Remarks

by

Thomas J. Curry
Comptroller of the Currency

Distinguished Banking and Finance Lecture Series
Central Connecticut State University

New Britain, Connecticut

March 9, 2017

Good evening. Thank you for inviting me to participate in the Distinguished Banking and Finance Lecture Series here at Central Connecticut State University. It's an honor to join the long and distinguished list of speakers who have addressed this institution, and I always enjoy returning to New England, which I call home. It's also a treat to see long-time friends like Howard Pitkin. It is wonderful that so many students can benefit and learn from Howard's nearly 40 years as a bank regulator. Howard, thank you for the invitation to speak tonight.

As Comptroller of the Currency, I have the opportunity to speak to many groups. Some are more familiar with what we do as regulators than others. That's why I enjoy events like this one, because you understand the important work done by the Office of the Comptroller of the Currency (OCC) over the last 154 years. You already know that the agency charters and supervises more than 1,400 banks and thrifts across the nation, from community banks meeting local needs to the nation's largest internationally active banks. It has been my honor to serve as Comptroller over the last five years, and I am very proud of the work that the 4,000 men and women at the OCC do each day.

As Comptroller, I've also been involved in the efforts to make our nation's financial services industry more resilient and capable of meeting the changing needs of the consumers, businesses, and communities it serves. Tonight, I want to share a few observations about the condition of our federal banking system today and how things have changed since the crisis that started 10 years ago.

I want to begin by talking about an aspect of our banking system that is not often discussed, but that I feel strongly about—the diversity of our financial system. When I speak of diversity, I am talking about many things. Of course, we need banks with ownership and management that reflect the diversity of the people who make up our nation. We also need banks that vary in size and complexity, with various business models and ownership structures. And, we need a healthy dual banking system, with federal banks complementing state-chartered ones. This diversity helps the system remain vibrant, to meet all of our nation's financial services needs, and to be capable of adapting to change and withstanding adversity.

When Howard invited me to speak, he reminded me that this event was made possible by a grant from the American Savings Foundation, a legacy of the former American Savings Bank. He said "legacy" because American Savings Bank is one of our country's many community banks that have disappeared as a result of industry consolidation. More to the point, it was a mutually owned savings association that converted to a stock-owned institution and was then acquired. During my career as Comptroller, FDIC board member, and as Bank Commissioner in Massachusetts, I've spent a good deal of time addressing issues of importance to community banks and savings associations, including mutually owned institutions, because they are important to the diversity of the banking system and often serve as anchors for their communities.

That's why, in 2014, the OCC issued guidance that stressed the special characteristics of mutual savings associations and the unique supervisory considerations such institutions present.[1]

[1] See OCC Bulletin 2014-35, "Mutual Federal Savings Associations." July 22, 2014 (https://www.occ.gov/news-issuances/bulletins/2014/bulletin-2014-35.html).

The idea for that guidance came from a meeting of our Mutual Savings Association Advisory Committee. The committee advises the OCC on how to ensure the continued health and viability of mutuals, and it has helped me and the OCC team stay on top of concerns facing mutuals.[2] The committee also has been a source of ideas that help all community institutions, such as our paper on collaboration.[3] That paper explores how community banks and thrifts can share expertise, resources, and costs to take advantage of some of the economies of scale that benefit larger institutions. Examples of successful collaboration include exchanging information, jointly purchasing materials or services, sharing back-office functions, and working together to conduct due diligence and monitor the performance of shared service providers. Community banks may find that the savings outweigh the competitive challenges that result from collaboration, particularly if they work with companies that are not direct competitors.

While mutuals are unique, they share the same challenges facing other community banks. One of those challenges involves undue regulatory burden. I've worked to eliminate or streamline regulations that don't make sense, and to make necessary regulations clearer so community banks can easily understand and meet their regulatory responsibilities. We can't eliminate all burden, but we can work to provide relief where it makes sense and where we have discretion.

One good example is reporting. I have heard from many community banks about the demands of reporting and the complexity of the "Call Report." At the end of 2016, the OCC joined the Fed and the FDIC to finalize changes to the Call Report and streamline reporting for community banks. Through the Federal Financial Institutions Examination Council, we reduced the report from 85 to 61 pages and removed 40 percent of the 2,400 data items[4] for 90 percent of

[2] See OCC Mutual Savings Association Advisory Committee (https://www.occ.gov/topics/bank-management/mutual-savings-associations/mutual-savings-associations-advisory-committee.html).
[3] See "An Opportunity for Community Banks: Working Together Collaboratively." January 2015 (https://www.occ.gov/publications/publications-by-type/other-publications-reports/pub-other-community-banks-working-collaborately.PDF).
[4] See "FFIEC Streamlines "Call Report" for Small Institutions." December 30, 2016 (https://www.ffiec.gov/press/pr123016.htm).

all filers. That is a significant step in the right direction.

Regulators, of course, don't have the power to implement every change that makes sense. Some require legislative action, and we have shared several ideas with Congress that can make a meaningful difference. The first, already enacted, expands the number of small, well-managed institutions that qualify for an 18-month examination cycle versus a 12-month cycle. Following Congress' authorization in 2015, the agencies worked together to quickly implement a rule that allowed 600 more institutions—a total of 4,800—to qualify for less frequent exams. These actions also help regulators focus resources on institutions that present capital, managerial, or other issues of more significant supervisory concern.

Two other ideas that still require congressional action are a community bank exemption from the Volcker Rule and more flexibility for thrifts to expand their business model without changing their governance structure.

Our proposal would exempt some 6,000 banks from the Volcker Rule. Most banks and thrifts with less than $10 billion in assets do not engage in proprietary trading, and we don't believe they should spend limited resources on determining whether they have compliance obligations under the law. It is important, however, to reserve the authority of regulators should the specific circumstances warrant application of the Volcker Rule to individual banks. The Volcker Rule is an important protection against future crises, but it was never intended to cover smaller institutions in the way that it does.

The second proposal we hope Congress will take up would make it easier for thrifts, including mutuals, to expand their business models without changing their governance structures. Over time, markets change and customers' needs evolve. But, if a federal savings association wants to adjust its strategy to increase commercial lending or some types of consumer credit, it's stuck—unless it changes charters. That's expensive and should be unnecessary. The charter should accommodate change. That's something we allowed in Massachusetts, and it makes sense for the federal thrift charter too.

Another way we are working to support community banks is through our responsible innovation initiative.[5] That effort began almost two years ago as the growth in financial technology firms accelerated their delivery of more and more services that used to be available only from traditional banks. This remains a major strategic risk. We saw that to remain relevant banks of all kinds must be able and willing to adapt to the evolving needs of their customers and to use the best innovations available. That's why we set out to make certain that institutions with federal charters have a regulatory framework that is receptive to responsible innovation along with the supervision that supports it.

In October, I announced the agency's framework for responsible innovation and established the OCC's Office of Innovation to be the central point of contact and clearinghouse for requests and information related to innovation. Its staff will conduct outreach and provide technical assistance, and will hold office hours in cities with significant interest in financial innovation to make candid regulatory advice more accessible. The office will promote awareness and training among OCC employees to improve our understanding of these important issues, and lead our collaboration with other regulators, foreign and domestic. We hope to roll out more information about this office soon.

Now let me shift gears and talk about some of the things we have done since the financial crisis of 2008 to make our banking system more resilient. In particular, I want to focus on the value of strong capital, the need for ample liquidity, and the importance of effective supervision.

With regard to capital, the U.S. banking system is as well capitalized as any in the world. The level and quality of capital has improved through the concerted effort of regulators and bankers who recognize that stronger capital means stronger and more competitive banks. U.S.

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[5] See Responsible Innovation on OCC.gov at https://www.occ.gov/topics/bank-operations/innovation/index-innovation.html.

banks have made steady progress building their capital. Common equity is more than double that of the first quarter of 2009.[6] That's a $700 billion increase in common equity capital. At this level, even under the most severe scenario of the Federal Reserve's stress tests, the largest bank holding companies would continue to be well capitalized and capable of lending into a recession. That will reduce the severity and length of a downturn.

But, we are hearing some people question whether capital requirements have gone too far. Critics suggest that capital requirements restrict lending and hold back the economy. While that's a legitimate policy question, the crisis provided the troubling answer of what happens when banks fail to hold capital levels commensurate with their risks. In an economic downturn, undercapitalized banks are simply incapable of lending and restabilizing the economy. I, for one, do not want to repeat our experience of less than 10 years ago, and I hope that others will not forget the benefits of a healthy banking system built on strong capital that can withstand a downturn.

Good memories also will recall the lack of liquidity was as much a factor in 2008 as capital. Since then we have moved in the right direction by implementing the Liquidity Coverage Ratio and proposing the Net Stable Funding Ratio. These two ratios complement each other and push covered banks to hold sufficient ready resources to meet short-term cash outflows and to shift to more stable, longer-term funding. These safeguards make the riskiest behavior more expensive, while minimizing the impact on less risky community banks. We should take care not to undo these safeguards as we consider ways to make regulation less burdensome and to encourage economic expansion.

The last topic I want to cover is perhaps the most important, and that's the value of

[6] See Comprehensive Capital Analysis and Review 2016: Assessment Framework and Results. The Board of Governors of the Federal Reserve System. June 29, 2016 (http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20160629a1.pdf).

supervision by highly trained professional examiners. Seasoned regulators will agree with me when I say that the most powerful means of affecting behavior and promoting a healthy risk culture among financial institutions is good supervision based on clear expectations.

Over the past several years, the OCC has set heightened standards for management and boards of directors of the largest banks we supervise that establish clear expectations for good governance and risk management.[7] These standards grew from observations by examiners who had front-row seats during the crisis and saw what worked and what didn't. We distilled those observations into enforceable standards for our largest banks, and we supervise against them today.

Internally, the OCC started an effort in 2013 to assess how well we supervised large and midsize banks. We asked respected international peers to review our approach.[8] This International Peer Review provided recommendations related to our mission and strategic goals, risk identification and ratings systems, staffing and supervisory strategies, and enterprise governance. You know what the most shocking thing we did was? We published that report, warts and all, for everyone to see and to hold ourselves accountable for improving. And improve we did![9] We created cross-functional teams of employees dedicated to transforming the agency because they recognized that world-class organizations stay that way by seeking feedback, measuring results, and continuously improving.

I am very proud of what our employees were able to do to make us a more effective and efficient regulator. After three years of hard work, we invited the same group of international supervisors to come in and assess our progress.[10] I was pleased that the team saw real

[7] See OCC Bulletin 2014-45. "Heightened Standards for Large Banks; Integration of 12 CFR 30 and 12 CFR 170." September 25, 2014 (https://www.occ.gov/news-issuances/bulletins/2014/bulletin-2014-45.html).
[8] See NR 2013-184, "OCC Releases International Peer Review of OCC Supervision of Large and Midsize Institutions." December 5, 2013 (http://www.occ.gov/news-issuances/news-releases/2013/nr-occ-2013-184.html).
[9] See NR 2014-75, "OCC Announces Actions to Respond to International Peer Review Recommendations." May 28, 2014 (http://www.occ.gov/news-issuances/news-releases/2014/nr-occ-2014-75.html).
[10] See NR 2016-155, "OCC Releases Review of Efforts To Enhance Large Bank Supervision." December 13, 2016 (https://www.occ.gov/news-issuances/news-releases/2016/nr-occ-2016-155.html).

improvements in making our large and midsize bank supervision more effective. While happy with those findings, my agency colleagues and I recognize that we must continue to improve and learn from our successes and lapses.

In the end, the question is whether all of these collective efforts have made the financial system stronger, more resilient, and more capable of meeting customers' needs than it was heading into and during the crisis. We have every indication that the answer to that question is "yes."

We see it on the balance sheets. Tier 1 common equity is nearly 13 percent of risk-weighted assets, up from 9 percent in the fall of 2008. The leverage ratio is now at 9.1 percent, almost one-third higher than in 2008. And, liquid assets have achieved a 30-year high of 16 percent of total assets. America's community banks are stronger too with return on equity nearly recovered to pre-crisis levels, with loans growing steadily.

While encouraged with how far we've come, my job as a regulator is to ask, are we—regulators and bankers—prepared for the next stress event or downturn? I assure you, now is not the time to fundamentally change course. We must remain vigilant about maintaining capital in good times so that it will be there as a bulwark during the next recession. We need to manage the risks of interest rates increasing after this extended period of historic lows. We have to limit concentrations in assets such as commercial real estate that have been sources of problems in the past. Those of you who have witnessed more than one credit cycle know a downturn will come. Effective regulation and supervision will help ensure that the trough will not be so deep or so wide.

I want to conclude by again thanking Howard and Central Connecticut State University for having me here tonight. We need to see more foundations like the American Savings Foundation investing in academic work in banking and finance and providing forums like this one.

Thank you for your attention and I would be happy to answer a few of your questions.