April 26, 2022 Minority Depository Institution Advisory Committee Minutes

The Minority Depository Institution Advisory Committee (MDIAC) convened its virtual meeting at 1:00 Eastern Daylight Time on April 26,2022. The meeting was open to the public, as required under Public Law 92-463.The Office of the Comptroller of the Currency (the OCC), management and staff attended largely from OCC Headquarters in Washington, DC. Committee members, external panelists, public observers and management and staff not in OCC Headquarters attended virtually from around the United States.

Committee Members Present

Natalie Abatemarco, Managing Director, Citi Community Investing and Development, New York, NY
John J. Hou, Chief Executive Officer and President, Asian Pacific National Bank, San Gabriel, CA
Dr. Jody Lee, Chairman of the Board, Southwestern National Bank, Houston, TX
Beverly Meek, First Vice President, CRA Director, Flagstar Bank, FSB, Troy MI
Thomas Ogaard, President and Chief Executive Officer, Native American Bank, National Association, Denver, CO
Joe Quiroga, President, Texas National Bank, Mercedes, TX
Kelly Skalicky, President and Chief Executive Officer, Stearns Bank National Association, St. Cloud, MN
Laurie Vignaud, Director, Unity National Bank of Houston, Houston, TX

Staff from the OCC Present

Michael Hsu, Acting Comptroller of the Currency; Charlotte Bahin, Senior Advisor for Thrift Supervision; David Black, Community Development Expert, Compliance and Community Affairs; Emily Boyes, Counsel, Bank Advisory; Beverly Cole, Deputy Comptroller, Northeastern District and Designated Federal Officer; Greg Coleman, Senior Deputy Comptroller for Large Bank Supervision; Janet Fix, Analyst, Community Affairs; Grovetta Gardineer, Senior Deputy Comptroller for Bank Supervision Policy; Brian James, Deputy Comptroller, Central District; Ernie Knott, National Bank Examiner, Resource & Financial Analysis; Deena Kuko, National Bank Examiner, ADC-Sf/La/Sa; Terence Mack, Associate Deputy Comptroller, Southeast; Sydney Menefee, Senior Deputy Comptroller for Midsize and Community Bank Supervision; Andrew Moss, Director for Minority Outreach; Donna Murphy, Deputy Comptroller for Compliance Risk Policy; Linda Nichols, National Bank Examiner, Midsize and Community Bank Supervision; Valarina Oliver-Dumont, Bank Examiner, Licensing; Erica Onsager, Counsel, Legal; Lauren Oppenheimer, Senior Deputy Comptroller and Chief of Staff; Brittany Shaw, Program Analyst, External Outreach & Minority Affairs; Andrea Shearin, Cra/FI Compliance Policy Specialist; Johnny Stanley, Associate Deputy Comptroller, Northeastern District; Jasmine J. Talton, Counsel; Edward Thomson, National Bank Examiner, Midsize Asset Management; Troy Thornton, Deputy Comptroller, Southern District; Barry Wides, Deputy Comptroller for Community Affairs.

Public Observers

Diana C. Banks, American Bankers Association; Catherine Berman, Founder and Managing Director, CNote; Donald Bowers, Federal Reserve Bank; Tara Campbell, Vice President, CED Lending and Investment Strategies Director, Fifth Third Bank; Joannette Cintron, Old National Bank; Charles Cooper, Department of Financial Services; Robert De Acevedo, CTBC Bank; Ralph DeLeon, Senior Vice President of Industry Engagement, Ncontracts; Seth Dunbar, Federal Reserve Bank; Chris Garcia, Banc of California; Steve Herman, California Bank & Trust; Kelcy Johnson, Senior Vice President, CRA Program Manager, Amegy Bank; Kendra Key, Head of MDI Engagement, Citi; Corrie Maki Knudson, Old National Bank; Clarinda Landeros, Director of Public Policy, National Association for Latino Community Asset Builders; Jennifer Leighton-Guzman, Vice President, Community Development Officer, Texas Capital Bank; Cheryl Mancha, Federal Reserve Bank; Richard Pallay, Jr., Executive Vice President, National Asian American Coalition; C. Earl Peek, CPA, Founder and Managing Partner, Diamond Ventures; Seth Reimer, President, Stanford Road Advisors, LLC; Edythe Repoff, New Omni Bank; Christine Rifkin, Vice President, Fidelity National Title; William Sit, American Plus Bank; Robert Sutton, Compliance, CRA and Fair Lending, American National Bank; Emeka Thompson, Citi; Niko Trumbauer, ESG Analyst, Angel Oak Capital Advisors, LLC; Nadia van de Walle, Wells Fargo, Banking Inclusion Initiative, Consumer and Small Business Banking; Michael Will, Community West Bank; Sharon Zimmerman, Vice President, Community Development Relationship Manager.

Call to Order and Welcome

The event producer (Marvin) provided instructions to the participants on opening the chat panel and stated anyone requiring technical help should send a question to the event producer. Marvin also provided notice that telephone lines were muted until the question-and-answer (Q & A) portion of the call. He instructed participants to send questions through the chat panel until the lines were opened during the Q & A session. The call was then turned over to Beverly Cole, Designated Federal Officer (DFO) for the OCC's Minority Depository Institution's Advisory Committee (MDIAC) and Northeastern District Deputy Comptroller. DFO Cole thanked Marvin for providing instructions to the audience, called the meeting to order and welcomed the attendees.

DFO Cole indicated the meeting would follow the agenda as written included in the handouts. Those in attendance received a meeting invitation from Barbara Jennings that included the agenda, list of attendees, presentations, and the one written public comment received before the meeting. The meeting was turned over to Acting Comptroller Hsu.

MDIAC Roundtable with Acting Comptroller Michael Hsu

Acting CoC Michael Hsu thanked everyone for attending this important meeting. He stated now is an interesting time as there's a lot of different forces at play such as money made available for MDIs because the need is so great. At the same time there's challenges community banks including MDIs face, with the pandemic in the current rate environment. ACoC Hsu indicated an interest in hearing from the committee members. DFO Cole reminded the members OCC management appreciates their candid comments and that they should not disclose confidential, supervisory information in the discussions since the audience was not closed to regulators.

Committee member Natalie Abatemarco highlighted some actions for the committee members' awareness related to the focus on the technical assistance work. She encouraged everyone, not only at this meeting, but at the collaboration meetings coming up, to ensure that we're covering all the topics that need to be addressed beyond just the core working group. She also mentioned the innovation work included a look at what Fintechs are doing and the potential partnerships that are out there like the bridge built by Citi and others, so as not to lose that topic as meetings continue. Lastly she referenced the upcoming July 12th meeting. That meeting is scheduled to not only celebrate Project REACh, but also the work of MDIs, and to capture some of the best practices. It is hoped that more MDIs can participate and that other regional, midsize, and large banks also participate and join us in this work. Ultimately Ms. Abatemarco's question was how do we spread that word beyond the core working groups that we currently have?

ACOC Hsu appreciated Ms. Abatemarco's point on Project REACh. He indicated with the two-year anniversary approaching the MDI revitalization work stream is a critical one. He thought we could target increasing the number of pledges but really talking about why. And there's a lot more than just money. He acknowledged that her participation has been a key part in terms of the technical assistance and that there are other parts which strengthen the relationship, and this is a key to having that sustained improvement in progress.

Committee member Ogaard indicated he represented Native American Bank in Denver which is slated to get ECIP funding. He was curious from the OCC's perspective and particularly as examinations are conducted whether there is concern from OCC about the amount of funding that some banks can get? In Native American Bank's case, they will be able to generate enough to possibly triple the institution's asset size. So, from a regulatory perspective, as OCC looks at banks that are receiving this kind of funding, what are the concerns and how are you communicating that? Mr. Ogaard stated he had a good dialogue with the Western District OCC office but was curious from the broader OCC perspective.

DFO Cole stated that OCC realized ECIP is going to be a game changer for the institutions that receive money and there are going to be significant opportunities for them that perhaps have not existed before. But those opportunities only materialize in a healthy way if there are adequate risk management processes in place, a clear strategic vision, competent management, and staff to execute on that vision. And so those are the things that we expect, just in general, in supervision. OCC expects bankers to use a measured and well-developed strategic plan, that outlines what, how, etc. you are trying to do. Now MDIs have the capital to accomplish those plans and the ability to acquire the expertise not already on your staff or keep the expertise on your staff.

Further, Gary TeKolste in the OCC's Western District developed a presentation that provide information to OCC examiners and management. He presents to various internal OCC examiner and management forums to educate our staff internally on ECIP. The presentation pulls together information regarding the work of the MDIAC, Project Reach, and ECIP. It includes the various aspects of MDI technical assistance, Project REACh work streams, as well as ECIP so that there is a full picture of what this looks like, including the collaboration efforts. OCC does not want the field examiners that have the most contact with the bankers to carry a different message than OCC executive management. If people have questions, then there are several OCC persons that serve as points of contact so we can ensure the appropriate OCC persons respond to any questions.

Deputy Comptroller Troy Thornton added that the deployment of ECIP funds with risk management and safety and soundness in mind we are not going to be concerned. Additional capital is usually a good thing. He further stated strategic planning is key and it would be a good time to lay out concentration limits early in that process. But strong management and good risk management practices to guide those change management factors will be important.

SDC Gardineer stated on a different subject, that there are several efforts that are underway by regulatory agencies and others on addressing the racial equity gap. She wondered what the OCC's efforts are or thoughts on working across the regulatory agencies on this issue, as it relates also to MDIs.

ACOC Hsu responded that there's a number of different efforts and there's not one single, unified effort to address the racial equity gap. And, that different issues require different configurations of cooperation. So, great example would be the work we are doing on Community Reinvestment Act. That's one that's got a huge amount of momentum and work behind it. Complimentary to that is the

PAVE Task Force on appraisal bias. And so that was very explicitly set up by executive order; led by HUD Secretary, Domestic Policy Council, Ambassador Rice, with a total of 14 agencies working on the issue. There is recognition that no one agency alone could address the issue. It took a village of agencies to get together, diagnose the problem, identify action items and all the agencies are committed to taking the individual steps that will add up to something. So right there, that's around housing, we all know home ownership is the key to building wealth and that we've got a racial home ownership gap. Those stats are now well known. It is a focus and we are doing what we can to help on those fronts. OCC has Project REACh and a lot of those projects have other impacts. Credit invisibles, that impacts credit scoring agencies. You're seeing some attention from CFPB and some others. So, there's not a single answer. ACoC Hsu asked if there are other areas where we need to work together? That we need more renewed attention? SDC Gardineer stated that Project REACh is addressing many of the issues that we're seeing and it is also bringing together, not just OCC's opinion, but also the community. So, OCC is engaged in that and looking forward to seeing where it takes us.

ACOC Hsu mentioned that special purpose credit programs have been set up to target closing the racial wealth gap and participants are needed. OCC has provided all the assurances we can to indicate institutions can participate in these programs. So, now institutions and communities can use them – that is another thing we are doing through Project REACh.

Committee member Kelly Skalicky representative of Stearns Bank a $2.4 billion institution stated they participate in five initiatives through Project REACh. And, indicated she is one of the biggest, strongest advocates for Project REACh because it has opened so many opportunities for our communities. Examples included: (1) a co-sponsored project with Stearns Bank and Bank of Whittier – a community dinner for Ramadan of about a hundred people at the Islamic Center in St. Cloud, Minnesota. (2) An initiative with Native American Bank, on the subgroup for technology convened by the OCC. The subgroup is engaged in developing a technology checklist, (3) The Future Bankers Programs – an effort with MDIAC member Jody Lee at Southwestern National Bank, Houston, TX. This effort involves speaking engagements at Texas Southern University's (TSU) Future Bankers Program, a historically black college. President Skalicky indicated that participation in these type projects brings more to the respective communities, than could have done alone before. The goal is to continue to build and make connections and discuss these programs. She stated that because the agency set the table, various stakeholders brainstorm and pull action plans together. She stated an appreciation for the guidance and encouragement from the agencies, and that in a very short time a lot has been learned and her institution is involved in five concrete initiatives. She reported being a stronger advocate of banks participating in the program.

DFO Cole thanked President Skalicky for her comments. And, stated one of the reasons for OCC establishing the MDI Collaboration efforts was to focus on relationships which are longstanding versus transactions. Former Deputy Comptroller Bill Haas (now retired) operationalized the vision that was discussed by the OCC's Mutual Savings Association Advisory Committee and the MDIAC. Charlotte Bahin was one of the authors of OCC MDI Collaboration Paper.

Committee member Jody Lee thanked President Skalicky and Andrew for helping with the TSU Future Bankers Program in Houston, Texas. She reported that Southwestern National Bank committed to more than a hundred thousand dollars in cash for scholarship and internship programs. Southwestern National Bank is partnering with Stearns Bank in the internship program effort. She further stated if it weren't for the MDIAC, she would never have met any of those involved with MDIAC and Project REACh. She thanked Andrew Moss for providing information about opportunities for college students at the OCC and the Treasury Department.

Committee member Natalie Abatemarco indicated the importance for more MDIs to become CDFIs. She also indicated the FDIC's focus on the unbanked is another aspect and critical role MDIs play. She reported in her view MDIs are not acknowledged as much as they should be for meeting the needs of the unbanked. And we know the numbers are tremendous and very large, especially in black and brown communities. Ms. Abatemarco thought it would be helpful to think about this in a continuum and continue to talk with other agencies so we are all singing from the same prayer book. Andrew Moss indicated we have been contacted by the FDIC regarding the work that we're doing in Project REACh. And of course, as you mentioned, FDIC is very focused on the unbanked and how they can get more individuals into the financial mainstream by opening an account, particularly the BankOn Initiative. One of the things that we find with what we're doing in Project REACh that it may be a little bit more sophisticated when it comes to how we are providing financial services, such as small business loans and mortgages. It's an access to capital issue that we're trying to address here. However, a lot of that does start with your basis of becoming a banked consumer. And so, we are trying to marry that up, whereas it graduates into what they're doing with their Alliance for Economic Inclusion at the FDIC, that it marries up into what we're doing with Project REACh. So that once an individual does become banked, they're provided with the financial education, consumer education, and the support to become a home buyer and business owner.

Committee member John Hou from Asian Pacific National Bank in Los Angeles asked two questions regarding the MDI Policy Statement. He wondered if the OCC, FDIC and Federal Reserve would have a consistent definition on MDIs. Questions were around the inclusion of the U.S. subsidiary of a foreign owned bank as an MDI and the size of institutions considered as MDIs. DFO Cole deferred a response to these questions to later in the meeting.

Discussion on MDI Policy Statement

Next Charlotte Bahin led the discussion on the MDI policy. Charlotte thanked John Hou for his questions and stated she would start with some background and some context and then address specific questions. She indicated the questions OCC sent were to spark discussion but were not meant to be all inclusive. Charlotte mentioned the OCC had a working group review the 2013 policy statement on minority depository institutions. It was revised then to address a couple of needs that came up in the post-financial crisis and world. They reflect the market and the world as it existed in 2013. Based on the conversation over the last few minutes, the world has really changed a lot and continues to change. One of the goals of the revisions to the policy statement are to make the policy statement more, not necessarily forward looking, but have it be a policy statement that can stand the test of time, but that is also transparent and understandable for anyone who picks it up so that they can understand exactly what the OCC is thinking about MDIs and the definition of MDIs.

She referenced Section 308 which establishes some goals for the agencies for the minority depository institutions, the OCC included, and the other agencies as well, to have a program that MDIs be created, and be preserved, and be enhanced through a number of means, whether it's through organic growth or through mergers and acquisitions.

There are several ways that the statute requires the agencies to preserve and protect MDIs. As part of the statutory section, there is a definition of a minority. It's not a minority depository institution. It's got a slightly different word, but it includes a definition for MDIs that for privately owned entities, and MDI is one that's 51% owned by one or more socially and economically disadvantaged individuals, for publicly owned, it's the 51% of the stock is owned by one or more socially or economically disadvantaged individuals. For mutual institutions, there's a different test that doesn't address ownership because there aren't any owners of mutuals. In Section 308, there's also a definition of the term minority as any black American, native American, Hispanic American, or Asian American.

For the OCC, and as John has pointed out, the OCC does have a couple of different elements in its policy statement, its current policy statement, the OCC includes women owned national banks and federal savings associations. There's a different test for both mutual and stock in the policy statement. That's one way that the OCC is distinguished from the other agencies. Charlotte asked for additional questions or comments.

Committee member Tom Ogaard shared that as he was reading through information, it struck him that the typical bullet point about mutuals, it wraps around the question definitions number three, where if an MDI no longer meets the ownership test, but the OCC at its discretion can still deem it an MDI. In the third bullet point, if it's okay for mutual institutions, is there any consideration to make it okay for any institution that serves its community where it's board, account holders and community are predominantly minority? It's broader.

Charlotte Bahin explained that the reason that the mutual definition is what it is, with the board members, account holders, and the community, is that's what's in section 308. That's in the statute because they can't have an ownership test, so it's a way that Congress decided that mutuals could satisfy the definition. But your question is a great one. As you may know, or maybe you don't, the FDIC and the Federal Reserve both have alternative tests to the ownership test, which talk about board membership and management membership, and some element of community service as an alternative to the ownership test. It sounds like you would think that would be a good idea. We'd love to hear other people's comments, specifically on that, if you have thoughts on it. Tom, do you have examples, maybe, in your area, or at your bank, where you think that having an alternative test might be useful?

Tom Ogaard commented that he was thinking of those entities with which his institution partners that are located all over the country. Those partnerships may be local to their area in what they do and who they serve. The number of MDIs continues to shrink. Consequently, those banks that may not be under the current definition, but are doing that work, is there an avenue for them to be considered an MDI? The work we do in Indian country, all over the country, including Alaska, there's several partnerships there that they're not MDIs. You wouldn't normally consider them MDIs, but you look at who they serve. You look at who their leadership is. I'm not sure about their board composition, but they clearly have a mission orientation. I just wonder if there's the ability to consider that.

Charlotte Bahin clarified and provided more context that the current policy, the 2013 policy, was revised from the policy that had existed for about 13 years before that, to include this previously designated category for, as you point out that's described in bullet point 3 or that provides the OCC with some discretion to maintain the designation of an MDI that no longer meets the ownership requirements that are established in the statute.

There are a very small handful of national banks and federal savings associations that fall into this category. We refer to it as the previously designated category. It is something that if the ownership test for national banks and for stock federal savings association is no longer met, the 51% or greater that the OCC does in fact look at the community service and other factors, and does to the extent possible continue their designation as an MDI.

Charlotte asked a follow-up question. One of the factors that OCC struggles with is how to identify and how to measure a test that is not ownership based, or control based if it's a mutual entity. For a stock entity that doesn't have the ownership test, how do we identify and measure the appropriate mission focus for an MDI? Does anyone have any thoughts on that?

Laurie Vignaud indicated that usually when an institution applies for CDFI or some other designation, there is data that must be pulled, very similar to what you would do with a CRA examination. She asked if similar data, demographic, and such could also be incorporated into the way in which we would monitor or determine MDI status. She indicated involvement with a group trying to create an MDI that would not be able to meet the FDIC definition, based on our board, our composition, and our mission. Her thoughts were concern that a potential MDI be hindered because it does not meet that specific ownership definition, if it can be documented that management board, and the delivery of access to capital and communities would help them meet those criteria.

Charlotte Bahin clarified that at least for now, at the OCC, the bank does need to meet the ownership test, but after a period of time, the ownership test, because of investments that may be placed in the MDI, or other matters, that the ownership test may not be able to be met, but the OCC does actually retain discretion to permit the MDI so long as it meets these other tests to be designated as an MDI. It's just for at the very beginning, but again, we're really very interested in other ways to designate, define and how to measure an MDI.... Maybe the measure is the mission if that makes sense to think about it.

Charlotte asked “Are there other thoughts of among the committee members? Those of you that have partnerships with other MDIs, have you thought about how they are designated as MDIs, and how the definition works for them?”

Natalie Abatemarco stated that from a big bank perspective reliance is placed on the regulator's definitions and accepting it in that way. Are there other variables or practices that are looked at that support a mission driven organization in terms of lending practices, or banking practices that would conform with what we would consider responsible and fair practices? I don't know if that's a criterion that's looked at all.

Charlotte Bahin responded that at least, right now it’s something that's looked at for the previously designated, just because community services looked at from that perspective. That's broadly how the national bank, or the FSA, supports the community can be thought of in terms of the lending practices and marketing practices who lived in the community, that kind of thing. Those are items that are looked at when the ownership no longer meets the 51% threshold, but I take your point, especially from the CRA perspective. Looking at the agency's list is, I think, probably what's most frequently done.

DFO Cole interjected that when the 2013 policy statement was adopted, the industry was coming out of the financial crisis and several institutions that were MDIs were getting assistance, or capital, from majority institutions. That assistance would dilute the MDI ownership, although nothing changed other than the MDI now had a more stable balance sheet and was a more viable institution. It is a question about whether institutions that have always been MDIs and always operated under that umbrella, if they were simply no longer MDIs because of an investment for them to remain viable. That is the difference between a previously established MDI versus another institution, non-MDI, now saying, "Hey, I'm an MDI."

With the announcement of ECIP, there were lots of institutions that then decided that they were perhaps MDIs. We as regulators, also have a responsibility to make sure that we are being fair across the board in how we view this designation, and how we go about designating it. That's as diplomatically as I can say it.

Charlotte Bahin also mentioned another factor that builds into the process is making sure that, for the MDI, that the requirements, or the look, or the review that the OCC does to ensure on a regular basis that it still meets all the requirements of the definition and the policy statement, making sure that it's not overly burdensome for the bank, or even for anybody that's trying to confirm the information as well. That's something that we are mindful of because, as has already been noted, many MDIs are very small. They may not have the resources to pull together some of the data that's necessary. We're trying to make it not difficult for the MDI to show that they deserve the designation.

Natalie Abatemarco stated that since the OCC has the discretion, it eliminates the concern regarding fairness. The information provided by DFO Cole makes sense. It also makes it clearer, why that discretion is included in the policy statement. And, I don't see a strong need to change it.

Charlotte Bahin reaffirmed that Ms. Abatemarco did not see a strong need to change the ownership standard, so long as the OCC retains the discretion to continue a designation if the ownership test is no longer met. Charlotte asked if there were other characteristics, alternative tests, OCC should consider. She raised the prior comments on whether
MDIs should look at CDFI certification on a continuum of what they're doing and serving their community? And asked if that is a place where OCC should be looking for a discussion of mission, or are there other factors members wanted to share? The committee members discussed pros and cons of CDFI designation as a criteria. CDFI designation a pro as the institution would have to demonstrate that they are serving LMI and vulnerable populations. Also board and ownership, and constituents, and the geography, and then the demonstration, I guess, of the cultural competency of that institution, to me makes sense. Knowing that OCC has discretion, gave members pause that there is an opportunity to bring somebody in that's not exactly in the mold. Others shared that ownership and board are the key to the kind of company or organization one is. There was interest in giving freedom to MDIs to be formed and grow to be any kind of bank they want to be. Charlotte indicated the members' comments were focusing on what OCC had in the CDFI certification called the accountability test, meaning that you had either representation of the community in your governance, or you had structured an advisory board that would provide you with a information or a vehicle for assessing community needs, regarding the access to capital and credit. So those are good to take into consideration. I know that we have a different focus here when it comes to the FIRREA 308 definition. And so, it can make it more challenging for us to look at how the framing or the boxing of the designation for MDI is, compared to CDFI certification, but good points to take into consideration of how we might be able to review that under beneficiary view of the agency.
In response to a question it was reported that an institution's MDI designation is typically reviewed during the course of individual bank examinations. However, given the increased focus and activity in this space, OCC is considering reviewing the MDI designations on a centralized basis at least annually. Also, over time ownership structures have become more complex and require more specialized analysis. OCC wants to ensure consistency in our application of the designation.

Charlotte Bahin then turned to addressing John Hou's prior questions. He reported he likes the OCC definition except for OCC's exclusion of subsidiaries of foreign-owned banks. Charlotte reported the OCC had a prior policy statement for MDIs that was published in 2001. And it also includes this exclusion for subsidiaries of foreign-owned banks. We don't know why we do, and the other agencies don't, but it's certainly something that we can think about. And I'm not aware just off the top of my

head, without looking at the list, looking at the FDIC's list or the Federal Reserve's list to see whether there are foreign-owned banks, or subsidiaries of foreign-owned banks that are included as MDIs on those lists.
John Hou: Yes. The second question is I look at the list, and that has several banks. They are like a very large MDI. They have a total asset over 50 billion. I think two own 50 billion, and five banks have over 20 billion. So, I don't know how you compare, how you try to compare them with the much smaller NDIs, that's my quick question.

Mr. Hou's second question focused on the size of the institutions. Another member stated that there is a dual component to the definition, first, MDI is one and then the need to ensure the institution continues to target the community and they community that they represent. Charlotte stated that the definition is the key to the policy and how it works, and how the OCC looks at designating MDIs. But there are several other items in the policy, including a paragraph about the de novo in providing information for de novo MDI, or groups that wish to form de novo MDIs, and descriptions of some of the recent initiatives, including Project REACh and the collaboration initiative. Charlotte encouraged anyone with additional comments to share them now or later.

Committee Member Joe Quiroga stated a discount in assessment fees for MDIs would be another way to assist MDIs. DFO Cole stated that discussion is better suited for the Acting Comptroller and OCC's Executive Committee.

State of MDIs

DFO Cole asked Marvin to open the phone lines so public observers as well as committee members could address questions to DFA Ernie Knott as he reviewed his financial analysis on the state of MDIs. The meeting was turned over to Ernie Knott for the State of MDIs presentation. The presentation is attached as a handout. And the analysis is captured in the minutes so the reader does not have to analyze each slide independently.

Slide 2 is the agenda. Portfolio demographics, charter trends, assets, and the MDI Group location will be discussed. Next supervisory information was covered. That mainly is information gathered from examinations, such as ratings, risk assessments, examination cycles, Matters Requiring Attention (MRAs), and violations of law. Lastly, financial information from the Reports of Condition and Reports of Income (Call Reports) is addressed.

Ernie reported that the OCC regulates, a diverse group of 1,177 charters. Now, these first four columns are what we call the bank charters, and there's 1,059 bank charters that we regulate. Slide 4 reflects charters by MDIs and non-MDIs. The 53 MDIs represent 5% of OCC bank charters as of year-end 2021. And, is a big change from 2013, where MDIs only represented 3%. And on the bottom of the slide, the MDIs represent now 33 billion, or 3.5% of community bank assets. The chart does not include trust, midsize, or large banks since no MDIs are from those groups.

Slide 5 reflects the trend in MDI charters by MDI group. Now the net number of MDIs remained stable, you could see it was 54 in '13, and it's 53 now. But there was a gain as a share of OCC charters because the number of MDIs remain relatively stable, the total population of banks have declined. And this is the banking industry, both state and national banks have declined by 50% since 2001. And you can layer on there the other factor is a lack of de novo charters now in terms of the volume versus pre- Dodd-Frank.

The last column shows 18 women MDIs, and that's plus five from last year. Native American, are plus one – a new MDI in Oklahoma. Hispanic, no change. Asian, there's a plus one. There's a new MDI designation in Arizona, and there is no change in the African American population. But Broadway merged with City First, so now instead of Broadway it is City First.

Slide 6 shows the MDIs by state. The 53 MDIs are in 23 states as of year-end 2021. And they're concentrated in Texas and California. Three other states, Georgia, New York, and Oklahoma, have four each in those states.

Slide 7 documents Ernie's thought process in devising a MDI community bank peer group. The first bullet, the smallest MDI is 29 million, and the largest is 5.6 billion. The asset size for the peer group was kept within those parameters. MDIs fall into two institution type categories, national banks and stock FSAs. Since there's no mutuals right now, or trust companies, these type institutions were excluded them from the population. And bullet three, excluded the midsize and large banks. As such, the MDI peer group referenced throughout the presentation is community banks between the 29.4 million and 5.6 billion. And there are a few stats on MDIs supervised by other regulators.

Slide 8 reflects some slippage in the composite ratings over the last year. Not much. 79% of MDIs have a composite rating of one or two. There is no MDI rated five. There is no MDI rated worse than three for any specialty area, and that's very good news.

The top of Slide 9 addresses management ratings which are fair and improving. You can see now, we went from 23%, three, four, and five rated institutions down to 21. The bottom, looking at the exam cycle, shows that 75% of MDIs are on the 18-month exam cycle. And to be eligible, an institution must be less than three billion in size and must be one or two rated for the composite and management ratings, be well-capitalized, and not be under a formal action. And lastly, a change in control must not have happened in the previous 12-month period.

Slide 10 is showing the rating changes. This is the pipeline into the distribution for the next quarter, and it's really a leading indicator. Over the last year, we had a net upgrade of 14. Most downgrades were for asset quality, but most upgrades were for earnings. And management was balanced, going in and out, ups and downs. On the bottom, the top three risks for MDIs are credit, strategic, and operational. And credit, because we're transitioning out of the pandemic era, and still some banks were impacted even though past dues are low. Second strategic risk, about managing through the net interest margin period; will probably be there for a while because we're operating in a complex environment and the increasing cybersecurity threats right now

Slide 11 is information from examinations. On top the volume of MRAs is down 36% in 2021. Now, MRAs increased the most for commercial credit, and that's not unusual for any population, but they decreased the most for BSA AML. And you can see that there, the blue line down to the red line of 12%. Looks like about down in half. On the bottom, violations of law are also down over the last year, 32%. They're concentrated in consumer, but the top two violations of law are the availability of funds and collection of checks act, and loans in areas having special flood hazards. This is same for the community bank population

Slide 12 starts the financial analysis slides, with capital. This slide shows some of the changes from the CARES Act. It provided temporary relief and gradual phase in of the CBLR framework, and this was due to the pandemic. The framework was completely phased in as of March 31, 2022

Slide 13 shows MDIs are well-capitalized; ratings are stable this year. 86% of MDIs are rated one or two, with more one rated capital here for MDIs. If the bank is not a CBLR bank, to be well capitalized the traditional threshold of 5% for leverage, 8% for tier one capital, 10% for total, and 0.5% for common equity tier one. Some of the banks that are less than well-capitalized because they're under a formal action requiring a higher minimum. If you look at those ratios, they're all above the thresholds previously mentioned.

Let's look at the two key capital ratios. MDIs have higher leverage capital than all the populations right now, the peer group for the community bank and other MDIs. Now, it would be much higher if not for the PPP loans, they lower capital ratios by creating a larger denominator. But after adjusting for that, that 11% leverage would be up 34 basis points if we do neutralize the impact of PPP loans. Also, looking on the bottom part, that's the total capital. This also is down a bit, but that's due to a one-time impact when banks transitioned in 2019 to 2020 to the CBLR rule. Banks have opted in, which had much higher levels of capital, reduce the population. That change would've occurred at any point in time when the CBLR was introduced.

Next topic is earnings. The number of MDIs rated one or two rose to 78%, but they lag ratings in other areas, and this is currently common for all community banks. The bottom of the slide reflects an increase in ROE of 355 basis points for the MDIs, but you see it lags other peer groups because MDIs have such higher levels of capital. Slide 16 shows MDI ROA increased 18 basis points to 0.94%, and it's in line.

Slide 17 at the top reflects that despite margin compression, net income rose sharply in '21, and this is due to higher net interest income, strong growth in fee income, and lower provision expenses. And you can see there you have 20% growth in fee income and net interest income, and a drop in provision expense.

Most banks reserved heavily during the pandemic and will release reserves the same way you increased them when there was a concern in the early days of COVID. The bottom chart is just looking at the graphing, the components. There's a tight labor market and so the personnel related expenses may increase in 2022 as the market for talent is very competitive

It will be important to keep investing in IT, not just for cyber security, but for customer interface applications as well.

In response to a question Ernie stated that although he adjusted the leverage ratio for PPP impact, that was not done for the net income piece. It could be done. During this period net interest margins also benefited when you had accelerated recognition as well during those periods. The Call Reports gave banks an option to deduct PPP loans if they were pledged to the liquidity facility. Ernie did not do that analysis but given being familiar with the numbers, he thought it is not more than a 10 basis point impact, and might change the growth from 20% to 15%.

A committee member stated that the industry has be discussing if the trajectory was lower margins overall, and PPP helped mass some of that in 2020 and 2021 but it was a substantial amount of money. And, had a bigger impact to the overall bottom line, therefore, stressing the need that margins are still getting thinner. Ernie commented that 2021 was the lowest on record. And in terms of some fee income also, there were a lot of sales on loans that will probably not be seen in 2022 because of the environment we're in. Ernie further commented that most if not all community banks rely heavily on a net interest margin, 83% of the income comes from there

OCC also sees that during periods of net interest margin compression there is more industry consolidation, especially for the banks with the most compression. But one thing, no matter what size bank you're in, midsize, large, or community, there's also more cost cutting going as well during these periods. The takeaway is to focus on what can be done in growing income sources and volumes in a safe and sound manner. The bottom of the slide shows 11% decline since year end 2020, but declined less for MDIs than other community banks. So, MDIs as a group, were able to protect your margins better than the average community bank during this period.

Slide #19 was added to show what happened to the net interest margin during this period. Now, again, we're looking at we're merging all the banks again. The absolute volume of net interest income never decreased during the pandemic here, and that's the blue columns. And the number in parentheses, this is the average earning assets. To get margin, of course, you divide your net interest income divided by average earning assets. But when you do that, the margin narrowed about 13 basis points on a weighted average basis. And that's because this denominator grew 7.5 billion, or 34%. Which was a lot more than the numerator, grew 29%, and that caused the compression. But also, you're looking at the balance sheet impact, I added this as well. If you look at 2019 here, looking at the blue and the green right now, you had 81% in securities and loans, and now that's down to 76%.

And during this period, as well, 13% in interest bearing bank balances, now it's 18%. And I just use a quick example. The interest-bearing bank balances were only earning 0.35%. A couple years ago you had 13% earning that low amount, and now you have a larger portion earning that lower amount as well. Hopefully loan growth will be returning in 2022, and you will be able to deploy that money. Two things are happening (1) a rate issue, and (2) a balance sheet impact on the margin.

Slide 20 shows asset quality ratings are satisfactory and stable, 85% are rated one or two. There's no MDI rated five. And the past due loans in OREO fell to a decade low 1.93%. Again, very good news here, low, and declining. But there are modification programs related to the CARES Act that could be masking delinquencies, but that pool of loans is declining. They're down about 90% since second quarter of 2020. There might be an increase but currently this is probably the lowest levels seen in awhile.

Slide 21 on the top, we're looking at the classified assets number. These are numbers reported by bankers quarterly. These numbers have increased over the last couple years. And you can see the allowances also increased as well with a small increase in classified. And we would say that's directionally consistent.

Slide 22 – it was surprising to see that for mutuals, stock FSAs, and a lot of community banks, that many banks had negative or no growth during this period. But if you look on the top, on slide 22 right now, after adjusting for the PPP loans, you had a loan growth of about 7%. That's very good. And on the bottom, we're just unbundling that number based on size. And you can see MDIs over one billion had a double-digit loan grow. You maintain your relationships during this period, and you can see this peer group, your average community bank during that period. Normally, the banks under 100 million either are low single digits are sometimes negative.

Slide 23 on the top, using large buckets you see loan mix for the MDIs is concentrated in CRE loans. Loan balances only decreased for commercial loans, and that's because PPP loans fall into that category. On the bottom, excellent news, your losses are at an all-time low of 0.05%. And most loss is M&A, a very low number. But again, 0.05, that's much lower than the average community bank in 2021.

Slide 24 addresses liquidity. Liquidity rates remain strong and improving. 98% are rated one or two. MDIs are flush with liquidity now. Deposits grew. They grew maybe 15 to 20% for the average bank. But for MDIs, they grew about 26% year over year. And a lot of this is pandemic related deposits, I call them your stimulus checks, PPP funds, enhanced unemployment benefits that ran out in September. But there's also a higher consumer savings rate, which is normal during periods of uncertainty. In the beginning, not many folks realized how long the pandemic would last and how severe it would be. Now that savings rate has been coming down. Looking at the latest number from the Bureau of Economic Analysis, was 6.3% in February, and that was down from 13% the prior year.

Some folks think that these deposits will continue to run off and others think they will stabilize. There is excess liquidity now, and it is clearly reflected on the bottom of the slide there. And, a larger share in in the non-interest bearing deposits, which is good.

Slide 25 in looking at the ratios, they were literally on-hand liquidity was off the charts. But the ratios are both higher than pre-crisis and pre-pandemic. Now the smallest banks have the highest levels of on-hand on balance sheet liquidity. This is seen on the bottom part of the slide. The sharp rise in deposits resulted in less reliance on wholesale funding sources.

Slide 26 looks at sensitivity. It is adequately controlled, 92% are rated one or two. And non-maturity deposits on the bottom are up. They're down from last year, and that's the denominator effect, but strong growth in non-maturity deposits is reflected. But they are off their lows of 2013. And this is good news, because they reprice not as frequently and make the banks less vulnerable to raises in rates.

Next, Ernie provided a one-page high level economics update. Looking at employment, we had 431,000 jobs added in March. Unemployment is down to 3.6%. Labor market is at or near the Fed's full employment goal. And for the first time in years, we're focusing on inflation. The Fed will control inflation through a series of rate hikes as evidenced by the 25 basis points increase in their mid-March meeting. The consensus is the next two are going to be increases of 50 basis points.

The Ukraine war placed upward pressure on a lot of commodity prices, oil, metal, and agricultural commodities. The PCE price index, reportedly the Fed's preferred gauge, is at 5.4%, but it's the highest it has been in 40 years. Since the consumer makes up 70% of the economy, the retail sales report is an indicator of consumer sentiment. Retail sales did not make estimates last month, but they were good. Even though there's inflation, the consumers are spending. And the Michigan survey which focuses on current expectations of consumers and future was unexpectedly up in April.

The 10-year treasury, is a vital economic benchmark because it is tied to the 30-year mortgage rate. It is showing the steepest increase and making housing less affordable. Housing prices are increasing, and inventory is tight so there is a layering on and an affordability issue through the rise in this rate. Renting is expensive as well.

Ernie expressed appreciation to work with this group. To add value to the committee Ernie provided a demo of a board package prototype that the bankers might find useful. OCC supervised bankers can email Ernie to obtain the board package specific to their institution. Questions were asked to clarify specific numbers regarding composition of upgrades in the areas of asset quality and BSA/AML. The asset quality slide reflects that most of the rating changes were upgrades. In most instances upgrades were an indication that prior concerns were satisfactorily addressed.

Announcements

Nomination Process for MDIAC Membership
Next Charlotte Bahin noted OCC is in the process of renewing our MDIAC charter with Treasury which happens every two years. Again, we've submitted the preliminary materials to Treasury and gotten some feedback from them. And the next step is to send over a revised charter and membership balance plan to Treasury for their signature and filing with the appropriate committees of congress.

One of the factors about going through this process and starting it in this way is that we have from the very earliest days the support of the highest levels of this agency for this committee, which the acting comptroller reiterated in his comments earlier. But it's great news that the acting comptroller and his team support the continuation of this committee and its membership. So, once we get the charter renewed, then we'll start the solicitation for members. The committee per its charter can have up to 10 members. A notice will be published in the *Federal Register*, a press release sent, to let everybody know that we can that we're looking for members. So, if you have suggestions of people, MDIs, CEOs or senior management or directors, who you think would be good on the committee, please let us know when you see the notice.

There's no application process. It's just sending in the information to the email address that'll be published in the Federal Register and in the press release, and submitting, and then follow up with some biographical information, if that's necessary. Every person who nominates themselves, is nominated and makes it through the path to be one of the nominees that is submitted to Treasury must go through the FBI and IRS checks every time. So, if you did it last time, the bad news is that you must do it again, but at least you know what to expect. That process can take as long as two to six months, depending on what else is going on with Treasury, with the IRS, with the agencies, generally.

Once that's all done, then we send a couple of other memos to Treasury for their approval. And hopefully we'll be able to get the membership established early next year. We start the process early since the process has many steps and can be time consuming. So, please think about whether you want to nominate yourself or be nominated to serve again or whether you want to nominate other people. That'll be something that'll be coming up in the late spring or early summer

Future MDIAC Meeting Date
DFO Cole announced that the next MDIAC meeting is going to be Tuesday, September 27, 2022 and held in-person for members. The membership has the option for virtual or in-person.

Public Comments

DFO Cole shared that one public comment was received from the Ludwig Institute for Shared Economic Prosperity. The comment was included in the handouts for the meeting. There were no other public comments.

Closing Remarks

SDC Menefee made comments regarding the recent OCC MCBS Realignment. She stated the realignment is intended to position MCBS for the future. She stated the most important point to understand with the realignment is that our supervision remains local and there are no changes in the supervisory office or the supervisory approach for most of our community banks.

So first, we're going to be moving away from a district concept and we'll be moving away from that concept to more of a regional approach where we have six regions with associate deputy comptrollers. This is a leadership position that we currently have. And we'll be leaning on these leaders much more for interactions with regulated institutions. The Deputy Comptroller position and Assistant Deputy Comptroller positions remain. Bankers may see the Associate Deputy Comptrollers more actively engaged in outreach than they have been in the past. OCC will centralize some of the supervisory support functions, particularly our lead experts, risk officers, and some of our subject matter experts. Additionally, administrative tasks such as scheduling examinations and staff. With more centralized scheduling for these subject matter experts, we'll be able to ensure that we're sending the right people to the right place. And that's consistent with our philosophy of risk-based supervision. The experts will be organized by risk stripe versus geography. OCC sees some benefits and efficiencies with pooling like skill sets, like risk stripes together.

<u>Adjournment</u>

DFO Cole adjourned the meeting.

/s/ Beverly F. Cole