Remarks

By

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Thank you for having me here today. On behalf of Acting Comptroller of the Currency Keith Noreika, it's my pleasure to join you and share the OCC's perspective on the issues and topics that are important to our community banks and federal savings associations. Mr. Noreika hoped to be able to deliver these remarks personally, but is engaged in ensuring that transition to the 31st Comptroller of the Currency goes as smoothly as possible. In many ways, community banks are the backbone of our financial system, playing a vital role in meeting the needs of consumers and businesses in cities and towns nationwide. You are a key part of your community's heart and soul. Our country is unique in the number of types and sizes of banking institutions we have, and that diversity contributes to the overall resiliency and health of our financial system. As regulators, we should be doing everything we can to ensure that the system remains vibrant and adaptable to the changing needs and challenges of the marketplace, and that the institutions we supervise continue to meet customers' needs by operating in a safe and sound manner, providing fair access to financial services, and treating customers fairly.

Today, I want to share the OCC's optimism about the industry and the opportunity for meaningful regulatory relief, discuss some of the efforts underway at the OCC, and highlight a few issues that we all should continue to watch closely.

We have good reason for being optimistic about achieving regulatory relief that promotes economic opportunity. Bankers, industry representatives, regulators, and legislators are having conversations today that would not have been possible just a few months ago. That change in tone is very encouraging, and suggests that we can have a constructive process for sharpening our regulatory framework to ensure that it works for everyone. I think this process is just beginning, and that it is good for banks, their customers, and the nation's economy.

In testimony before the Senate Banking Committee in June, the Acting Comptroller shared 17 ideas for Congressional consideration that have since been widely distributed on Capitol Hill and in the press.[1] These ideas have generated a good deal of interest and additional conversation. These ideas also complement the Treasury's core financial principles released in June that lay out many opportunities and a direction that should be helpful in our conversations about rebalancing regulation and promoting economic opportunity.[2] In anything we consider, we need to weigh the cumulative effects of our actions. That includes the impacts on banks, consumers, markets, and other industry participants involved in delivering financial products and services to consumers, businesses, and communities.

The biggest reason for the growing optimism is the progress that we are seeing in a number of important areas. The first worth noting is the simplification of capital requirements. In September, the OCC, the Federal Deposit Insurance Corporation, and the Federal Reserve Board published a proposed rule to simplify agencies' regulatory capital requirements for banks with less than $250 billion in consolidated assets.[3] I think that applies to most everyone in this room.

[1] See Testimony of Keith A. Noreika, Acting Comptroller of the Currency, Before the Committee on Banking, Housing, and Urban Affairs. U.S. Senate. June 22, 2017 (https://www.occ.gov/news-issuances/news-releases/2017/nr-occ-2017-71b.pdf).
[2] *A Financial System That Creates Economic Opportunities: Banks and Credit Unions*. U.S. Department of the Treasury. June 2017.
[3] See "Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996." September 27, 2017 (https://www.occ.gov/news-issuances/news-releases/2017/nr-ia-2017-111a.pdf).

Generally, the proposal would replace the current, complex treatment of high-volatility commercial real estate exposures with a more straightforward treatment for most acquisition, development, and construction loans. It also would simplify the capital treatment for mortgage servicing assets, certain deferred tax assets, investments in the capital instruments of unconsolidated financial institutions, and minority interests. I hope you have taken the opportunity to comment on the proposed rule.

Another reason for optimism is the recent bipartisan agreement in the U.S. Senate, announced Monday, to make sweeping legislative reforms that would deliver meaningful relief to community banks and help rationalize our regulatory framework. The proposal includes a number of targeted fixes in a variety of areas that the OCC supported and were included in the Treasury Report on financial core principles.[4] Some of the reforms announced include raising the threshold for enhanced prudential standards for certain bank holding companies from $50 billion to $250 billion, and granting federal savings associations under $15 billion greater flexibility to operate with the same powers and duties as national banks. The proposal would exempt companies under $10 billion from the Volcker Rule if their trading assets and liabilities are less than 5 percent of their consolidated assets, and would require regulators to reduce reporting requirements for depository institutions with less than $5 billion in total consolidated assets and simplify capital requirements for community banks by establishing a community bank leverage ratio of tangible equity to average consolidated assets of not less than 8 percent and not more than 10 percent. We will closely review the proposal when it is introduced.

While there is optimism about opportunities for regulatory reform and promoting economic opportunities, we must remain vigilant toward key risks facing your institutions and

[4] Financial System That Creates Economic Opportunities: Banks and Credit Unions. U.S. Department of Treasury. June 2017 (https://www.treasury.gov/press-center/press-releases/Documents/A%20Financial%20System.pdf).

the federal banking system as whole. OCC staff members spend a significant amount of time and effort identifying, assessing, and communicating these risks to bankers, examiners, and other industry stakeholders through public reports and outreach. The agency's *Semiannual Risk Perspective*, which highlights key risks facing the federal banking system and our supervisory priorities, is one of our principal communication tools.[5]

The most recent report indicates that strategic, credit, operational, and compliance risks should be watched closely. Strategic risk remains elevated, as banks expand into new products or services, consider new delivery channels, conduct merger and acquisition activity, and compete with new entrants to the financial services space. One of the most significant strategic risks facing community banks involves succession planning—ensuring that your bank has the right leadership, experience, and talent to continue your good work. We see too many family-owned and operated banks reach a point where the next generation chooses to leave banking and as a result more small banks disappear.

While lagging measures of credit quality are quite good, credit risk remains elevated, as commercial and retail credit underwriting has loosened, showing a transition from a conservative stance coming out of the great recession to an increasing risk appetite over the past few years as banks strive to achieve loan growth and maintain or grow market share. Strong commercial real estate (CRE) loan growth is evident in all sizes of banks, but the CRE concentration build-up is primarily in community banks. Results from recent supervisory activities raise our concern over the quality of CRE risk management. Credit risk is increasing because of increased risk layering, rising loan policy exceptions, higher loan-to-value ratios, and weaker loan controls or covenant protections. At the same time, CRE investment has shifted from multifamily to retail sector

[5] See https://www.occ.gov/publications/publications-by-type/other-publications-reports/index-semiannual-risk-perspective.html.

projects, and the condition of the local economy can have a profound effect on the performance of these credit assets. Stress in the agricultural economy is something we are also watching closely. While the impact on banks with ag concentrations has been limited so far, forecasts of prolonged low commodity prices combined with rising interest rates and other potential stresses warrant close attention for banks with concentrations in ag loans and banks whose local economy is dependent at agriculture.

Operational risk covers a broad spectrum of concerns, including increasing cyber threats, reliance on concentrations in significant third-party service providers, and the need for sound governance over products, service, and delivery. One operational issue that crosses over into compliance risk involves banks' implementation of effective programs to comply with the Bank Secrecy Act (BSA), which helps protect our financial institutions and system from money laundering, terrorist financing, and other illegal activities.

For some banks, meeting BSA requirements is difficult, creating a source of compliance risk. Other compliance challenges banks face include adapting to the integrated mortgage disclosures under the Truth in Lending Act and Real Estate Settlement Procedures Act, the new requirements associated with implementing the Military Lending Act, and changes to the data collection and processing rules for the Home Mortgage Disclosure Act. These are risks that should sound very familiar to all of you, and it should not be a surprise that we will be focusing on these areas in the next six to 12 months.

One publication I encourage all of you to take a look at is our bank supervision operating plan for fiscal year 2018.[6] It provides the foundation for policy initiatives and for supervisory

[6] "Fiscal Year 2018 Bank Supervision Operating Plan." OCC. September 28, 2017 (https://www.occ.gov/news-issuances/news-releases/2017/nr-occ-2017-113.html).

strategies as applied to individual banks like yours, and OCC staff members use this plan to guide our supervisory priorities, planning, and resource allocations.

The publications we provide, and the resources and analytical tools national banks and federal savings associations can find on the OCC's BankNet website, are important in raising awareness of the risks to our banking system. But, the greatest resources community banks have are the teams of examiners who are assigned to your banks and who live in many of your communities. Many people think of the OCC as "the big-bank regulator." The reality is that community banks under $1 billion in assets make up more than 80 percent of the nearly 1,360 banks we supervise, and the majority of the men and women at the OCC are involved in community bank supervision. They share a passion for community banking, and our examiners and senior staff are never more than a phone call away. Whatever your concerns, they can share insight gained from having looked across many banks and can connect you to additional experts in accounting, legal, compliance, information technology, and economics.

If you need information about innovations in financial services, the OCC clearly has been a leader in the field, and our Office of Innovation is available to help. Headed by Chief Innovation Officer Beth Knickerbocker, the team was formed to be a resource for community banks. It began operating in earnest in January and serves as a clearinghouse for innovation-related matters and as a central point of contact for OCC staff, banks, nonbank companies, and other industry stakeholders. The office has published guides and reference materials for community banks, as well as financial technology companies and nonbank institutions.[7]

The Office conducts a good deal of outreach. So far, the team has held "office hours" in San Francisco and New York and plans to hold others in hubs of financial innovation. During

[7] See "Responsible Innovation" on occ.gov (https://www.occ.gov/topics/responsible-innovation/index-innovation.html).

these meetings, team members explore potential innovations, issues facing community banks, and how companies can work with banks. Please take advantage of these events when they are held near you, or contact Beth and her team through our website or by phone.

Open, two-way communication is the key to successful supervision, and the expertise and insight of OCC employees is one of the greatest values of maintaining a federal charter. I encourage you to take full advantage of the staff assigned to your institution.

Thank you again for having me here. Interacting with the bankers of this country is one of the highlights of my career at the OCC. During my many years at the OCC, I' have found that bankers across the country share a goal of serving their communities and delivering banking products in a safe, sound, and fair manner. I know everyone at the OCC share that purpose too, because they understand just how important community banks are to communities, the federal banking system, and our nation as whole.

Now, I'd be happy to answer as many questions as time permits.