certain violations of the Flood Act, restitution for certain Truth in Lending Restitution violations, and the referral of certain Equal Credit Opportunity Act violations to the U.S. Department of Justice."

However, as stated above, the primary source of examination policies regarding communication of supervisory concerns is the July 2016 Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations. Additional information on communicating supervisory concerns can be found in the Risk Management Manual of Examination Policies - Section 16.1 Report of Examination Instructions and Consumer Compliance Examinations—II-6.1 Communicating Findings.[34]

6. In the past 4 years, how many and what percentage of Section 38 Prompt Corrective Action escalations were for banks active in the fintech (third-party relationships) space?

Response:

None of the PCA Directives issued to FDIC-supervised banks over the past 4 years are banks active in the fintech (third-party relationship) space.

7. In the past 4 years, how many and what percentage of Section 39 Non-Capital Action escalations were for banks active in the fintech (third-party relationships) space?

Response:

Within the past 4 years (January 2020 – May 2024), the FDIC requested one FDIC-supervised bank that is active in the fintech (third-party relationship) space to submit 2 plans under

[33] The term "supervisory recommendations" refers to FDIC communications with an IDI that are intended to inform the IDI of the FDIC's views about changes needed in its practices, operations or financial condition. See Statement of FDIC Board of Directors on the Development and Communication of Supervisory Recommendations at https://www.fdic.gov/resources/supervision-and-examinations/statement-on-recommendations.html

[34] See Risk Management Manual of Examination Policies - Section 16.1 Report of Examination Instructions at https://www.fdic.gov/resources/supervision-and-examinations/examination-policies-manual/section16-1.pdf Also Consumer Compliance Examinations —II-6.1 Communicating Findings at https://www.fdic.gov/resources/supervision-and-examinations/consumer-compliance-examination-manual/documents/2/ii-6-1.pdf

Questions for the Record from Representative William Timmons for
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Section 39, representing 67 percent of Section 39 plans in that period.

8. In the past 4 years, what percentage of *formal* enforcement actions were for banks active in the fintech (third-party relationships) space? In that same period, what percentage of *informal* enforcement actions were for banks active in the fintech (third-party relationships) space?

Response:

Within the past four years (January 2020 – May 2024), 14 percent of the formal enforcement actions for FDIC-supervised banks were issued to those active in the fintech (third-party relationship) space.

Within the past four years (January 2020 – May 2024), 9 percent of informal enforcement actions for FDIC-supervised banks were issued to those active in the fintech (third-party relationship) space.

Questions for the Record from Representative Brad Sherman for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **<u>Coordination with Federal Home Loan Banks:</u> Having liquidity options is critical. The prudential regulators have made it a priority to ensure that your regulated entities can access the Federal Reserve's Discount Window if necessary.**

   a. **What percentage of the banks under your supervision have accessed the Window this calendar year? Are all banks under your supervision ready to tap the facility if they need contingent liquidity right now?**

<u>Response:</u>

The FDIC does not have access to data regarding each use of the Discount Window. That information is more appropriately maintained by the Federal Reserve Board. However, the Federal banking agencies and the National Credit Union Administration updated supervisory guidance on "Funding and Liquidity Risk Management on the Importance of Contingency Funding Plans" in July 2023.[35] The updated guidance was intended to remind depository institutions to maintain actionable contingency funding plans, including to encourage them to incorporate the discount window as part of their contingency funding arrangements. Furthermore, banks' contingency funding plans, which should prudently include access to the Discount Window, are routinely assessed as part of the FDIC's supervision program.

   b. **It is my understanding that the Federal Home Loan Banks have worked to establish intercreditor agreements with the various Federal Reserve Banks, which allow a lender to access both the Discount Window and FHLBanks. How does (or doesn't) utilization of these agreements ensure in moments of economic stress, lenders have the necessary means to sufficient liquidity?**

<u>Response:</u>

While these agreements are largely untested in moments of economic stress, they should serve to improve depository institutions' access to a broader range of contingency funding sources.

2. **<u>Domestic Manufacturing Competitiveness:</u> The National Association of Manufacturers highlighted in its comment letter that the Basel III Endgame proposal could "significantly increase the costs of critical risk management tools for U.S. manufacturers" given increased capital requirements associated with banks' market-making activities with respect to – for example – commodity derivatives for price fluctuations in raw materials, cross-currency swaps for international currency**

[35] See Updated Guidance: Interagency Policy Statement on Funding and Liquidity Risk Management on the Importance of Contingency Funding Plans, FIL-39-2023 (July 28, 2023) available at https://www.fdic.gov/news/financial-institution-letters/2023/fil23039.html.

variations, and interest rate swaps for interest rate changes on long-term liabilities. Moreover, manufacturers say that the capital increases associated with banks' capital markets activities may hurt America's ability to outpace foreign competitors, "thus impairing the ability of U.S. manufacturers to compete on price, capture market share, and lead the world in innovation." What are your agencies' assessments of the consequences that the Basel III Endgame proposal will have for the international competitiveness of American manufacturers – and for end-users more-generally – that want to hedge their risks?

Response:

The Federal Reserve, OCC, and the FDIC have worked cooperatively on the Basel III proposal.[36] The Federal banking agencies have received over 400 unique comment letters relating to the Basel III Endgame proposal and have also met with interested parties over 50 times. The FDIC greatly values all feedback received on the proposal and is carefully considering all comments received including those comments concerning the availability and cost of credit for small and medium-sized businesses.

On September 10, 2024, Federal Reserve Vice Chair Barr outlined a number of potential changes to the 2023 proposed rule that are responsive to commenters' concerns relating to credit risk, operational risk, and market risk.[37] I look forward to the agencies working together to bring Basel III to a conclusion that will strengthen bank capital and bolster financial system resilience and stability in light of the experience during the 2008 global financial crisis.

3. **Municipal Underwriting & Infrastructure: Congress pushed through substantial legislation to encourage investments in our infrastructure like the building of roads, schools, bridges, and hospitals across the country. As we pursue these infrastructure projects, we must be mindful not to undermine these critical investments and make municipal financing more expensive. As the Government Finance Officers Association pointed out in response to Basel III Endgame: "Increases in debt service costs for municipal issuers and conduit borrowers will result in declined investment in infrastructure, public safety, education, and numerous other social services." What do your agencies anticipate are the consequences of the Basel III Endgame proposal on financing schools, roads, or other infrastructure projects?**

Response:

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[36] See Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64018 (September 18, 2023) available at https://www.fdic.gov/sites/default/files/2024-03/2023-07-27-notice-dis-a-fr.pdf.

[37] See *The Next Steps on Capital*, Vice Chair for Supervision Michael S. Barr at the Brookings Institution, Washington, D.C. (September 10, 2024) available at https://www.federalreserve.gov/newsevents/speech/barr20240910a.htm.

Questions for the Record from Representative Brad Sherman for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
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The Federal Reserve, OCC, and the FDIC have worked cooperatively on the Basel III proposal.[38] The Federal banking agencies have received over 400 unique comment letters relating to the Basel III Endgame proposal and have also met with interested parties over 50 times. The FDIC greatly values all feedback received on the proposal and is carefully considering all comments received including those comments concerning the potential impact on municipal financing.

On September 10, 2024, Federal Reserve Vice Chair Barr outlined a number of potential changes to the 2023 proposed rule that are responsive to commenters' concerns relating to credit risk, operational risk, and market risk.[39] I look forward to the agencies working together to bring Basel III to a conclusion that will strengthen bank capital and bolster financial system resilience and stability in light of the experience during the 2008 global financial crisis.

[38] See Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 Fed. Reg. 64018 (September 18, 2023) available at https://www.fdic.gov/sites/default/files/2024-03/2023-07-27-notice-dis-a-fr.pdf.
[39] See *The Next Steps on Capital*, Vice Chair for Supervision Michael S. Barr at the Brookings Institution, Washington, D.C. (September 10, 2024) available at https://www.federalreserve.gov/newsevents/speech/barr20240910a.htm.

Questions for the Record from Representative Bryan Steil for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

1. **For years, the FDIC has taken the position that the Combined Collection Method for collecting customer Social Security Numbers (SSNs) does not hinder a bank's ability to prevent and detect money laundering and the financing of terrorism. Yet, in a March 2024 release, the FDIC seems to have reversed this position by indicating that banks are required to collect all nine digits of a SSN directly from a customer, increasing risk and friction in the account verification process.**

    a. **What risks or changes have prompted the FDIC's abrupt change in policy and practice of historically allowing the Combined Collection Method by banks for non-credit card loan products?**

Response:

The FDIC has not changed its policy or practice related to how banks collect required customer identifying information (i.e., name, date of birth, address, and identification number) prior to account opening. The agencies have not amended the Customer Identification Program (CIP) Rule since it was adopted in May 2003 (effective June 9, 2003), by the FDIC, Office of the Comptroller of the Currency, Federal Reserve Board, National Credit Union Administration, and the Financial Crimes Enforcement Network (FinCEN).[40]

As outlined in FinCEN's regulations at 31 CFR 1020.220(a)(2)(i)(A), other than a few limited exceptions, "the bank must obtain, at a minimum, the following information *from* the customer *prior* to opening an account..."[41] Those exceptions include credit card accounts and situations in which a person is applying for a taxpayer identification number (TIN).[42]

Accordingly, for the past two decades, banks have been required to obtain identifying information *from* the customer, *prior* to account opening. Banks offering other types of accounts besides credit card accounts, including deposit accounts, transaction or asset accounts, loan accounts, or other extensions of credit, must collect required customer information *from* the customer *prior* to opening the account. The FDIC's March 2024 advisory reminded bank management of existing requirements to collect *from* the customer the customer's name, date of birth, and residential or business street address, and identification number. Particularly, (1) for a U.S. person, a tax identification number (also referred to as a social security number) is required; and, (2) for a non-U.S. person, one or more of the following is considered an identification number pursuant to the CIP Rule: (a) taxpayer identification number; (b) a passport number and country of issuance; (c) alien identification card number; or (d) number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or

[40] *See*: Financial Crimes Enforcement Network's (FinCEN) CIP regulations for banks located at 31 C.F.R. 1020.220(a)(2)(i)(A)(1-4). FinCEN, a bureau of the U.S. Department of the Treasury, is the Administrator of the Bank Secrecy Act.
[41] 31 C.F.R. 1020.220(a)(2)(i)(A)
[42] 31 C.F.R. 1020.220(a)(2)(i)(B) and (C).

similar safeguard. Failure to collect the complete identification number or any other required customer information does not comply with the CIP Rule. The Advisory also encouraged banks to review and comment on FinCEN's CIP Request for Information, which also reminded institutions of the existing requirements. The comment period ended on May 28, 2024.

b. If the FDIC thinks that the Combined Collection Method is impermissible under the current law, why has it explicitly and openly allowed this collection for so many years?

Response:

The FDIC is does not have any regulation or guidance on a "Combined Collection Method." The only exception in the CIP Rule is for credit card accounts.[43]

If financial institutions work with third parties in an agent capacity to collect required customer information,[44] those third parties (acting as the financial institution's agent) must collect the complete TIN (and all other customer identifying information) *from* the customer *prior* to account opening. It would be impermissible for third parties (acting as agent) to use another third-party source (i.e., credit bureau database) to obtain required customer identifying information when opening an account on behalf of the bank. The bank is ultimately responsible for its agent's compliance with the CIP Rule; therefore, the third party, acting in the capacity as an agent on behalf of the bank, needs to comply with the same rules and requirements as if the bank itself was collecting the information.

c. Has this deviation from historic practice, which the industry has relied upon for many years, been ratified by the FDIC Board? If not, who at the FDIC has directed this change?

Response:

As indicated in the responses above, there has been neither a change to the CIP Rule, nor a change in FDIC policy related to CIP or the collection of required customer identifying information. Since June 2003, banks have been obligated to collect required customer identifying information *from* its customers *prior* to opening an account.

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[43] The CIP Rule credit card account exception allows financial institutions to obtain identifying information about the customer required under 31 CFR 1020.220(a)(2)(i)(A) from a third-party source prior to extending credit. That exception applies only to credit card accounts.

[44] Such third-party arrangements are contemplated in "Interagency Interpretive Guidance on Customer Identification Program Requirements under Section 326 of the USA PATRIOT Act," Customer Notice FAQ #2 published by FinCEN, Federal Reserve, FDIC, NCUA, OCC, OTS, Treasury (April 28, 2005).

Questions for the Record from Representative John Rose for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
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Representative John Rose:

1. **Chairman Gruenberg, do you believe the FDIC Chair is subject to impeachment by Congress under the Constitution's Article II?**

2. **Chairman Gruenberg, if you believe your office is immune from impeachment, please provide a detailed legal memo from the FDIC's Office of the General Counsel outlining the specific reasons for this immunity.**

3. **Chairman Gruenberg, if the House of Representatives were to impeach you and the Senate convict, would you accept the judgment of Congress and vacate the position of FDIC Chair?**

Response:

Questions regarding the interpretation of Article II, Section 4 of the U.S. Constitution (the Impeachment Clause) and the legal applicability of the law to the head of a Federal agency may more appropriately be directed to the Department of Justice Office of Legal Counsel.

4. **Chairman Gruenberg, on a scale of 1 to 100, with 1 being very low and 100 being very high, how would you rate the overall morale of FDIC employees?**

Response:

The Office of Personnel Management conducts an annual Federal Employee Viewpoint Survey (OPM FEVS) to survey and assesses how employees jointly experience the policies, practices, and procedures characteristic of their agency and its leadership. Results from the OPM FEVS offers insights into whether, and to what extent, workplace conditions characterizing successful organizations are present in Federal agencies, information important to successful organizational change and development initiatives. The FDIC participates in the annual FEVS, which is available at FEVS - OPM.gov.

The FDIC has also implemented a number of strategies to strengthen its workplace culture and enable employees to elevate concerns to the most senior levels of leadership. This includes the Workplace Excellence (WE) Program[45], the FDIC Labor Management Forum (LMF)[46], the

[45] The WE Program provides a forum where diverse employees across various organizations, share their perspectives on the FDIC work environment and collaborate on workplace improvements. In previous years, the successful launch of this program led to 10 Division/Office WE Councils and actively engaged 75% of all FDIC employees through WE employee engagement activities and accomplished over 80 WE Steering Committee and Council Projects and initiatives.

[46] The LMF is a mechanism to provide NTEU with pre-decisional input on workplace matters to the fullest extent practicable, without regard to whether those matters are negotiable subjects of bargaining. Together with the Workplace Excellence Program, the LMF strives to enhance communications, employee input and morale throughout FDIC.

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FDIC Employee Resource Group (ERG)[47] Program, as well as the Chairman's Diversity Advisory Council (CDAC).[48] More recently, the FDIC has implemented a comprehensive agency-wide Plan for cultural transformation, which includes initiatives aimed at strengthening employee satisfaction.[49] The plan was prepared at my request by FDIC senior leadership and staff. The Plan reflects comments and suggestions received during listening sessions held with FDIC employees in November. The Plan also reflects input from a range of FDIC stakeholders, including the Diversity and Inclusion Executive Advisory Council, personnel in the Office of Minority and Women Inclusion, and the employee resource groups.

5. **Chairman Gruenberg, with the increased prevalence of remote work, the Committee is concerned about potential incidents of accidental disclosure or misuse of confidential FDIC data by employees. Please discuss with your team and provide a written response for the record on the following:**

    a. **Have there been any documented incidents of accidental disclosure or misuse of confidential FDIC data by employees working remotely in the past five years?**

    b. **If so, please provide details regarding the nature of the incidents, including:**

        i. **Date range of the incidents.**

        ii. **Type of data involved (e.g., customer information, financial data).**

        iii. **Actions taken by the FDIC to address the incidents and prevent future occurrences.**

Response:
The FDIC documents and reports information security incidents, including incidents of accidental disclosure or misuse of confidential FDIC data, in accordance with government-wide standards,[50] which do not categorize incidents based on whether they were caused by employees working remotely.

The FDIC provides information on how the agency maintains and strengthens its own

[47] ERGs are FDIC-recognized networks of employees with common goals, interests, or experiences which are established to foster and encourage equality of opportunity, respect, and fair treatment for all.
[48] The mission of the Chairman's Diversity Advisory Councils (CDACs) is to provide advice to the FDIC Chairman, through the Office of Minority and Women Inclusion (OMWI) Director, on diversity and inclusion (D&I) issues and concerns.
[49] See FDIC Action Plan for a Safe, Fair, and Inclusive Work Environment, available at https://www.fdic.gov/action-plan.
[50] CISA, *Federal Incident Notification Guidelines*, April 1, 2017, https://www.cisa.gov/federal-incident-notification-guidelines.

cybersecurity as well as efforts to strengthen cybersecurity in the financial services sector as part of its annual Report on Cybersecurity and Resilience.[51] This includes statistical information on all security incidents involving FDIC information reported to the FDIC's Security Response Team (SRT) and incidents reported to the United States Computer Emergency Readiness Team (US-CERT) following the US-CERT Federal Incident Notification Guidelines.

The FDIC maintains a wide breadth of data including, among other types, data pertaining to bank supervision, receivership, legal, research, human resources, acquisition, and information technology. These types of data are involved in the incidents noted in the annual Report on Cybersecurity and Resilience, although none of the events reported in the most recent report met the criteria for classification as a "Major incident" and of the incidents reported to US-CERT received a CISA National Cyber Incident Scoring System (NCISS) priority score of either Baseline – Negligible or Baseline – Minor.

Like other federal agencies, the FDIC regularly updates process, technology, and employee awareness to prevent security incidents and respond effectively when incidents occur. In recent years, the FDIC has implemented an enhanced incident management system, expanded effective breach response procedures, implemented policy and technology solutions to appropriately label FDIC documents in electronic form, updated mandatory information security and privacy training for all FDIC employees, and provided a variety of awareness events and communications to FDIC employees.

6. **Chairman Gruenberg, it has come to my attention that the frontline supervisory staff of the FDIC have been overruled and instructed by FDIC staff based in Washington DC to change longstanding and well-established practice of the agency regarding the collection of social security numbers from customers in connection with a Customer Identification Program (CIP). Historically, the FDIC permitted banks, as part of their CIP policies and procedures, to use the Combined Collection Method to collect SSNs from customers for non-credit card lending products - allowing banks to collect customer SSNs by obtaining the last four digits directly from customers, and then using the partial SSNs and other identifying information collected from customers to obtain the full SSNs from reliable third-party vendors.**

   However, the FDIC recently released a letter emphasizing that the entire SSN must be collected directly from the customer, which could introduce security and other concerns, at the same time as a release from FinCEN requesting comment on this requirement.

[51] See 2024 Report on Cybersecurity and Resilience, available at https://www.fdic.gov/system/files/2024-08/2024-cybersecurity-financial-system-resilience-report.pdf.

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a. What is the rationale for this abrupt change?

Response:

The FDIC has not changed its policy or practice related to how banks collect required customer identifying information (i.e., name, date of birth, address, and identification number) prior to account opening. The regulatory requirements implemented by the Customer Identification Program (CIP) have not changed since the CIP Rule was adopted in May 2003 and became effective on June 9, 2003.[52]

As outlined in FinCEN's regulations at 31 CFR 1020.220(a)(2)(i)(A), other than a few limited exceptions, "the bank must obtain, at a minimum, the following information *from* the customer *prior* to opening an account..."[53] Those exceptions include credit card accounts and situations in which a person is applying for a taxpayer identification number (TIN).[54]

Accordingly, for the past two decades, banks have been required to obtain identifying information *from* the customer, *prior* to account opening. Banks offering other types of accounts besides credit card accounts, including deposit accounts, transaction or asset accounts, loan accounts, or other extensions of credit, must collect required customer information *from* the customer *prior* to opening the account.

The FDIC's March 2024 advisory reminded bank management that it must collect *from* the customer the customer's name, date of birth, and residential or business street address, and identification number. Particularly, (1) for a U.S. person, a tax identification number (also referred to as a social security number) is required; and, (2) for a non-U.S. person, one or more of the following is considered an identification number pursuant to the CIP Rule: (a) taxpayer identification number; (b) a passport number and country of issuance; (c) alien identification card number; or (d) number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard. Failure to collect the complete identification number or any other required customer information does not comply with the CIP Rule. The Advisory also encouraged banks to review and comment on FinCEN's CIP Request for Information, which also reminds institutions of the existing requirements.

b. As you know the FinCen is actively seeking comments on the Combined Collection Method, signaling that FinCen may soon codify the Combined Collection Method. Shouldn't FDIC, at a minimum, pause this abrupt and

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[52] *See*: Financial Crimes Enforcement Network's (FinCEN) CIP regulations for banks located at 31 C.F.R. 1020.220(a)(2)(i)(A)(1-4). FinCEN, a bureau of the U.S. Department of the Treasury, is the Administrator of the Bank Secrecy Act.
[53] 31 C.F.R. 1020.220(a)(2)(i)(A)
[54] 31 C.F.R. 1020.220(a)(2)(i)(B) and (C).

unjustified change until FinCen's transparent rulemaking is complete?

Response:

The FDIC supervises banks under existing laws and regulations. The FDIC has not changed its policy or practice related to how banks collect required customer identifying information (i.e., name, date of birth, address, and identification number) prior to account opening since the CIP Rule was adopted in 2003.

c. Why is the FDIC in Washington DC pushing this change when there appears to be no risk, policy or supervisory rationales to justify this change?

Response:

As indicated in the responses above, there has been neither a change to the CIP Rule, nor a change in FDIC policy related to CIP or the collection of required customer identifying information. Since June 2003, banks have been required by the CIP Rule to collect required customer identifying information *from* its customers *prior* to opening an account.

d. Given the major consumer privacy concerns related to full SSN collection, why would you move forward without public comment or at a minimum some guidance? (Maxine Waters raised this issue in a letter attached).

Response:

There have been no changes the CIP Rule or FDIC policy. The FDIC's March 28, 2024, Advisory was issued to remind FDIC-supervised banks of the CIP requirements to collect identifying information. The Advisory also encouraged banks to review and comment on FinCEN's CIP RFI.

7. Chair Gruenberg, what are your plans regarding artificial intelligence?

Response:

With regard to the FDIC's supervisory responsibilities, the FDIC is neutral as to specific technologies used by the industry. The agency focuses on the outcomes produced by the technology, policies, procedures, and systems implemented by financial institutions to conduct its operations and deliver products and services. Regardless of the tools used by financial institutions, it is the responsibility of an institution's board and management to ensure that the institution is operating in a safe and sound manner, and in compliance with all applicable laws and regulations;[55] this includes the institution's use of any technology, including AI.

[55] See 12 CFR 364.

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As part of its supervisory program, the FDIC uses a risk-focused examination approach to evaluate a bank's safety and soundness and consumer compliance. The examination approach focuses examiner resources on assessing management's ability to identify and control risks. For AI, this often includes assessing a bank's model risk management function. An institution's model risk management practices are expected to be commensurate with the institution's risk exposure, as well as the complexity and extent of its model use. The FDIC has hired relevant expertise to assist the FDIC in these supervisory processes. The FDIC has also issued guidance to the industry by adopting Supervisory Guidance on Model Risk Management[56] and issuing the Interagency Statement on Model Risk Management for Bank Systems Supporting Bank Secrecy Act/Anti-Money Laundering Compliance.[57]

[56] See FDIC Financial Institution Letter (FIL)-22-2017, Adoption of Supervisory Guidance on Model Risk Management, June 7, 2017, https://www.fdic.gov/news/financial-institution-letters/2017/fil17022.html
[57] See FDIC FIL-27-2021, Bank Secrecy Act: Agencies Address Model Risk Management for Bank Models and Systems Supporting Bank Secrecy Act/Anti-Money Laundering and Office of Foreign Assets Control Compliance, April 2021 https://www.fdic.gov/news/financial-institution-letters/2021/fil21027.html

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1. **Has the FDIC specifically targeted institutions that partner with fintech companies for more rigorous examinations and or enforcement, resulting in a disproportionate share of regulatory actions compared to traditional depository institutions during the same timeframe?**

Response:

No. All examinations are based on the concept of risk-focused supervision, where the scope of review reflects the risk to the institution and consumers harm. The examination scope will depend on the nature and complexity of the institution's business activities, the institution's risk profile, and areas highest consumer harm risk, not whether a product offered is a traditional banking product or one involving a partnership with a financial technology firm.

2. **And what additional training have you provided to those examiners so that they are equipped to evaluate this type of relationship in a risk-based manner?**

Response:

The FDIC is committed, and takes several measures, to ensure staff across the FDIC have the appropriate skillsets to perform their duties. This includes, but is not limited to, skillsets related to emerging technology. These measures include workforce planning, the hiring process, training initiatives, and performance management processes, among others. The FDIC has established, and continues to develop, dedicated resources in several divisions to ensure appropriate skills are in place. The FDIC's approach to ensuring that appropriate skills are in place takes into consideration the FDIC's ongoing monitoring of industry trends.

For example, during 2023, the Division of Risk Management Supervision (RMS) established a new Emerging Technology Section and Division of Depositor and Consumer Protection (DCP) established a new Technology Enterprise and Consumer Harm Risk and Innovation (TECH) Section. These new sections are bringing increased focus to policy development, training, examination support, and interagency collaboration on emerging technology topics related to insured financial institutions. In 2020, the Office of the General Counsel formed the Emerging Technology & Anti-Money Laundering (AML)/Cyber Fraud Policy Group. The Emerging Technology & AML/Cyber Fraud Policy Group houses a team of attorneys that, along with other groups focused on supervisory risk and consumer issues within the Legal Division, supports these new sections and focuses on legal issues facing both the FDIC and its supervised and insured banks and savings associations arising from emerging forms of technology. Collectively, these activities help to inform the FDIC's supervisory strategy and regulatory policymaking for responding to opportunities and risks presented using emerging technologies at supervised financial institutions. Prior to that, in 2016, the FDIC established the Emerging Technology Steering Committee to, among other things, monitor and assess technology activities, risks, and trends and evaluate their potential impact on the banking system, deposit insurance system,

effective regulatory oversight, economic inclusion, and consumer protection. The Committee is comprised of the Directors of the FDIC's Division of Risk Management Supervision, Division of Depositor and Consumer Protection, other FDIC Divisions, as well as the General Counsel, the Chief Risk Officer, and the Chief Information Officer.

In September 2023, Government Accountability Office (GAO) issued a report titled, *Financial Technology: Agencies Can Better Support Workforce Expertise and Measure the Performance of Innovation Offices* (Report) (GAO-23-106168). The Report examines the regulators' financial technology expertise. While the Report recognizes and reflects that the FDIC has incorporated leading workforce planning practices, the Report included a recommendation that the FDIC fully incorporate leading workforce planning practices for the primary offices involved in policymaking and oversight related to financial technology.[58] The Report included a similar recommendation to other agencies. In response to the Report, the FDIC has committed to considering additional workforce planning practices identified in the Report's recommendation

3. **In 2023, the FDIC's OIG issued a report titled "FDIC Strategies Related to Crypto-Asset Risks." In that Report, there were several recommendations for corrective action that the FDIC was expected to complete by January 30, 2024. Can you describe the progress (if any) made to date, and when financial institutions will receive details on the outcome of those recommendations?**

Response:

The report made two recommendations related to the FDIC's process for assessing risks pertaining to crypto-related activities and providing feedback to FDIC-supervised institutions on crypto-related activities. The FDIC concurred with both recommendations, has implemented one recommendation, and continues to make progress to address the remaining recommendation in the OIG Report. Because the recommendations related to internal FDIC processes, however, outcomes of the recommendations will not be communicated to financial institutions, but the OIG Semiannual Report to Congress reflects whether OIG recommendations to the FDIC remain outstanding.

4. **Separately, in public remarks before the Mercatus Center on March 11, 2024, Vice Chair Travis Hill described a public perception that the FDIC is "closed for business if institutions are interested in anything related to blockchain or distributed ledger technology." By extension, he also stressed the importance of allowing**

[58] The Report (page 44) recommends that "The Chair of the Federal Deposit Insurance Corporation should fully incorporate leading workforce planning practices for the primary offices involved in policymaking and oversight related to financial technology by collecting staff skillset data and determining the critical financial technology skills the agency needs; developing targeted strategies to address financial technology-related skills gaps; and measuring the effectiveness of its financial technology related training in addressing skill needs." https://www.gao.gov/products/gao-23-106168

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experimentation and testing. What is the FDIC doing about this perception and developing a path forward, especially where, in October 2023, the Federal Reserve Board introduced a Novel Supervisory Activities Program to allow financial institutions to explore not only the use of DLT, but also technology-driven partnerships with non-banks.

Response:

The FDIC neither promotes nor discourages supervised institutions from pursuing any particular business line, service, or delivery channel; doing business with any particular type or class of customer; using any particular technology; or partnering with third parties, provided institutions operate in a safe and sound manner and in compliance with all applicable laws and regulations.

The FDIC developed a process pursuant to which it requests that supervised banks notify the FDIC of crypto-related activities, which includes participating in blockchain- and distributed ledger-based settlement or payment systems. As part of that process, the FDIC provides feedback to supervised banks, as appropriate, which may include feedback on how supervised institutions can improve various functions to more appropriately identify and manage risks associated with crypto-asset related activities.

5. **Have your agencies taken responsibility for assessing the Basel proposal's impact on the municipal bond market? What type of interaction has your agency had with the SEC or the MSRB on the topic of municipal bonds? Furthermore, how does the government plan to address the identified risks, particularly the projected increase in the cost of capital for holding municipal bonds and its potential adverse effects on borrowing costs for municipalities nationwide?**

Response:

The Federal banking agencies have received over 400 unique comment letters relating to the Basel III Endgame proposal and have also met with interested parties over 50 times. The FDIC greatly values all feedback received on the proposal and is carefully considering all comments received including those comments concerning borrowing costs for municipalities.

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1. **As of late, we've witnessed the FDIC hold a hostile aggression towards banks who partner with fintechs. Under your leadership, the FDIC has created an overly adversarial regulatory environment that is using enforcement action that will impact the development of innovative products and services that benefit consumers and businesses. Has the FDIC performed any independent study (formal or informal) on the impact of formal enforcement actions on bank deposit decline?**

Response:

The FDIC has identified a number of factors that can influence deposits either increasing or decreasing in the banking sector. Most recently these factors have included higher inflation, changes in interest rates, Federal Reserve monetary policy actions, and volatility resulting from the failures of several large banks in March 2023.

After a period of extraordinary deposit growth as a result of actions taken by monetary and fiscal authorities, and by individuals, businesses, and financial market participants in response to the COVID-19 pandemic, higher than target inflation measures, peaking at 9.1 percent, spurred the Fed to increase interest rates dramatically starting in the first quarter of 2022. The Fed hiked rates a total of 11 times between March 2022 and July 2023, increasing them from at or near zero to between 5.25 and 5.50 percent, where they currently remain.

Banks were slow to raise interest rates on deposits and over the course of 2022 there was significant outflow to higher yielding alternatives such as money market funds. Domestic deposits decreased for six straight quarters with the biggest decline occurring in the first quarter of 2023 as uninsured depositors sought safety in the wake of two large bank failures.

As of March 31, 2024, domestic deposits increased by $191 billion, the second consecutive quarter increase, driven by growth in transaction accounts. The shift away from noninterest-bearing deposits toward interest-bearing deposits continued, as interest-bearing deposits increased 1.7 percent quarter over quarter and noninterest-bearing deposits declined for the eighth consecutive quarter.

Estimated uninsured deposits increased $63 billion in the first quarter of 2024, representing the first reported increase since fourth quarter 2021, and indicating some stabilization. In briefings for the FDIC's Quarterly Banking Profile, it was noted that the increase was led by global systemically important banks (G-SIBs), mainly in their custodial operations as they competed for business.

Estimated insured deposits increased by 1.1 percent, below the typical expected growth rate for a first quarter. This is likely due to the ongoing effects of inflation and higher consumer spending. In April 2024, the personal saving rate – personal saving as a percentage of disposable personal income - measured 3.6 percent, about 2 percent lower than the same period in 2023, and lower

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than pre-pandemic levels.

Changes to the Federal Reserve's balance sheet contribute to aggregate, system wide fluctuations in deposits. Growth in the Federal Reserve's balance sheet tends to cause bank deposits to expand, while a decline in their balance sheet may cause bank deposits to fall. This results from changing the supply of treasuries available for purchase by the private sector—as the private sector buys more treasuries, during quantitative tightening periods, they pull deposits from the banking sector. The Federal Reserve is currently undergoing quantitative tightening. Total assets at the Federal Reserve peaked at nearly $9 trillion in April 2022 and have since declined to $7.3 trillion.

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1. **Pivoting to FDIC policy— Chairman Gruenberg, I'm concerned about the FDICs increasingly hostile posture toward bank-fintech partnerships. In the past four years, how many financial institutions were issued any type of enforcement action for third-party risk related to their partnerships with a FinTech company?**

Response:

The FDIC neither promotes nor discourages supervised institutions from pursuing any particular business line, service, or delivery channel; doing business with any particular type or class of customer; using any particular technology; or partnering with third parties, provided institutions operate in a safe and sound manner and in compliance with all applicable laws and regulations.

During the last four years (January 2020 – May 2024), enforcement actions issued to 25 FDIC-supervised banks included issues involving third-party risk and fintech relationships.

2. **In a previous hearing focused on bank mergers, I briefly asked about bank-fintech partnerships and the FDIC's view of innovation in Financial Services. Your staff held that the FDIC engages with industry participants but does not have a dedicated office for financial innovation. Would you please describe specifically how the FDIC engages with banks that partner with FinTechs, aside from enforcement actions?**

Response:

FDIC staff engages regularly with supervised institutions, including those that partner with fintechs, which can occur through a range of supervisory processes, such as examinations or regular communications between bank management and the FDIC's local field office or regional office staff. In addition, the FDIC routinely engages with industry stakeholders through a number of channels to better understand the potential benefits and risks of financial technology. For example, the FDIC issues periodic Requests for Information regarding insured financial institutions' current and potential activities involving modern technologies, such as digital assets and artificial intelligence; publishes proposed policy statements and industry guidance for public comment, including the Interagency Guidance on Third-Party Relationships: Risk Management, (issued for public comment in July 2021 and finalized in June 2023);[59] and coordinates with other Federal and state regulatory agencies on financial technology issues. The FDIC has also

[59] *See* 86 Fed. Reg. 38182 (July 19, 2021): Proposed Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2021/07/19/2021-15308/proposed-interagency-guidance-on-third-party-relationships-risk-management; *see also* 88 Fed. Reg. 37920 (June 9, 2023): Interagency Guidance on Third-Party Relationships: Risk Management. https://www.federalregister.gov/documents/2023/06/09/2023-12340/interagency-guidance-on-third-party-relationships-risk-management.

sponsored financial technology-related conferences and periodically participated jointly with other federal agencies in panel discussions, presentations, and meetings with industry representatives.

3. Do you provide clear guidelines for banks that would like to partner with FinTechs?

a. If yes, did you work with banks and FinTechs to develop those guidelines, absent a Congressional framework?

Response:

Yes. While banks are ultimately responsible for managing activities conducted through third-party relationships and identifying and controlling the risks arising from such relationships to the same extent as if the activity were handled within the institution, the FDIC has provided several resources to assist banks and FinTech entities understand, evaluate, and mitigate risks that may result from such arrangements.

To help banking organizations manage risks associated with third-party relationships, on June 6, 2023, after issuance of a proposal and careful consideration of comments received, the federal banking agencies (FDIC, FRB, and OCC) issued final joint *Interagency Guidance on Third-Party Relationships: Risk Management* on managing risks associated with third-party relationships, including financial technology companies.

The final guidance provides sound principles that support a risk-based approach to third-party risk management that banking organizations may consider when developing and implementing risk management practices for all stages in the life cycle of third-party relationships. The guidance also states that sound third-party risk management considers the level of risk, complexity, and size of the banking organization and the nature of the third-party relationship.

Further, the agencies issued *Third-Party Risk Management - A Guide for Community Banks* on May 3, 2024, as a resource to help community banks in developing and implementing their third-party risk management programs, policies, and practices.

In December 2023, the FDIC finalized amendments to Part 328 of its regulations (*FDIC Official Signs and Advertising Requirements, False Advertising, Misrepresentations of Insured Status, and Misuse of the FDIC's Name or Logo*) to modernize the rules governing use of the official FDIC sign and insured depository institutions' (IDIs') advertising statements to reflect how depositors do business with IDIs today. The FDIC noted that consumers are increasingly relying on internet and mobile banking channels to access IDI banking services, bank branches are continually evolving to serve depositors, and FinTech companies are offering consumers new options and alternatives for accessing banking products and services. The final rule also clarifies the FDIC's regulations regarding misrepresentations of deposit insurance coverage, which apply to any person, including IDIs and non–bank entities, which can include FinTech companies.

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The FDIC released additional publications and guidance that provide information and resources relevant to financial institutions considering or already engaging in business arrangements with third parties, including financial technology companies. Some publications on the topic of bank and third-party relationships include the following:

- *Conducting Due Diligence on Financial Technology Companies: A Guide for Community Banks*, that was published in August 2021 by the FDIC, the Federal Reserve, and the OCC.
- *FDIC's Conducting Business with Banks: A Guide for Third Parties*, which was published by the FDIC in February 2020.
- *FDIC DCP Consumer Compliance Supervisory Highlights,* issued in April 2020, March 2021, March 2023, and March 2024, which identify notable concerns related to bank and third-party relationships.
- *Advisory to FDIC-Insured Institutions Regarding Deposit Insurance and Dealings with Crypto Companies,* issued by the FDIC in July of 2022, which reminds IDIs of the risks that could arise related to misrepresentations of deposit insurance by crypto–asset companies.

1. **Mr. Gruenberg, there were 92 sexual harassment complaints that made it to a formal review process between 2015 and 2023 and "not a single one resulted in removal, reductions in grade or pay, or any discipline more serious than a suspension." How many of those incidents were you made aware of?**

Response:

It should be noted that the 92 complaints identified in the FDIC's No FEAR Act Annual Reports to Congress for fiscal years 2015-2023, includes all forms of harassment, not just sexual harassment. Additionally, outcome of these complaints does not account for instances where individuals were separated from the agency by retiring or resigning to avoid facing more serious disciplinary action.

While the agency Chair is made aware information contained in the agency's No FEAR Act Annual Report, it is not the agency's prevailing practice to inform members of the Board of Directors of the specific facts or circumstances of individual disciplinary matters or of individual EEO claims. There have been numerous initiatives, however, intended to shed light on the workplace experience and elevate employees' general concerns to the most senior levels of leadership. This has been reflected in the establishment of the Workplace Excellence (WE)

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Program[60], the FDIC Labor Management Forum (LMF)[61], the FDIC Employee Resource Group (ERG)[62] Program, as well as the Chairman's Diversity Advisory Council (CDAC).[63]

[60] The WE Program provides a forum where diverse employees across various organizations, share their perspectives on the FDIC work environment and collaborate on workplace improvements. In previous years, the successful launch of this program led to 10 Division/Office WE Councils and actively engaged 75% of all FDIC employees through WE employee engagement activities and accomplished over 80 WE Steering Committee and Council Projects and initiatives.

[61] The LMF is a mechanism to provide NTEU with pre-decisional input on workplace matters to the fullest extent practicable, without regard to whether those matters are negotiable subjects of bargaining. Together with the Workplace Excellence Program, the LMF strives to enhance communications, employee input and morale throughout FDIC.

[62] ERGs are FDIC-recognized networks of employees with common goals, interests, or experiences which are established to foster and encourage equality of opportunity, respect, and fair treatment for all.

[63] The mission of the Chairman's Diversity Advisory Councils (CDACs) is to provide advice to the FDIC Chairman, through the Office of Minority and Women Inclusion (OMWI) Director, on diversity and inclusion (D&I) issues and concerns.

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Representative John Rose:

1. **Chairman Gruenberg, do you believe the FDIC Chair is subject to impeachment by Congress under the Constitution's Article II?**

2. **Chairman Gruenberg, if you believe your office is immune from impeachment, please provide a detailed legal memo from the FDIC's Office of the General Counsel outlining the specific reasons for this immunity.**

3. **Chairman Gruenberg, if the House of Representatives were to impeach you and the Senate convict, would you accept the judgment of Congress and vacate the position of FDIC Chair?**

Response:

Questions regarding the interpretation of Article II, Section 4 of the U.S. Constitution (the Impeachment Clause) and the legal applicability of the law to the head of a Federal agency may more appropriately be directed to the Department of Justice Office of Legal Counsel.

4. **Chairman Gruenberg, on a scale of 1 to 100, with 1 being very low and 100 being very high, how would you rate the overall morale of FDIC employees?**

Response:

The Office of Personnel Management conducts an annual Federal Employee Viewpoint Survey (OPM FEVS) to survey and assesses how employees jointly experience the policies, practices, and procedures characteristic of their agency and its leadership. Results from the OPM FEVS offers insights into whether, and to what extent, workplace conditions characterizing successful organizations are present in Federal agencies, information important to successful organizational change and development initiatives. The FDIC participates in the annual FEVS, which is available at FEVS - OPM.gov.

The FDIC has also implemented a number of strategies to strengthen its workplace culture and enable employees to elevate concerns to the most senior levels of leadership. This includes the Workplace Excellence (WE) Program[45], the FDIC Labor Management Forum (LMF)[46], the

[45] The WE Program provides a forum where diverse employees across various organizations, share their perspectives on the FDIC work environment and collaborate on workplace improvements. In previous years, the successful launch of this program led to 10 Division/Office WE Councils and actively engaged 75% of all FDIC employees through WE employee engagement activities and accomplished over 80 WE Steering Committee and Council Projects and initiatives.

[46] The LMF is a mechanism to provide NTEU with pre-decisional input on workplace matters to the fullest extent practicable, without regard to whether those matters are negotiable subjects of bargaining. Together with the Workplace Excellence Program, the LMF strives to enhance communications, employee input and morale throughout FDIC.

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FDIC Employee Resource Group (ERG)[47] Program, as well as the Chairman's Diversity Advisory Council (CDAC).[48] More recently, the FDIC has implemented a comprehensive agency-wide Plan for cultural transformation, which includes initiatives aimed at strengthening employee satisfaction.[49] The plan was prepared at my request by FDIC senior leadership and staff. The Plan reflects comments and suggestions received during listening sessions held with FDIC employees in November. The Plan also reflects input from a range of FDIC stakeholders, including the Diversity and Inclusion Executive Advisory Council, personnel in the Office of Minority and Women Inclusion, and the employee resource groups.

5. **Chairman Gruenberg, with the increased prevalence of remote work, the Committee is concerned about potential incidents of accidental disclosure or misuse of confidential FDIC data by employees. Please discuss with your team and provide a written response for the record on the following:**

    a. **Have there been any documented incidents of accidental disclosure or misuse of confidential FDIC data by employees working remotely in the past five years?**

    b. **If so, please provide details regarding the nature of the incidents, including:**

        i. **Date range of the incidents.**

        ii. **Type of data involved (e.g., customer information, financial data).**

        iii. **Actions taken by the FDIC to address the incidents and prevent future occurrences.**

Response:
The FDIC documents and reports information security incidents, including incidents of accidental disclosure or misuse of confidential FDIC data, in accordance with government-wide standards,[50] which do not categorize incidents based on whether they were caused by employees working remotely.

The FDIC provides information on how the agency maintains and strengthens its own

[47] ERGs are FDIC-recognized networks of employees with common goals, interests, or experiences which are established to foster and encourage equality of opportunity, respect, and fair treatment for all.
[48] The mission of the Chairman's Diversity Advisory Councils (CDACs) is to provide advice to the FDIC Chairman, through the Office of Minority and Women Inclusion (OMWI) Director, on diversity and inclusion (D&I) issues and concerns.
[49] See FDIC Action Plan for a Safe, Fair, and Inclusive Work Environment, available at https://www.fdic.gov/action-plan.
[50] CISA, *Federal Incident Notification Guidelines*, April 1, 2017, https://www.cisa.gov/federal-incident-notification-guidelines.

cybersecurity as well as efforts to strengthen cybersecurity in the financial services sector as part of its annual Report on Cybersecurity and Resilience.[51] This includes statistical information on all security incidents involving FDIC information reported to the FDIC's Security Response Team (SRT) and incidents reported to the United States Computer Emergency Readiness Team (US-CERT) following the US-CERT Federal Incident Notification Guidelines.

The FDIC maintains a wide breadth of data including, among other types, data pertaining to bank supervision, receivership, legal, research, human resources, acquisition, and information technology. These types of data are involved in the incidents noted in the annual Report on Cybersecurity and Resilience, although none of the events reported in the most recent report met the criteria for classification as a "Major incident" and of the incidents reported to US-CERT received a CISA National Cyber Incident Scoring System (NCISS) priority score of either Baseline – Negligible or Baseline – Minor.

Like other federal agencies, the FDIC regularly updates process, technology, and employee awareness to prevent security incidents and respond effectively when incidents occur. In recent years, the FDIC has implemented an enhanced incident management system, expanded effective breach response procedures, implemented policy and technology solutions to appropriately label FDIC documents in electronic form, updated mandatory information security and privacy training for all FDIC employees, and provided a variety of awareness events and communications to FDIC employees.

6. **Chairman Gruenberg, it has come to my attention that the frontline supervisory staff of the FDIC have been overruled and instructed by FDIC staff based in Washington DC to change longstanding and well-established practice of the agency regarding the collection of social security numbers from customers in connection with a Customer Identification Program (CIP). Historically, the FDIC permitted banks, as part of their CIP policies and procedures, to use the Combined Collection Method to collect SSNs from customers for non-credit card lending products - allowing banks to collect customer SSNs by obtaining the last four digits directly from customers, and then using the partial SSNs and other identifying information collected from customers to obtain the full SSNs from reliable third-party vendors.**

   However, the FDIC recently released a letter emphasizing that the entire SSN must be collected directly from the customer, which could introduce security and other concerns, at the same time as a release from FinCEN requesting comment on this requirement.

[51] See 2024 Report on Cybersecurity and Resilience, available at https://www.fdic.gov/system/files/2024-08/2024-cybersecurity-financial-system-resilience-report.pdf.

Questions for the Record from Representative John Rose for
The Honorable Martin J. Gruenberg
Chairman, Federal Deposit Insurance Corporation
May 15, 2024, Hearing entitled, "Oversight of the Prudential Regulators"
House Financial Services Committee

a. What is the rationale for this abrupt change?

Response:

The FDIC has not changed its policy or practice related to how banks collect required customer identifying information (i.e., name, date of birth, address, and identification number) prior to account opening. The regulatory requirements implemented by the Customer Identification Program (CIP) have not changed since the CIP Rule was adopted in May 2003 and became effective on June 9, 2003.[52]

As outlined in FinCEN's regulations at 31 CFR 1020.220(a)(2)(i)(A), other than a few limited exceptions, "the bank must obtain, at a minimum, the following information *from* the customer *prior* to opening an account..."[53] Those exceptions include credit card accounts and situations in which a person is applying for a taxpayer identification number (TIN).[54]

Accordingly, for the past two decades, banks have been required to obtain identifying information *from* the customer, *prior* to account opening. Banks offering other types of accounts besides credit card accounts, including deposit accounts, transaction or asset accounts, loan accounts, or other extensions of credit, must collect required customer information *from* the customer *prior* to opening the account.

The FDIC's March 2024 advisory reminded bank management that it must collect *from* the customer the customer's name, date of birth, and residential or business street address, and identification number. Particularly, (1) for a U.S. person, a tax identification number (also referred to as a social security number) is required; and, (2) for a non-U.S. person, one or more of the following is considered an identification number pursuant to the CIP Rule: (a) taxpayer identification number; (b) a passport number and country of issuance; (c) alien identification card number; or (d) number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard. Failure to collect the complete identification number or any other required customer information does not comply with the CIP Rule. The Advisory also encouraged banks to review and comment on FinCEN's CIP Request for Information, which also reminds institutions of the existing requirements.

b. As you know the FinCen is actively seeking comments on the Combined Collection Method, signaling that FinCen may soon codify the Combined Collection Method. Shouldn't FDIC, at a minimum, pause this abrupt and

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[52] *See*: Financial Crimes Enforcement Network's (FinCEN) CIP regulations for banks located at 31 C.F.R. 1020.220(a)(2)(i)(A)(1-4). FinCEN, a bureau of the U.S. Department of the Treasury, is the Administrator of the Bank Secrecy Act.
[53] 31 C.F.R. 1020.220(a)(2)(i)(A)
[54] 31 C.F.R. 1020.220(a)(2)(i)(B) and (C).

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unjustified change until FinCen's transparent rulemaking is complete?

Response:

The FDIC supervises banks under existing laws and regulations. The FDIC has not changed its policy or practice related to how banks collect required customer identifying information (i.e., name, date of birth, address, and identification number) prior to account opening since the CIP Rule was adopted in 2003.

c. Why is the FDIC in Washington DC pushing this change when there appears to be no risk, policy or supervisory rationales to justify this change?

Response:

As indicated in the responses above, there has been neither a change to the CIP Rule, nor a change in FDIC policy related to CIP or the collection of required customer identifying information. Since June 2003, banks have been required by the CIP Rule to collect required customer identifying information *from* its customers *prior* to opening an account.

d. Given the major consumer privacy concerns related to full SSN collection, why would you move forward without public comment or at a minimum some guidance? (Maxine Waters raised this issue in a letter attached).

Response:

There have been no changes the CIP Rule or FDIC policy. The FDIC's March 28, 2024, Advisory was issued to remind FDIC-supervised banks of the CIP requirements to collect identifying information. The Advisory also encouraged banks to review and comment on FinCEN's CIP RFI.

7. Chair Gruenberg, what are your plans regarding artificial intelligence?

Response:

With regard to the FDIC's supervisory responsibilities, the FDIC is neutral as to specific technologies used by the industry. The agency focuses on the outcomes produced by the technology, policies, procedures, and systems implemented by financial institutions to conduct its operations and deliver products and services. Regardless of the tools used by financial institutions, it is the responsibility of an institution's board and management to ensure that the institution is operating in a safe and sound manner, and in compliance with all applicable laws and regulations;[55] this includes the institution's use of any technology, including AI.

[55] See 12 CFR 364.

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As part of its supervisory program, the FDIC uses a risk-focused examination approach to evaluate a bank's safety and soundness and consumer compliance. The examination approach focuses examiner resources on assessing management's ability to identify and control risks. For AI, this often includes assessing a bank's model risk management function. An institution's model risk management practices are expected to be commensurate with the institution's risk exposure, as well as the complexity and extent of its model use. The FDIC has hired relevant expertise to assist the FDIC in these supervisory processes. The FDIC has also issued guidance to the industry by adopting Supervisory Guidance on Model Risk Management[56] and issuing the Interagency Statement on Model Risk Management for Bank Systems Supporting Bank Secrecy Act/Anti-Money Laundering Compliance.[57]

[56] See FDIC Financial Institution Letter (FIL)-22-2017, Adoption of Supervisory Guidance on Model Risk Management, June 7, 2017, https://www.fdic.gov/news/financial-institution-letters/2017/fil17022.html
[57] See FDIC FIL-27-2021, Bank Secrecy Act: Agencies Address Model Risk Management for Bank Models and Systems Supporting Bank Secrecy Act/Anti-Money Laundering and Office of Foreign Assets Control Compliance, April 2021 https://www.fdic.gov/news/financial-institution-letters/2021/fil21027.html

Office of the Comptroller of the Currency

Washington, DC 20219

July 25, 2024

The Honorable Patrick McHenry
Chairman
Committee on Financial Services
United States House of Representatives
Washington, D.C. 20515

Dear Chairman McHenry:

Please find enclosed my responses to the questions for the record submitted following the May 15, 2024, hearing entitled "Oversight of Prudential Regulators."

I hope the information provided is helpful to the Committee. If you have questions or need additional information, please contact Carrie Moore, Director, Public Affairs and Congressional Relations, at 202-649-6737.

Sincerely,

Michael J. Hsu
Acting Comptroller of the Currency

Enclosure

Answers to Questions for the Record Following a Hearing entitled "Oversight of Prudential Regulators" conducted by the House Committee on Financial Services

On May 15, 2024, the Committee on Financial Services convened a hearing at which Michael J. Hsu, Acting Comptroller of the Currency, testified on "Oversight of Prudential Regulators." After the hearing, members of the Committee submitted questions for the record. This document provides the Office of the Comptroller of the Currency's responses.

Representative Andy Barr:

1. Recently, the FDIC and OCC have proposed significant changes to their bank merger review processes.

   a. Do you have any concerns about increased divergence between the OCC's own merger review process and those of your fellow bank regulators?

      Response: The OCC coordinates on a regular basis with the other federal banking agencies about merger review processes. The OCC extended the comment period for the OCC's Notice of Proposed Rulemaking (NPR) from April 15, 2024 to June 15, 2024 to provide stakeholders with additional time to comment. The OCC looks forward to reviewing all comments to determine whether changes to its proposal are appropriate.

   b. Do you believe that greater divergence between the Federal banking agencies in their merger review processes will create greater uncertainty for banks seeking to merge?

      Response: As noted above, the OCC coordinates with the other federal banking agencies in connection with merger review processes. The OCC issued its NPR to provide greater transparency, facilitate interagency coordination, and enhance public engagement, thus providing greater certainty for applicants.

   c. Does this disincentive to merge potentially create concerns that banks that would benefit from a merger, for instance, a weaker bank being acquired by a strong bank, create potential risks to financial stability that could otherwise be avoided?

      Response: Applications that are consistent with the Bank Merger Act's statutory factors will be approved, including instances where weaker banks are being acquired by stronger banks.

2. In 2020, the Federal Reserve Board unanimously approved new rules to provide clarity on bank control. Consumer Financial Protection Director Chopra stated at a recent FDIC board meeting that these changes, "sent a clear message that the Federal Reserve would be lenient when it came to enforcing Congressional prohibitions and limitations on ownership of banks."

   a. Do you agree with FDIC Director Chopra that the Federal Reserve Board's determinations of control are too lenient and allow for manipulation?

Response: The OCC works closely with the Federal Deposit Insurance Corporation (FDIC) and the Board of Governors of the Federal Reserve System (FRB) when the Change in Bank Control Act (CBCA) applies within the OCC's jurisdiction as the appropriate federal banking agency (AFBA) for national banks and federal savings associations. The OCC takes no position on whether FRB determinations of control for institutions for which the FRB is AFBA are appropriate.

b. At the same FDIC Board meeting, FDIC Director Chopra also suggested the only reason a bank would become a member of the Federal Reserve System is to evade FDIC oversight. Can you respond to his inference that there are material differences between the federal banking agencies' ability to supervise and regulate banks?

Response: Bank supervision at the federal level is carried out by three agencies: the OCC, the FRB, and the FDIC, each with specific responsibilities that enable both independent and joint supervision of specific financial institutions. The OCC charters, regulates, and supervises all national banks, federal savings associations, and federal branches and agencies of foreign banks. The OCC's mission is to ensure that the banks we supervise operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations. All national banks are statutorily required to be members of the Federal Reserve System.

The OCC is not in a position to opine on FDIC Director Chopra's comment with respect to state-chartered banks.

In his statement accompanying his vote against issuing the proposed statement of policy on bank merger transactions for comment, FDIC Director McKernan stated, "I have not been persuaded that there is a basis in law for an expectation that the post-merger bank do 'better' on the convenience and needs factor." Would you please point to and explain the statute on which the FDIC is relying on to adopt a new expectation "that a merger between IDIs will enable the resulting IDI to BETTER meet the convenience and the needs of the community to be served than would occur absent the merger?"

Response: The FDIC is best positioned to answer specific questions regarding its proposed Statement of Policy.

3. Earlier this month, the OCC issued a joint proposed rulemaking on incentive-based compensation agreements for public comment with only the FDIC and FHFA joining. FDIC Vice Chairman Hill gave pause, saying "It is extremely odd to issue this proposal without all the relevant agencies participating. Should commenters invest time and resources to respond to this proposal, or wait until all the relevant agencies are in agreement?" Why did the OCC waste valuable time and resources to pursue a rulemaking that does not include all the agencies required to participate by law?

Response: The OCC approved issuing this proposed rule in an effort to comply with the statutory requirement in section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act

(Dodd-Frank Act) to promulgate rules or guidelines related to certain aspects of incentive-based compensation.

4. Recently the OCC, FDIC, and FHFA adopted a Notice of Proposed Rulemaking to address incentive-based compensation arrangements pursuant to section 956 of Dodd-Frank. Additionally, the NCUA plans to act on the NPR in the near future and the SEC has included it in their rulemaking agenda. Yet conspicuously missing from the joint rulemaking process is the Federal Reserve Board, who is also required to join the rulemaking in section 956. Fed Chair Powell said before this Committee in March that, "I would like to understand the problem we're solving, and then I would like to see a proposal that addresses that problem."

a. Do you agree with Fed Chair Powell that we should understand the problem first before acting on any rule on executive compensation?

   Response: Section 956 of the Dodd-Frank Act requires the agencies to address incentive-based payment arrangements that encourage inappropriate risks by covered financial institutions by providing excessive compensation or that could lead to material financial loss to the covered financial institution. The proposed rule draws on the agencies' supervisory experience, recent developments, and prior rulemaking efforts to address this issue and the other provisions of section 956. We welcome public comment on the proposed rule's approach during the comment process.

b. In your statement accompanying the NPR's approval for comment you clarified that, "this NPR has not been adopted by all six agencies, so we are not requesting publication in the Federal Register." So, is this even a formal APA-compliant notice and comment rulemaking process?

   Response: Approving the issuance of this proposed rule was the first step toward issuing a final rule in compliance with the statutory requirement. The OCC will continue to follow all applicable laws, including the Administrative Procedure Act (*see*, e.g., 5 U.S.C. § 553(c)), throughout the rulemaking process.

5. You have been in an acting capacity for nearly 4 years. Do you think it is appropriate for an acting agency head to be the deciding vote at two different agencies for a rulemaking as momentous as Basel III Endgame?

Response: As provided in the Federal Deposit Insurance Act, the Acting Comptroller of the Currency also serves on the FDIC Board.

6. In July 2023, you expressed a potential willingness for the OCC to be more open to bank mergers given the pressures banks currently face as well as expressing the potential for a combination of banks to create a safer and sounder institution that is more easily regulated and supervised. In contrast, the OCC's proposed changes to its merger review process move in a direction that suggests the OCC is less open to bank mergers by creating a process that is likely to act as a roadblock to successful mergers. Please explain the contrast between your comments

in July 2023 and the OCC's proposal released a little more than six months later in January 2024?

Response: The OCC is committed to ensuring continued competition in the federal banking system, including through bank mergers. The purpose of the OCC's NPR is to provide greater transparency into the indicators for applications likely consistent with approval and applications that raise supervisory or regulatory concerns.

7. You have said, "There should be competition amongst large banks, and simply prohibiting mergers of large banks really locks in the concentration amongst the existing megabanks, and I don't think that's the right answer."

a. Do you still agree with these comments that allowing regional banks to merge presents an opportunity to increase competition amongst the largest banks?

   Response: It is important to promote competition for banks of all sizes, including the largest banks. The OCC will consider the competitive effects of any bank merger as required under the Bank Merger Act.

b. Do you think that the OCC's proposed merger guidelines, which states that applications that gain approval will generally have the feature that the resulting institution will have total assets less than $50 billion, is consistent with this desire to allow bank mergers that would increase competition to the GSIBs?

   Response: The NPR is consistent with my prior statements. The NPR identifies features of applications that are likely to be consistent with approval, and do not otherwise raise supervisory or regulatory concerns, including where the acquiring bank has satisfactory supervisory ratings, no open enforcement actions, and no fair lending, Community Reinvestment Act (CRA), Bank Secrecy Act (BSA), or consumer compliance concerns, and the resulting institution will have total assets less than $50 billion. These applications tend to withstand scrutiny more easily and are more likely to be approved expeditiously.

   The NPR also notes that, on the other end of the spectrum, applications where the acquirer has unsatisfactory supervisory ratings, open or pending BSA enforcement actions, poor CRA ratings, or other supervisory concerns are highly unlikely to receive approval unless and until such concerns are resolved. The OCC anticipates that most mergers are likely to fall in the middle, and applications that do not raise supervisory or regulatory concerns may ultimately be consistent with approval.

Questions for the Record
8. The Basel III Endgame proposal is fundamentally flawed, and, at best, a re-proposal is necessary. The proposal will likely raise capital requirements for U.S. financial institutions by more than 20%. There are suggestions that the EU and UK are supportive of implementing the Basel III Endgame proposal at a lower calibration – closer to a 5 to 7% increase. What does proposed additional gold plating on U.S. firms mean for our international competitiveness?

Response: The bank regulatory agencies issued the proposal to better ensure the strength and resilience of the banking system. The proposed revisions would be generally consistent with the international capital standards issued by the Basel Committee on Banking Supervision (BCBS), which are developed by consensus and are not legally binding. The proposal would help promote competitive equity among large U.S. banks and their foreign peers and reduce opportunities for regulatory arbitrage across jurisdictions. Individual jurisdictions may choose to implement different standards through their own legislative and regulatory processes. The U.S. bank regulatory agencies carefully consider the specific characteristics of U.S. markets, requirements under the applicable accounting standards, practices of domestic banks, and local legal requirements and policy objectives when considering implementing the BCBS standards.

Additionally, the Federal Reserve Board undertook a supplemental data collection to further clarify the estimated effects of the capital proposal. The federal banking agencies will utilize the information from this data collection, together with input from commenters on the proposal, to inform any final rule.

9. You have stated that "[w]e need a system that enables mergers..."

a. Do you still hold this position?

Response: Yes, we need a system that enables bank mergers. The U.S. needs a diverse and dynamic U.S. banking system that serves the broader economy. The OCC is committed to ensuring continued competition in the federal banking system.

b. Concerningly, on the other hand, CFPB Director Chopra stated he was "glad that [the FDIC was] moving away from a pro-merger posture." The OCC's Acting Senior Deputy Comptroller and Chief Counsel testified in front of my Subcommittee earlier this month that "ensuring continued diversity and competition in the federal banking system is of critical importance to the Acting Comptroller and the OCC." Are you concerned about your fellow FDIC Board Member's view on mergers and how this will influence the rulemaking and the potential detriment it will have on community and midsize banks?

Response: I welcome a diversity of opinions and believe that robust stakeholder comments will lead to a merger review process that is robust, promotes financial institutions of all sizes, and ensures the convenience and needs of the communities they serve.

10. You recently argued that the Federal banking agencies should not be "creating more process and opportunities for turf battles or fragmentations." Yet less than two weeks later, the OCC joined the FDIC in re-issuing the executive compensation proposal that was first put out for

comment in 2016. The Dodd Frank Act made clear that this was supposed to be a joint rulemaking with the Fed and the SEC, yet both are conspicuously absent. Please explain how this is not leading to the very turf battles and fragmentations that you cautioned against?

Response: The OCC is committed to acting jointly to issue a rule to implement section 956 of the Dodd-Frank Act, as required by the statute. We look forward to continuing to work with our colleagues at the FDIC, National Credit Union Administration (NCUA), Federal Housing Finance Agency (FHFA), FRB, and U.S. Securities and Exchange Commission (SEC) to issue a joint rule that fulfills the mandate of section 956.

Acting Comptroller Hsu, you have said, "Several U.S. banks . . . have begun reforming their overdraft programs and making them more pro-consumer. This development holds the promise of relieving millions of deserving people from the high cost of making ends meet, while empowering them and improving their overall financial health." While I appreciate your positive outlook on bank overdraft programs, another agency, the Consumer Financial Protection Bureau, has proposed a rule that would significantly limit or eliminate consumers' access to overdraft by imposing one-size-fits-all mandates and price controls.

a) Are you concerned that this rule would limit, or even eliminate, consumer access to this emergency helping hand?

Response: The OCC, along with a number of other federal agencies, engages with the CFPB on its rulemakings as part of the consultation process required under the Dodd-Frank Wall Street Reform and Consumer Protection Act. The OCC provides its supervisory perspective as part of the consultation process.

b) Are you concerned that the overdraft rulemaking, particularly when combined with the Federal Reserve's Regulation II rulemaking, will again cause access to free checking to contract?

Response: The OCC is monitoring this rulemaking, including reviewing public comments on the proposed rule. The OCC will continue to participate in the consultation process for this rulemaking with the CFPB.

c) Have you and your team at the OCC done an analysis about the impact this proposal will have on mid-size and regional bank balance sheets?

Response: The OCC has not conducted a specific analysis of the potential impact a proposal issued by the CFPB might have on banks' balance sheets.

11. Chairman Powell has repeatedly said that there would be broad and material changes to the Basel III Endgame proposal based on the comments received. I have called for these rules to be withdrawn and re-proposed, particularly in light of the volume and breadth of comments submitted from individuals and institutions across U.S. markets, political spectrum, and geography. Notably, the comments reveal particular downsides of the proposal for the availability and cost of credit for small and medium-sized businesses.

a. In finalizing any Basel-related rules under consideration, specifically as they relate to credit risk calculations, will due consideration be given to the call for continuing flexibility to recognize the value of for highly liquid non-financial collateral, such as accounts receivable and inventory?

Response: As part of the Basel III rulemaking process, the bank regulatory agencies received a significant number of comments, including those regarding highly liquid non-financial collateral such as accounts receivable and inventory. The OCC greatly values public comments and is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (see, e.g., 5 U.S.C. § 553(c)).

b. Does the special data collection referenced in your comments include the data drawn from the agencies' direct oversight (and which informs current regulatory guidance), which support the distinction among different types of loan structures and has been provided by commenters for review?

Response: The FRB undertook a supplemental data collection to further clarify the estimated effects of the capital proposal. It is a core principle of the administrative process that federal agencies be open to considering additional data as part of a rulemaking to ensure that a proposal achieves its intended objectives. The federal banking agencies will utilize the information from this data collection, together with input from commenters on the proposal, to inform any final rule.

c. Will consideration be given to the impact of the rules on the amount of capital required to support a swingline loan structure and the disincentives it will pose, particularly when fronting exposure is mitigated by reimbursement obligations owing from highly secure investment grade financial institutions?

Response: As part of the Basel III rulemaking process, the bank regulatory agencies received a significant number of comments, which include comments on the proposal's impact on swingline loan structures. For all rulemakings, the OCC follows the Administrative Procedure Act (*see*, e.g., 5 U.S.C. § 553(c)). As part of the rulemaking process, we encouraged all stakeholders to submit comments and data on the proposal. We asked questions in the proposal to seek specific industry feedback. The OCC, along with the other federal banking agencies, is carefully reviewing and considering all comments received.

12. You stood behind the findings of the independent "Cleary report" on FDIC workplace issues and Chairman Gruenberg's temperament. Regarding the latter, while the Cleary report places severe doubt on Mr. Gruenberg's ability and "moral authority" to be able to successfully lead necessary structural changes at the FDIC, and while you stand behind the Clearly report findings, you expressed support in the May 15, 2024, Financial Services Committee hearing on oversight of the prudential regulators for Mr. Gruenberg and his ability to successfully lead necessary structural changes at the FDIC. Please explain the apparent contradiction in standing behind the Cleary report's findings and also standing behind Mr. Gruenberg who the report finds lacks the moral authority to be able to lead structural change at the FDIC.

Response: As I noted in my June 12, 2024 testimony to the Committee on Financial Services, my support for Chairman Gruenberg is conditional on his delivering on his commitment to implementing the recommendations in a timely manner.

13. Regarding a conversation with Mr. Gruenberg related to issues surrounding the posting of FDIC Board materials on the unrelated Consumer Financial Protection Bureau's website, you testified that Mr. Gruenberg expressed passion about the issues. In this conversation, did the expressions of passion involve any ill-temperament on the part of Mr. Gruenberg toward you, including using a raised voice or using curses, expletives, swear words, profanities, or any other vulgarities?

Response: My recollection is that Chairman Gruenberg was passionate but not unprofessional.

Representative Jim Himes:
Comptroller Hsu – Last month, the FDIC considered two proposals related to asset managers' investments in banks. Both proposals would have addressed situations in which an asset manager's funds collectively own more than 10% of a particular bank. In your remarks, you stressed that all three banking regulators need to be coordinated on this issue, because all three agencies have equities here. Can you expand on why the agencies need to coordinate on this particular issue?

Response: The Change in Bank Control Act (CBCA) assigns jurisdiction over CBCA notices to each of the OCC, FDIC, and FRB based on which agency is the appropriate federal banking agency for the affected institution. Regulators should work to ensure a level playing field where all institutions subject to the CBCA have equal access to investment capital.

Representative Bill Foster:
Basel III Endgame Quantitative Impact Study
Thank you for your decision to conduct a quantitative impact study (QIS) on the impact of the Basel III Endgame proposal. I believe it is an important exercise that will help our committee and the public better understand the real impact of what is being proposed on the U.S. economy. I think it is important for the findings of the QIS to be made public and allow for public engagement on the findings as you continue working to reach consensus on the proposal.
Question 1: Acting Comptroller Hsu, do you intend to release the QIS results for public comment and use public comments on the results to inform next steps on the rule?
Follow Up: What is the path forward for the Basel III Endgame QIS and final rule. Can you share any additional information regarding process, timing, and substance?

Response: The FRB undertook a supplemental data collection to further clarify the estimated effects of the capital proposal. It is a core principle of the administrative process that federal agencies be open to considering additional data as part of a rulemaking to ensure that a proposal achieves its intended objectives. The federal banking agencies will utilize the information from this data collection, together with input from commenters on the proposal, to inform any final rule. The FRB has indicated its intention to make a summary public.[1]

1"Federal Reserve Board launches data collection to gather more information from the banks affected by the large bank capital proposal it announced earlier this year," press release, October 20, 2023, https://www.federalreserve.gov/newsevents/pressreleases/bcreg20231020b.htm.

Representative Michael V. Lawler:

1. The market risk component of the Basel III Endgame proposal is highly complex and would increase capital requirements on critical market making activities by over 70%. For example, the Business Roundtable stated in their comment letter that "the new framework for market risk and the new additive requirements for derivative transactions (CVA) would significantly raise the costs for U.S. public companies to hedge business and operating risks." Derivatives are a critical risk management tool and without them, risk both inside the financial system and across the broader economy will increase. Considering that the aim of the Basel III Endgame proposal is to mitigate risk, please explain what steps you will take to ensure that the proposal does not make it more difficult for American businesses to manage risk?

Response: The OCC appreciates the importance of considering the effect the proposed framework for market risk and CVA could have on businesses, including how U.S. public companies manage risk. As part of the regulatory capital proposal, the federal banking agencies assessed the impact of the proposal on bank capital requirements and its likely effect on economic activity and resilience.[1] Additionally, the OCC performs regulatory impact analysis pursuant to the Regulatory Flexibility Act[2] and consistent with the Unfunded Mandates Reform Act of 1995.[3] Such analysis considers estimated costs and benefits of a rulemaking, including implementation costs. The OCC's regulatory impact analysis for the regulatory capital proposal is part of the "support and related materials" publicly available on Regulations.gov.[4]

1 *See* 88 FR 64167 (September 18, 2023) for the impact and economic analysis section of the regulatory capital proposal.
[2] See 5 USC 601 *et. Seq.*
[3] See 2 USC 1532.
[4] See OCC's regulatory impact analysis for the regulatory capital proposal at https://www.regulations.gov/document/OCC-2023-0008-0001.

Questions for the Record
2. Basel III Endgame's new approach to holding capital against operational risk is the biggest driver of the proposal's overall large capital increase. Operational risk is already accounted for in the Fed's annual stress test, which determines a firm's capital requirements, making this requirement duplicative without justification.

a. Would you explain it makes sense to double count the operational risk component?

Response: The OCC appreciates that banks have raised concerns that the changes to the risk-based capital framework combined with the stress test, result in a "double counting" of risk that is already captured in the minimum requirements. The federal banking agencies sought comments on all elements of the proposed risk-based capital framework, including the proposal's interaction with stress testing. The OCC greatly values public comments and is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (see, e.g., 5 U.S.C. § 553(c)).

b. As operational risk impacts every bank, product, and service, does this double-counting approach to operational risk make every bank product and service more costly?

Response: The OCC appreciates the importance of considering the effect the proposal could have on products and services, including lending to consumers and businesses. As part of the regulatory capital proposal, the federal banking agencies assessed the impact of the proposal on bank capital requirements and its likely effect on economic activity and resilience.[1] For all rulemakings, the OCC also performs an additional regulatory impact analysis pursuant to the Regulatory Flexibility Act and consistent with the Unfunded Mandates Reform Act of 1995.[2]

[1] See 88 FR 64167 (September 18, 2023) for the impact and economic analysis section of the regulatory capital proposal.
[2] See 2 USC 1532.

Representative Joyce Beatty:
Acting Comptroller Hsu, I'd like to follow up on a letter I sent you in January with many of my colleagues regarding Basel III and access to credit for low-and-moderate income and underserved communities, first time homebuyers, and small business owners. I appreciate your acknowledgement of my letter, and I understand that you're still working through the hundreds of letters, opinions, and impact statements that were submitted during the comment period. Many stakeholders in my district have brought this issue to my attention and expressed concern about the potential impacts of the rule. The capital requirements proposal is sweeping and complex, so we want to make sure we get this right for consumers and small businesses in Ohio and across the nation. How are you incorporating the feedback you've received from consumers and stakeholders?

Response: The OCC does not intend the proposal to diminish bank lending that supports homeownership opportunities, including for low- and moderate-income home buyers or other historically underserved markets. The OCC appreciates the importance of considering the effect the proposal could have on consumers and small businesses. The regulatory capital proposal included questions to solicit specific feedback on the impact of the proposal on home affordability and home ownership and encouraged all stakeholders to submit comments and data on the proposal. As part of the rulemaking process, the bank regulatory agencies received a significant number of comments on these and other issues. The OCC is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (*see*, e.g., 5 U.S.C. § 553(c)).

Representative Brad Sherman:
Coordination with Federal Home Loan Banks
Having liquidity options is critical. The prudential regulators have made it a priority to ensure that your regulated entities can access the Federal Reserve's Discount Window if necessary. What percentage of the banks under your supervision have accessed the Window this calendar year? Are all banks under your supervision ready to tap the facility if they need contingent liquidity right now?

Response: OCC expects banks to have a formal contingent funding plan (CFP) that clearly sets out the strategies for addressing liquidity shortfalls in emergency situations. A CFP should delineate policies to manage a range of stress environments, establish clear lines of responsibility, and articulate clear implementation and escalation procedures. OCC examiners routinely evaluate banks' contingency funding plans and ensure that contingency funding sources are routinely tested to ensure access and operational efficacy. The agency's network groups which include lead experts and field staff also emphasize the importance of banks establishing and testing discount window access.

It is my understanding that the Federal Home Loan Banks have worked to establish intercreditor agreements with the various Federal Reserve Banks, which allow a lender to access both the Discount Window and FHLBanks. How does (or doesn't) utilization of these agreements ensure in moments of economic stress, lenders have the necessary means to sufficient liquidity?

Response: The OCC recommends that banks diversify available funding sources in their contingent funding plans (CFPs) and that the plans have been tested and are operational.

By allowing for access to both the discount window and FHLB, the intercreditor agreements could help to ensure that cash and collateral can be moved where and when needed, which increases the likelihood of accessing sufficient liquidity during stress. Intercreditor agreements are intended to clarify the disposition and security interest in collateral. Since collateral arrangements at both the discount window and FHLB are organized as Borrower in Custody (BIC), where banks retain collateral on book, the lending entities need to have a means of clearly identifying and recording the assets pledged and ultimately borrowed against. The FRB enforces a superior collateral interest on assets and there are no instances where banks can leverage assets to borrow from both entities. A borrowing against an asset with one lender will be excluded as collateral to leverage at the other. These agreements will in effect aid in ensuring each entity can perfect its security claims and more efficiently lend in periods of stress.

Domestic Manufacturing Competitiveness
The National Association of Manufacturers highlighted in its comment letter that the Basel III Endgame proposal could "significantly increase the costs of critical risk management tools for U.S. manufacturers" given increased capital requirements associated with banks' market-making activities with respect to – for example – commodity derivatives for price fluctuations in raw materials, cross-currency swaps for international currency variations, and interest rate swaps for interest rate changes on long-term liabilities. Moreover, manufacturers say that the capital

increases associated with banks' capital markets activities may hurt America's ability to outpace foreign competitors, "thus impairing the ability of U.S. manufacturers to compete on price, capture market share, and lead the world in innovation." What are your agencies' assessments of the consequences that the Basel III Endgame proposal will have for the international competitiveness of American manufacturers – and for end-users more-generally – that want to hedge their risks?

Response: The OCC appreciates the importance of considering how the proposal may impact the ability of U.S. manufacturers and other end-users to manage market risk by hedging that risk with derivatives. The OCC is carefully considering concerns raised during the comment period, including the potentially higher capital requirements from the proposed CVA framework and proposed revisions to the market risk framework applicable to bank derivative and market-making activities, and the potential impact of those requirements on the liquidity, accessibility, and affordability of cleared derivatives. The OCC greatly values public comments and is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (*see, e.g.*, 5 U.S.C. § 553(c)).

Municipal Underwriting & Infrastructure

Congress pushed through substantial legislation to encourage investments in our infrastructure like the building of roads, schools, bridges, and hospitals across the country. As we pursue these infrastructure projects, we must be mindful not to undermine these critical investments and make municipal financing more expensive. As the Government Finance Officers Association pointed out in response to Basel III Endgame: "Increases in debt service costs for municipal issuers and conduit borrowers will result in declined investment in infrastructure, public safety, education, and numerous other social services." What do your agencies anticipate are the consequences of the Basel III Endgame proposal on financing schools, roads, or other infrastructure projects?

Response: The capital proposal is intended to strengthen the regulatory capital framework by improving its comprehensiveness and risk sensitivity, enhance the financial resilience of large banks, and improve transparency facilitating more effective supervisory and market assessments of capital adequacy. The proposed capital framework is intended to allow banks to continue to meet the needs of their communities – including financing schools, roads, or other infrastructure projects – in a manner that is consistent with the OCC's mission of ensuring safety, soundness, and fairness.

The proposal solicited comments and encouraged all stakeholders to share feedback, including supporting data. The OCC is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (see, e.g., 5 U.S.C. § 553(c)).

Representative Scott Fitzgerald:
To date the OCC has only granted one national bank charter for the custody of digital assets and related services. I find this odd after all these years considering how many state trusts are custodying digital assets. Will the OCC grant any other banks or other entities a national bank charter to custody digital assets?

Response: The OCC evaluates each application for a national bank charter on its own merits, guided by the goal of maintaining a safe, sound, and fair banking system. The OCC has previously concluded that a national bank may engage in crypto-asset custody provided that it can demonstrate, to the satisfaction of its supervisory office, that it has controls in place to conduct the activity in a safe and sound manner, and in compliance with applicable laws. See OCC Interpretive Letter 1170 (July 22, 2020) and OCC Interpretive Letter 1179 (Nov. 8, 2021). A charter applicant would be expected to similarly demonstrate its ability to conduct crypto-asset custody in a safe, sound, and fair manner, and in compliance with applicable laws.

Why do you think there are not any current applicants, or that previous applicants have not met your standards?

Response: The OCC does not comment on confidential bank- or applicant-specific information nor speculate on institutions' business decisions. However, the OCC has observed that, for example, compliance with Bank Secrecy Act/Anti-money Laundering requirements appears to be a challenge for many digital asset companies.

Representative John Rose:
Acting Comptroller Hsu, with the increased prevalence of remote work, the Committee is concerned about potential incidents of accidental disclosure or misuse of confidential Office of the Comptroller of the Currency data by employees. Please discuss with your team and provide a written response for the record on the following:

Have there been any documented incidents of accidental disclosure or misuse of confidential Office of the Comptroller of the Currency data by employees working remotely in the past five years?

If so, please provide details regarding the nature of the incidents, including:
• Date range of the incidents.
• Type of data involved (e.g., customer information, financial data).
• Actions taken by the Office of the Comptroller of the Currency to address the incidents and prevent future occurrences.

Response: The OCC has not identified disclosures or data misuse due to remote work. Regardless of an OCC employee's work location, the agency's data controls are consistent. OCC requires encryption specifications when sending an email to a non-OCC email address. OCC also manages restrictions when attempting to download data onto thumb drives and other external media. These restrictions are monitored across all users as part of the agency's cyber program.

Acting Comptroller Hsu, what are your plans regarding artificial intelligence?

Response: The OCC recognizes that rapid innovations require robust and responsive approaches by regulators. We are committed to being agile and credible on financial technology developments so that we can balance prudence with innovation. The OCC is focused on educating examiners on a wide range of artificial intelligence (AI) uses and risks as part of training courses and other educational resources. The OCC recently held a full-day workshop for all employees, which included an introduction to different types of AI, a discussion of real-world applications, live demonstrations of AI tools, and discussions on AI challenges and safety. Internal OCC use of AI technology is guided by an internal AI working group that is tasked with overseeing agency usage of AI tools and ensuring that they are used in a safe and sound manner. In addition, the OCC has implemented a policy regarding employee use of AI technologies, which highlights AI safety concerns and reminds employees of their responsibilities to safeguard OCC information.

In addition, the OCC continues to work on an interagency basis to better understand and monitor AI risks and benefits and assess the need for any additional industry policy and guidance.

Representative French Hill:
Have your agencies taken responsibility for assessing the Basel proposal's impact on the municipal bond market? What type of interaction has your agency had with the SEC or the MSRB on the topic of municipal bonds? Furthermore, how does the government plan to address the identified risks, particularly the projected increase in the cost of capital for holding municipal bonds and its potential adverse effects on borrowing costs for municipalities nationwide?

Response: The proposal is intended to strengthen the regulatory capital framework by improving its comprehensiveness and risk sensitivity, enhance the financial resilience of large banks, and improve transparency facilitating more effective supervisory and market assessments of capital adequacy. These enhancements to the capital framework are intended to allow banks to continue meeting the needs of their communities -- including establishing the market for municipal bonds to be sold to institutional investors and members of the public – in a manner that is consistent with safety and soundness principles.

The OCC appreciates the importance of considering the potential effect the proposal has on the municipal bond market. The OCC is carefully reviewing and considering all comments received on the capital proposal consistent with the requirements of the Administrative Procedure Act (*see*, e.g., 5 U.S.C. § 553(c)).

The federal banking agencies assessed the impact of the proposal on bank capital requirements and its likely effect on economic activity and resilience.[1] For all rulemakings, the OCC performs an additional regulatory impact analysis pursuant to the Regulatory Flexibility Act and consistent with the Unfunded Mandates Reform Act of 1995. The OCC's analysis of the proposal considered estimated costs and benefits, including implementation costs, and is publicly available.[2]

1 *See* 88 FR 64167 (September 18, 2023) for the impact and economic analysis section of the regulatory capital proposal.
[2] *See* OCC's regulatory impact analysis for the regulatory capital proposal at https://www.regulations.gov/document/OCC-2023-0008-0001.

Representative Zach Nunn:
Mr. Hsu, in March of last year, the SEC issued a proposed rule, "Safeguarding Advisory Client Assets," that amends the custody requirements for investment advisers. The proposed rule would expand the scope of the custody rule to include derivatives, a sea change from current requirements and applies to products that already have extensive regulation from other regulators: the CFTC, the OCC, the Federal Reserve, and the FDIC. Further, expanding the scope of the rule in this way is inconsistent with the structure of the derivatives markets, and would require some banks to take on more obligations in an already heavily regulated marketplace. These additional, contradicting requirements proposed by the SEC would only decrease the availability of derivatives, vital hedging tools for businesses all across the country. In a hearing before this Committee in February, Treasury Secretary Yellen said that she had concerns on how this proposal would impact banks and she had raised those concerns with the SEC Chairman. Do you share Secretary Yellen's concerns on the SEC's custody rule proposal, and have you shared those concerns with SEC Chairman Gary Gensler?

Response: OCC staff have informally shared comments and concerns with SEC staff about the proposed rule, as well as the regulatory framework governing the operations of bank custodians. OCC staff did not share any written comments on the proposal with the SEC.

With respect to derivatives, although bank custodians typically hold collateral associated with such transactions, we note it would be a departure from current practice for the bank to custody the derivatives themselves.

Representative Dan Meuser:
OCC Supervision of Larger Banks

1) It seems as if you'd need a deep perspective of large and regional bank practices and sophisticated examiner talent to effectively supervise companies. The OCC has the most large banks under its watch, with its heightened standards, and the Fed has all the large Bank Holding Companies, and its enhanced prudential standards. Would it be fair to say that the regulators with a broader perspective and the experience of a deep examiner bench on the large bank landscape would have an advantage on supervising large and regional banks?

   Response: The OCC has a dedicated team of examiners that provide ongoing supervision to all large banks supervised by the OCC. As part of their responsibilities, these examiners conduct planned supervisory activities and regularly meet with bank management and directors to discuss the results of the supervisory reviews, any outstanding concerns and remediation efforts, and changes in the bank's operations. This supervisory approach enables the OCC to actively monitor current and emerging issues or risks, as well as alert management and the board of any concerns in a timely manner.

OCC Bulletin 2023-34

1) Last November, the OCC released "Bulletin 2023-34" that provides guidance for banks regarding commercial loans to early-, expansion-, and late-stage companies. This bulletin misses key components on how to value venture loans. Is the OCC engaged with lenders and other regulators to evolve its views on venture loans and can we expect additional or revised guidance?

   Response: There are no plans to revise the guidance in OCC Bulletin 2023-34, "Commercial Lending: Venture Loans to Companies in an Early, Expansion, or Late Stage of Corporate Development," to address loan valuation.[1] Bank personnel, or third parties acting on behalf of banks, value loans as part of banks' accounting, lending, and risk management processes. The carrying amount is typically determined based on the outstanding loan amount plus accrued interest at a moment in time. Fair value represents an observable market price, if available. For a loan without an active market, the bank can estimate fair value based on assumptions a market participant would use to value the loan at the measurement date.[2]

   The OCC regularly engages with banks and other prudential regulators on the topic of venture loans. Loan valuation, however, has not been a focus of recent discussion. OCC examiners evaluate the regulatory risk rating of venture loans consistent with methodologies for other commercial and industrial loans and based on existing supervisory and policy standards. This includes regulations establishing operational and managerial standards relating to loan documentation, underwriting, and asset quality.[3]

1OCC Bulletin 2023-34 is available at https://www.occ.treas.gov/news-issuances/bulletins/2023/bulletin-2023-34.html.
[2] Further information for reporting on the Consolidated Reports of Condition and Income (call report) is available at https://www.ffiec.gov.
[3] For example, refer to 12 CFR 30, appendix A.

Representative Josh Gottheimer:

1. Comptroller Hsu, competition among state-chartered and national banks is vital to the American economy. Our dual-chartering framework depends upon the OCC defending its national bank powers against encroachment by state authorities. Last week, the American Bankers Association and 52 state bankers associations, including the New Jersey Bankers Association, sent you a letter urging the OCC to defend its regulatory authority against state attorneys general and lawmakers. I am concerned that so-called "fair access" laws at the state level could undermine federal efforts to ensure that nationally chartered banks are preventing financial crimes like money laundering and terrorism financing. Is the OCC concerned that these efforts undermine the OCC's role in prudential regulation of national banks? What kind of dialogue does the OCC have with state regulators on this issue?

   Response: The OCC is aware that some states have passed laws that purport to apply to OCC-supervised national banks and Federal savings associations. We share your concern about the effect of such laws on the ability of federally-chartered banks to provide financial services consistent with safety, soundness, and the fair treatment of customers. Where there is a conflict between the requirements of state and federal law, the Supremacy Clause of the U.S. Constitution is clear: state law is preempted. The OCC is closely monitoring state law developments and will vigorously defend preemption in core areas, including both national security and financial stability.

2. Acting Comptroller Hsu, I want to ask you about a topic you've spoken about a few times in the last year: the separation of banking and commerce. I'd like to hear you share your thoughts – from an activities perspective, what is banking and what is commerce? How do you judge what's on one side of the line or the other?

   Response: As I recently discussed, banking can be defined in several ways, including from an activities, legal, policy, or regulatory perspective. From an activities perspective, banks are institutions that take deposits, make loans, and facilitate payments. In practical terms, these activities involve the bundling of deposit-taking, credit intermediation, maturity transformation, and payments facilitation in single institutions. From a legal perspective, banks are the only entities authorized to take deposits. From a policy perspective, banks are "special" because in holding readily transferrable demand deposits they are able both to provide back-up liquidity to all other parties in the economy and to function as a transmission belt for monetary policy. And from a regulatory perspective, banks are chartered, regulated, and supervised by prudential authorities, like the OCC.

   "Commerce" is everything else, including nonbank finance and the unbundled components of banking. A blurring of the line between banking and commerce can lead to financial instability.

Representative John Rose:
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(Original Signature of Member)

118TH CONGRESS
2D SESSION

H. R. _____

To require the Board of Governors of the Federal Reserve System to issue a rule relating to stress capital buffer requirements, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

Mr. BARR introduced the following bill; which was referred to the Committee on _____

A BILL

To require the Board of Governors of the Federal Reserve System to issue a rule relating to stress capital buffer requirements, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Stress Testing Accountability and Transparency Act".

SEC. 2. RULEMAKING RELATED TO STRESS CAPITAL BUFFER REQUIREMENTS.

(a) IN GENERAL.—Not later than 90 days after the date of the enactment of this section, the Board of Governors of the Federal Reserve System (in this Act referred to as the "Board") shall issue a rule to establish any models, assumptions, formulas, or other decisional methodologies that are used to determine any component or subcomponent of the stress capital buffer requirement for a bank holding company.

(b) CHANGES.—The Board may only make changes to the rule issued under subsection (a) through notice and comment rulemaking.

(c) STRESS CAPITAL BUFFER REQUIREMENT DEFINED.—The term "stress capital buffer requirement" has the meaning given the term in section 225.8(c) of title 12 of the Code of Federal Regulations.

SEC. 3. RULEMAKING RELATING TO STRESS TESTING.

(a) IN GENERAL.—Beginning in the first calendar year after the date of the enactment of this section, the Board shall, not less than 30 days before conducting a stress test pursuant to section 165(i) of the Financial Stability Act of 2010, issue a rule to establish each scenario used to be used in such stress test.

(b) PROHIBITION.—The Board may not, by rule or otherwise, subject any nonbank financial company to a cli-

mate-related stress test using the authority provided in section 165(i) of the Financial Stability Act of 2010.

SEC. 4. GAO REPORT.

(a) IN GENERAL.—The Comptroller General of the United States shall, every 3 years, conduct a study and submit a report to the Congress with respect to the stress tests conducted by the Board under section 165(i) of the Financial Stability Act of 2010 in the 3 most recent calendar years.

(b) CONTENTS.—The report submitted to the Congress under subsection (a) shall—

(1) evaluate whether the stress tests are sufficiently robust and promote preparedness; and

(2) consider whether the stress tests adequately identify salient risks to—

(A) the safety and soundness of the nonbank financial institutions subjected to stress tests; and

(B) the stability of the United States financial system.

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(Original Signature of Member)

118TH CONGRESS
2D SESSION

H. R. _____

To amend the Federal Deposit Insurance Act and the Federal Credit Union Act to improve the timeliness of examination reports and other guidance and to establish panels to oversee appeals from insured depository institutions and insured credit unions of material supervisory determinations, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

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A BILL

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Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Bank Supervision Appeals Improvement Act of 2024".

SEC. 2. TIMELINESS OF EXAMINATIONS AND REQUIRED PERMISSION, REGULATORY, AND REPORTING GUIDANCE.

(a) EXIT INTERVIEW REQUIREMENT; TIMELINESS OF EXAMINATIONS.—

(1) INSURED DEPOSITORY INSTITUTIONS.—Section 10(d) of the Federal Deposit Insurance Act (12 U.S.C. 1820(d)) is amended by adding at the end the following:

"(11) EXAMINATION TIMELINESS.—The appropriate Federal banking agency shall complete any examination of an insured depository institution within 270 days of commencing the examination, except that such period may be extended by the appropriate Federal banking agency by providing written notice to the insured depository institution describing with particularity the reasons that a longer period is needed.

"(12) EXIT INTERVIEW REQUIREMENT.—Within 30 days of completing an examination, the appropriate Federal banking agency shall conduct an exit interview with the insured depository institution's senior management and board of directors.

"(13) TIMELINESS OF EXAMINATION REPORTS.—

"(A) FINAL EXAMINATION REPORT.—With respect to an examination of an insured depository institution by an appropriate Federal banking agency, the appropriate Federal banking agency shall provide a final examination report to the insured depository institution not later than 60 days after the later of—

"(i) the exit interview for the examination; or

"(ii) the provision of additional information by the insured depository institution relating to the examination.

"(B) EXAMINATION MATERIALS.—Upon the request of an insured depository institution, the appropriate Federal banking agency shall include with a final examination report an appendix listing all materials relied upon by the agency in support of all material supervisory determinations.

"(C) MATERIAL SUPERVISORY DETERMINATION DEFINED.—In this paragraph, the term 'material supervisory determination' has the meaning given such term in section 309(i)

of the Riegle Community Development and Regulatory Improvement Act of 1994.".

(2) INSURED CREDIT UNIONS.—Section 204 of the Federal Credit Union Act (12 U.S.C. 1784) is amended by adding at the end the following:

"(h) EXIT INTERVIEW REQUIREMENT; TIMELINESS OF EXAMINATIONS.—

"(1) EXAMINATION TIMELINESS.—The Board shall complete any examination of an insured credit union within 270 days of commencing the examination, except that such period may be extended by the Board by providing written notice to the insured credit union describing with particularity the reasons that a longer period is needed.

"(2) EXIT INTERVIEW REQUIREMENT.—Within 30 days of completing an examination, the Board shall conduct an exit interview with the insured credit union's senior management and board of directors.

"(3) TIMELINESS OF EXAMINATION REPORTS.—

"(A) FINAL EXAMINATION REPORT.—With respect to an examination of an insured credit union, the Board shall provide a final examina-

tion report to the insured credit union not later than 60 days after the later of—

"(i) the exit interview for the examination; or

"(ii) the provision of additional information by the insured credit union relating to the examination.

"(B) EXAMINATION MATERIALS.—Upon the request of an insured credit union, the Board shall include with a final examination report an appendix listing all materials relied upon by the Board in support of all material supervisory determinations.

"(C) MATERIAL SUPERVISORY DETERMINATION DEFINED.—In this paragraph, the term 'material supervisory determination' has the meaning given such term in section 309(i) of the Riegle Community Development and Regulatory Improvement Act of 1994.".

(b) TIMELINESS OF REQUIRED PERMISSION, REGULATORY, AND REPORTING GUIDANCE.—

(1) INSURED DEPOSITORY INSTITUTIONS.—Section 10 of the Federal Deposit Insurance Act (12 U.S.C. 1820) is amended by adding at the end the following:

"(l) TIMELINESS OF REQUIRED PERMISSION, REGULATORY, AND REPORTING GUIDANCE.—

"(1) REQUEST FOR PERMISSION OR GUIDANCE.—An insured depository institution may request a written determination by the appropriate Federal banking agency of—

"(A) the agency's permission to take an action where permission is mandated by regulation;

"(B) the agency's interpretation of a law or regulation; and

"(C) the agency's interpretation of generally accepted accounting principles or accounting objectives, standards, and requirements under section 37.

"(2) CONTENTS OF REQUEST.—A request made under paragraph (1) shall be in writing and contain—

"(A) the nature of the request;

"(B) applicable facts relating to the matter;

"(C) applicable law, regulation, or generally accepted accounting principles relating to the matter; and

"(D) a summary of the request.

"(3) RESPONSE TO REQUEST.—A Federal banking agency receiving a request under paragraph (1) shall, not later than 30 days after receiving the request—

"(A) provide the insured depository institution making the request with written notification that the agency received the request and stating whether the request contains the information required under paragraph (2); and

"(B) if the request does not contain the information required under paragraph (2), provide the insured depository institution with an explanation of what information is missing.

"(4) PROVIDING MISSING INFORMATION.—If a Federal banking agency informs the insured depository institution under paragraph (3) that the request does not contain all the information required under paragraph (2), the insured depository institution may provide the missing information to the Federal banking agency during the 30-day period beginning on the date the insured depository institution receives the explanation of the missing information under paragraph (3).

"(5) DETERMINATION.—A Federal banking agency receiving a request under paragraph (1) shall

make a determination on the request and provide the insured depository institution with a written notice of such determination—

"(A) if the initial request contains the information required under paragraph (2), not later than the end of the 60-day period beginning on the date the Federal banking agency notifies the insured depository institution of the receipt of the request under paragraph (3); or

"(B) if the initial request does not contain the information required under paragraph (2)—

"(i) not later than the end of the 60-day period beginning on the date that the insured depository institution provides the Federal banking agency with the missing information under paragraph (4); or

"(ii) if the insured depository institution does not provide the Federal banking agency with the missing information within the 30-day period described under paragraph (4), not later than the end of the 60-day period beginning on the end of such 30-day period.

"(6) REPORTS AND PUBLICATION.—Each Federal banking agency shall, within 120 days after

making a determination under paragraph (5), publish a summary of the determination. Each Federal banking agency shall redact any confidential supervisory information about the insured depository institution, any identifying facts about the institution, and any sensitive personally identifiable information.".

(2) INSURED CREDIT UNIONS.—Section 209 of the Federal Credit Union Act (12 U.S.C. 1789) is amended by adding at the end the following:

"(c) TIMELINESS OF REQUIRED PERMISSION, REGULATORY, AND REPORTING GUIDANCE.—

"(1) REQUEST FOR PERMISSION OR GUIDANCE.—An insured credit union may request a written determination by the Board of—

"(A) the Board's permission to take an action where permission is mandated by regulation;

"(B) the Board's interpretation of a law or regulation; and

"(C) the Board's interpretation of generally accepted accounting principles or other accounting objectives, standards, and requirements.

"(2) CONTENTS OF REQUEST.—A request made under paragraph (1) shall be in writing and contain—

"(A) the nature of the request;

"(B) applicable facts relating to the matter;

"(C) applicable law, regulation, or generally accepted accounting principles relating to the matter; and

"(D) a summary of the request.

"(3) RESPONSE TO REQUEST.—The Board, upon receiving a request under paragraph (1) shall, not later than 30 days after receiving the request—

"(A) provide the insured credit union making the request with written notification that the Board received the request and stating whether the request contains the information required under paragraph (2); and

"(B) if the request does not contain the information required under paragraph (2), provide the insured credit union with an explanation of what information is missing.

"(4) PROVIDING MISSING INFORMATION.—If the Board informs the insured credit union under paragraph (3) that the request does not contain all

the information required under paragraph (2), the insured credit union may provide the missing information to the Board during the 30-day period beginning on the date the insured credit union receives the explanation of the missing information under paragraph (3).

"(5) DETERMINATION.—The Board shall make a determination on a request made under paragraph (1) and provide the insured credit union with a written notice of such determination—

"(A) if the initial request contains the information required under paragraph (2), not later than the end of the 60-day period beginning on the date the Board notifies the insured credit union of the receipt of the request under paragraph (3); or

"(B) if the initial request does not contain the information required under paragraph (2)—

"(i) not later than the end of the 60-day period beginning on the date that the insured credit union provides the Board with the missing information under paragraph (4); or

"(ii) if the insured credit union does not provide the Board with the missing in-

formation within the 30-day period described under paragraph (4), not later than the end of the 60-day period beginning on the end of such 30-day period.

"(6) REPORTS AND PUBLICATION.—The Board shall, within 120 days after making a determination under paragraph (5), publish a summary of the determination. The Board shall redact any confidential supervisory information about the insured credit union, any identifying facts about the credit union, and any sensitive personally identifiable information.".

SEC. 3. UPDATE OF INDEPENDENT INTRA-AGENCY APPELLATE PROCESS FOR REVIEWING MATERIAL SUPERVISORY DETERMINATIONS.

(a) UPDATE OF INDEPENDENT INTRA-AGENCY APPELLATE PROCESS.—Not later than 180 days after the date of enactment of this Act, the Board of Governors of the Federal Reserve System, the Comptroller of the Currency, the Federal Deposit Insurance Corporation Board, and the National Credit Union Administration Board shall revise the independent intra-agency appellate process required under section 309(a) of the Riegle Community Development and Regulatory Improvement Act of 1994 (12 U.S.C. 4806(a)).

(b) OFFICE OF SUPERVISORY APPEALS; APPEALS PROCESS.—Section 309 of the Riegle Community Development and Regulatory Improvement Act of 1994 (12 U.S.C. 4806) is amended—

(1) by redesignating subsection (f) as subsection (i); and

(2) by inserting after subsection (e) the following:

"(f) OFFICE OF SUPERVISORY APPEALS.—The Federal banking agencies and the National Credit Union Administration shall each establish an Office of Supervisory Appeals to carry out the independent intra-agency appellate process required under this section.

"(g) APPEALS OFFICIALS.—

"(1) APPOINTMENT.—The head of each of the Federal banking agencies and the National Credit Union Administration shall appoint appeals officials, in a number sufficient to fully staff the panels described under subsection (h), from among the following classes of individuals:

"(A) Individuals who have financial institutions regulatory agency experience.

"(B) Individuals who—

"(i) are a licensed attorney or a certified public accountant authorized to prac-

tice under the laws of a State, the District of Columbia, or a territory of the United States

"(ii) have either academic or private sector experience;

"(iii) have relevant subject matter knowledge or work-related experience in the financial services sector, as determined by the agency making the appointment; and

"(iv) are not, and were not during the previous 10-year period, employed by a Federal banking agency, a Federal reserve bank, or the National Credit Union Administration.

"(C) Individuals—

"(i) with at least 10 years private sector financial services senior management-level experience; and

"(ii) recommended by—

"(I) an insured depository institution;

"(II) an insured credit union; or

"(III) a trade association for such institutions or credit unions.

"(2) TERM.—

"(A) IN GENERAL.—Each appeals official appointed under paragraph (1) shall serve for a term of 3 years.

"(B) TERM LIMITATION.—No individual may be appointed under paragraph (1) to serve more than 2 full terms.

"(C) DISMISSAL.—An appeals official appointed under paragraph (1) may be removed at any time by the appointing agency.

"(h) APPEALS PROCESS AND PANEL HEARING OF MATERIAL SUPERVISORY DETERMINATIONS.—

"(1) APPEAL TO THE HEAD OF SUPERVISION.—

"(A) IN GENERAL.—An institution seeking an appeal of a material supervisory determination shall—

"(i) file a written appeal to the head of supervision for the agency not later than 30 days after receiving the material supervisory determination from the agency; and

"(ii) include in the appeal—

"(I) a clear and complete statement of all relevant facts and issues;

"(II) all arguments that the institution wishes to present; and

"(III) all relevant and material documents that the institution wishes to be considered.

"(B) EXTENSION.—The institution may file a written request with the head of supervision for an extension of the 30-day time period described under subparagraph (A)(i), which shall state good cause for granting the extension. Such request shall be granted in the sole discretion of the head of supervision.

"(C) INFORMATION MADE AVAILABLE TO INSTITUTION.—An institution seeking an appeal of a material supervisory determination may, not later than 7 days after receiving the material supervisory determination, request that the agency provide the institution with any information relied upon by the agency in making the material supervisory determination. The agency shall provide that information to the institution not later than 14 days after receiving the request.

"(2) CONSIDERATION OF APPEAL BY THE HEAD OF SUPERVISION.—

"(A) IN GENERAL.—A head of supervision receiving an appeal under paragraph (1) shall,

after reviewing the information provided by the institution in such appeal—

"(i) grant the appeal;

"(ii) refer the appeal to a panel appointed under paragraph (3); or

"(iii) deny the appeal.

"(B) NOTIFICATION.—A head of supervision shall promptly inform the institution and the head of the agency after granting, referring, or denying an appeal under subparagraph (A).

"(C) RIGHT TO APPEAL DENIAL.—An institution that has an appeal denied by the head of supervision under subparagraph (A) may appeal such denial to a panel appointed under paragraph (3).

"(3) APPOINTMENT OF PANEL.—

"(A) IN GENERAL.—With respect to each appeal referred by a head of supervision under paragraph (2)(A)(ii) or appealed by an institution after a denial under paragraph (2)(A)(iii), the agency shall appoint a panel of 3 appeals officials to provide a recommendation on such appeal, with 1 of the 3 appeals officials being appointed to the panel from individuals in each

of the classes described under subparagraphs (A), (B), and (C) of subsection (g)(1).

"(B) REPORTING PROHIBITION.—An appeals official may not be appointed to a panel under subparagraph (A) if the appeals official is reporting, or has reported, directly or indirectly, to the agency official who made the material supervisory determination under review.

"(4) PANEL HEARINGS.—

"(A) REQUEST FOR HEARING.—An institution may request a hearing with the panel on the institution's appeal by—

"(i) making such request not later than 7 days after the date on which the institution is informed the head of supervision referred an appeal to a panel under paragraph (2); or

"(ii) making such request in the institution's appeal of a denial of the institution's appeal under paragraph (2).

"(B) TIMING OF HEARING.—If an institution requests a hearing, as described under subparagraph (A), the panel shall provide the institution with a hearing on the institution's appeal not later than 30 days after the date the hear-

ing is requested, except the panel may, in the discretion of the panel or upon good cause shown, extend such deadline by up to 15 days.

"(C) RULEMAKING.—The Federal banking agencies and the National Credit Union Administration shall each issue rules to establish procedures for panel hearings described under this paragraph, including that—

"(i) the institution may appear at the hearing personally or through counsel;

"(ii) the institution may provide an oral and written presentation at the hearing;

"(iii) the panel may ask questions of any person participating in the hearing;

"(iv) the hearing may not involve—

"(I) taking testimony;

"(II) a cross-examination; and

"(III) discovery;

"(v) the hearing shall not governed by formal rules of evidence; and

"(vi) the panel shall have a verbatim transcript of the hearing prepared.

"(5) RECOMMENDATION BY PANEL.—

"(A) IN GENERAL.—A panel making a recommendation on an appeal under this subsection shall make the recommendation not later than—

"(i) 90 days after the date on which the appeal was referred by a head of supervision under paragraph (2)(A)(ii) or appealed by an institution after a denial under paragraph (2)(A); or

"(ii) if the institution requested a hearing under paragraph (4), 60 days after the date on which the hearing concluded.

"(B) FORM OF RECOMMENDATION.—The panel may recommend—

"(i) that the material supervisory determination be continued, terminated, or otherwise modified; or

"(ii) that the material supervisory determination be remanded to the examiners to allow the examiners to consider additional information presented in connection with the appeal.

"(C) NOTICE.—After a recommendation is made under subparagraph (A), the panel shall promptly notify the institution, the head of su-

pervision of the agency, and the head of the agency of the recommendation, which shall contain a statement of the basis for the panel's recommendation and identify the information on which the panel relied in reaching the recommendation.

"(D) PUBLICATION.—A copy of each panel recommendation shall be posted on the agency's public website as soon as practicable, with exempt information redacted. If the panel determines that redaction is insufficient to prevent improper disclosure, the recommendation may be presented in summary form.

"(E) STANDARD OF REVIEW.—A panel's review of a material supervisory determination being appealed under this subsection shall be de novo.

"(F) NO AUTHORITY TO DELAY OR STAY ORDERS.—A panel shall have no authority to delay or stay the implementation of any formal order from the applicable agency.

"(6) REVIEW BY THE HEAD OF THE AGENCY.—

"(A) RESPONSE BY INSTITUTION.—Not later than 15 days after receiving a notice of a recommendation under paragraph (5)(C), the

institution may submit to the head of the agency written exceptions to the recommended decision.

"(B) REVIEW BY HEAD OF THE AGENCY.—Not later than 45 days after receiving a notice of a recommendation under paragraph (5)(C), the head of an agency shall review such decision and either ratify or reject the panel's decision.

"(C) REVIEW MAY NOT BE DELEGATED.—A review by the head of an agency under this paragraph may not be delegated to any other employee of the agency and, in the case of an agency that is headed by a body made up of multiple individuals, all such individuals shall participate in the review.

"(D) REPORTS TO CONGRESS.—The Federal banking agencies and the National Credit Union Administration shall each, not later than 90 days after the end of each calendar year, issue a report to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate describing the actions taken by the agency under this paragraph

during such calendar year, including information on each of the panel decisions reviewed, after redacting any confidential supervisory information.

"(E) PUBLICATION.—A copy of each decision by the head of the agency under this paragraph shall be posted on the agency's public website as soon as practicable, with exempt information redacted. If the head of the agency determinates that redaction is insufficient to prevent improper disclosure, the decision may be presented in summary form.

"(7) RIGHT TO JUDICIAL REVIEW.—An institution shall have the right to petition for review of an agency head's decision under paragraph (6) by filing a petition for review not later than 60 days after the date on which the decision was made in the United States Court of Appeals for the District of Columbia Circuit or the circuit in which the institution is located.

"(8) RETALIATION PROHIBITED.—The Federal banking agencies and the National Credit Union Administration may not—

"(A) retaliate against an insured depository institution or insured credit union, or a

service provider or institution-affiliated party of an insured depository institution or insured credit union, for exercising rights under this subsection; or

"(B) delay or deny any agency action that would benefit an insured depository institution or insured credit union, or a service provider or institution-affiliated party of an insured depository institution or insured credit union, on the basis that a matter under this section is pending under this section.

"(9) DEFINITIONS.—With respect to the appeal of a material supervisory determination under this subsection:

"(A) AGENCY.—The term 'agency' means the Federal agency, either a Federal banking agency or the National Credit Union Administration, that made the material supervisory determination.

"(B) INSTITUTION.—The term 'institution' means the company, either an insured depository institution or an insured credit union, with respect to which the material supervisory determination was made.".

SEC. 4. REVIEW OF RESOLUTION ACTIONS RESULTING IN A MATERIAL LOSS.

Section 38(k) of the Federal Deposit Insurance Act (12 U.S.C. 1831o(k)) is amended by adding at the end the following:

"(7) REVIEW OF RESOLUTION ACTIONS BY CORPORATION INSPECTOR GENERAL.—

"(A) IN GENERAL.—If the Deposit Insurance Fund incurs a material loss with respect to an insured depository institution, the inspector general of the Corporation shall—

"(i) review the Corporation's resolution of the institution to determine whether the material loss to the Deposit Insurance Fund could have been avoided by the Corporation when resolving the institution; and

"(ii) make a written report to the Corporation and the Congress containing the results of such review and any recommendations for preventing a material loss to the Deposit Insurance Fund in the future when resolving an institution.

"(B) TESTIMONY TO CONGRESS.—If the inspector general of the Corporation determines, in a review carried out under subpara-

graph (A) that the Corporation's resolution of an institution caused a material loss to the Deposit Insurance Fund, but such resolution could have been carried out in a manner to avoid such a material loss, the Chairperson of the Corporation shall testify before the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate to explain why the material loss occurred.".

(Original Signature of Member)

118TH CONGRESS
2D SESSION

H. R. _____

To require the Board of Governors of the Federal Reserve System to carry out a review of discount window operations, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

Mr. BARR introduced the following bill; which was referred to the Committee on _____

A BILL

To require the Board of Governors of the Federal Reserve System to carry out a review of discount window operations, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Bringing the Discount Window into the 21st Century Act".

SEC. 2. REVIEW OF DISCOUNT WINDOW OPERATIONS.

Section 10 of the Federal Reserve Act (12 U.S.C. 241 et seq.) is amended—

(1) by redesignating paragraph (12) as paragraph (11); and

(2) by adding at the end the following:

"(12) REVIEW OF DISCOUNT WINDOW OPERATIONS.—

"(A) IN GENERAL.—Not later than 60 days after the date of enactment of this paragraph, the Board of Governors shall commence a review of the discount window lending programs of the Federal reserve banks (the 'discount window'), and shall complete such review not later than 240 days after the date of enactment of this paragraph.

"(B) CONTENTS.—The review required by subparagraph (A) shall include a consideration of—

"(i) the effectiveness of the discount window in providing liquidity to financial institutions, including in times of financial stress;

"(ii) whether the technology infrastructure, including means of communications, are sufficient to support the timely provision of liquidity, including in times of financial stress;

"(iii) the effectiveness of cybersecurity measures;

"(iv) the effectiveness of communications between Federal reserve banks regarding discount window operations;

"(v) the effectiveness of the Board of Governors in providing oversight of the discount window;

"(vi) how the discount window interacts with other providers of liquidity, including the Federal Home Loan Banks, during both normal operations and times of financial distress; and

"(vii) the effectiveness of existing discount window operating hours and whether such hours should be expanded, taking into account the interaction between discount window operating hours and the operating hours of payment systems of the Board of Governors and Federal reserve banks, such as FedWire and FedNow.

"(C) PUBLIC COMMENT.—In carrying out the review required by subparagraph (A), the Board of Governors shall provide the public with an opportunity to comment on the effec-

tiveness of discount window operations and to offer suggestions for improving operations.

"(D) REMEDIATION PLAN.—After completing the review required by subparagraph (A) and considering any public comments received pursuant to subparagraph (C), the Board of Governors shall develop, and approve by a vote of the Board of Governors, a written plan to remediate any identified deficiencies or areas for enhancing effectiveness of the discount window, which shall include—

"(i) an identification of actions that the Board of Governors will take to remediate those deficiencies;

"(ii) timelines and milestones for implementing the plan and measures to demonstrate how the Board of Governors will maintain implemented improvements on an ongoing basis; and

"(iii) measures of managing and controlling deficiencies until the plan is implemented in full.

"(E) REPORT TO CONGRESS ON REVIEW AND PLAN.—

"(i) IN GENERAL.—Not later than 365 days after the date of enactment of this paragraph, the Board of Governors shall, after approval by a vote of the Board of Governors, submit a report to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate containing—

"(I) the findings of the review required by subparagraph (A);

"(II) the remediation plan required by subparagraph (D);

"(ii) CONSULTATION.—Before submitting the report required by clause (i), the Board of Governors shall—

"(I) provide a copy of the proposed report to the Comptroller General of the United States and the Inspector General of the Board of Governors of the Federal Reserve System and the Bureau of Consumer Financial Protection; and

"(II) provide the Comptroller General and Inspector General with

an opportunity to provide feedback on the report.

"(iii) TESTIMONY.—The Chairman of the Board of Governors shall testify before the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate with respect to the contents of the report required under this subparagraph.

"(F) ANNUAL REPORTS TO CONGRESS.—

"(i) REPORTS BY THE BOARD.—The Board of Governors shall submit an annual report to the Committee on Financial Services of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate containing a review of the effectiveness of discount window operations.

"(ii) REPORTS BY THE INSPECTOR GENERAL.—The Inspector General of the Board of Governors of the Federal Reserve System and the Bureau of Consumer Financial Protection shall submit an annual report to the Committee on Financial Serv-

ices of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate containing a report on the progress of the Board of Governors in implementing the remediation plan required by subparagraph (D).

"(G) CONFIDENTIAL REPORT INFORMATION.—Any report required under this paragraph may contain a confidential annex containing information that details any cybersecurity deficiencies or any deficiencies which, if made public, could cause financial instability.".

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118TH CONGRESS
1ST SESSION

H. R. 4346

To raise the consolidated assets threshold under the small bank holding company policy statement, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

JUNE 23, 2023

Mr. MOONEY (for himself, Mr. BARR, Mr. DONALDS, Ms. DE LA CRUZ, Mr. OGLES, and Mr. NUNN of Iowa) introduced the following bill; which was referred to the Committee on Financial Services

A BILL

To raise the consolidated assets threshold under the small bank holding company policy statement, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Small Bank Holding Company Relief Act of 2023".

SEC. 2. CHANGES REQUIRED TO THE SMALL BANK HOLDING COMPANY AND SAVINGS AND LOAN HOLDING COMPANY POLICY STATEMENT.

Not later than 180 days after the date of enactment of this Act, the Board of Governors of the Federal Reserve System shall revise appendix C to part 225 of title 12, Code of Federal Regulations (commonly known as the "Small Bank Holding Company and Savings and Loan Holding Company Policy Statement"), to raise the consolidated asset threshold under that appendix to $10,000,000,000 for any bank holding company or savings and loan holding company.

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