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TESTIMONY OF

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COMPTROLLER OF THE CURRENCY

before the

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

UNITED STATES SENATE

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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 represent the views of the President.

I. Introduction

Chairman Crapo, Ranking Member Brown, and members of the Committee, thank you for the invitation to appear before you today to discuss the Economic Growth, Regulatory Relief, and Consumer Protection Act (Economic Growth Act or Act). I am honored to join my colleagues from the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), and the National Credit Union Administration (NCUA).

The Economic Growth Act is a testament to the bipartisan work of this Committee, under the leadership of Chairman Crapo, to provide prudent burden relief for the small and mid-size financial institutions that need it most. The Office of the Comptroller of the Currency (OCC) recognizes the importance of this effort and is committed to implementing the Act quickly so that the national banks and federal savings associations (banks) we supervise can continue to create jobs and promote economic opportunity in a safe, sound, and fair manner. The work needed to write the implementing regulations called for by the statute is well underway. In the meantime, the OCC has joined the Board and the FDIC (collectively, the agencies) to clarify our intention to regulate and supervise financial institutions consistent with the outcomes that the Act requires.

Before I turn to the specific progress the OCC has made to implement the Economic Growth Act, I would like to describe briefly the current condition of the federal banking system. The OCC has supervisory responsibility for over 1,300 banks. Together, these banks hold $11.8 trillion in assets—roughly 67 percent of the commercial banking system. They service 33 percent of the country’s first-lien residential mortgages and issue 66 percent of all credit card balances. The vast majority of these 1,300 banks are smaller banks, with less than $10 billion in assets. These numbers show the important role that OCC-supervised institutions have in the nation’s economy and how essential it is for these banks, especially community and mid-size banks, to operate efficiently and effectively and to offer the products and services that their customers and communities need.

The OCC works to promote a vibrant and diverse banking system that benefits consumers, communities, businesses, and the economy. We ensure that banks operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations. The dedication and commitment of the OCC, and that of the other agencies, have contributed to the strength and resiliency of the U.S. banking system. The overall capital position and the credit quality at large and small banks have strengthened considerably in recent years, as has liquidity and profitability. This environment has contributed to banks' abilities to develop innovative approaches to delivering their products and services. I am optimistic about the direction of the country's economy, in no small part because of the regulators' work to support and enable a strong and resilient banking system.

I am well aware, however, that with opportunity comes risk. The OCC regulates banks to ensure that their boards of directors and management clearly understand and actively manage the risks they face. We are closely monitoring trends with respect to credit, interest rate, operational, and compliance risks, and we continue to share our insights and concerns with the banks we supervise. In addition, the OCC assesses new and emerging threats, including those related to cybersecurity. I believe that these efforts have made and will continue to make banks safer and stronger.

II. The Economic Growth Act

The strength and vitality of the nation's financial system depend, in large part, on the ability of financial institutions, particularly community and mid-size banks, to operate efficiently, effectively, and without unnecessary regulatory burden. The Economic Growth Act is a bipartisan, common sense law that will significantly reduce regulatory burden for small and mid-size institutions while safeguarding the financial system and protecting consumers. The Act includes several features that will benefit community banks in particular and are consistent with my priorities as Comptroller, including reducing the number of banks subject to the Volcker Rule and providing a simpler capital regime for highly capitalized community banks. These and other provisions in the Act will help the federal banking system continue to foster job creation and promote economic opportunity. Today, I will outline the steps the OCC has taken to ensure that the relief provided by the Economic Growth Act is realized as quickly as possible.

A. Interagency Statement Regarding the Impact of the Economic Growth, Regulatory Relief, and Consumer Protection Act[1]

Following passage of the Economic Growth Act and in response to questions from various stakeholders, the agencies issued an Interagency Statement to financial institutions to clarify how we would administer certain provisions of the Act. For example, a number of provisions of the Act were effective upon enactment or soon thereafter, but agency regulations had yet to be revised to reflect these changes in the law. In order to avoid confusion and the unnecessary use of institutions' compliance resources, the agencies issued the Interagency Statement to demonstrate our commitment to administering our regulations, during the interim period before we promulgate any necessary conforming regulations, in a manner consistent with the Act.

The Interagency Statement provides direction and sets the table for upcoming regulatory revisions in a number of areas. For example, the Economic Growth Act at section 401 raises the

[1] Joint Release, OCC NR 2018-69, *Agencies Issue Statement Regarding the Impact of the Economic Growth, Regulatory Relief, and Consumer Protection Act*, July 6, 2018 (Interagency Statement).

threshold at which bank holding companies (BHCs) and depository institutions are required to perform company-run stress tests from $10 billion to $250 billion. This change was effective immediately for BHCs with less than $100 billion in total consolidated assets but not for similarly-sized depository institutions. In order to provide parity and avoid unnecessary burden, the Interagency Statement explains that the agencies will not require depository institutions with less than $100 billion in total consolidated assets to perform company-run stress tests during this interim period.

In addition, sections 203 and 204 of the Economic Growth Act make changes to the statutory provisions underlying the Volcker Rule, including reducing the number of institutions subject to its requirements. These changes provide regulatory relief to institutions that do not pose the types of risks the Volcker Rule was intended to limit. To address conflicts between the agencies' current Volcker Rule and these statutory changes, the Interagency Statement explains that the agencies will not enforce the Volcker Rule in a manner inconsistent with the Act.

B. Recently Completed Actions

I am happy to report that we have made steady and significant progress implementing the Act since the agencies issued the Interagency Statement in early July. As discussed below, we have completed several actions and are engaged with our fellow regulators to move quickly on the remaining rulemakings.

Thrift charter flexibility. On September 10, 2018, the OCC issued a notice of proposed rulemaking (NPR) to provide greater flexibility to federal savings associations by implementing a new section of the Home Owners' Loan Act added by section 206 of the Economic Growth Act.[2] This proposal would establish streamlined standards and procedures under which a federal

[2] OCC NR 2018-95, *Office of the Comptroller of the Currency Invites Comment on Proposed Rule to Enhance Business Flexibility for Federal Savings Associations*; 83 Fed. Reg. 47101 (Sept. 18, 2018).

savings association with total consolidated assets of $20 billion or less can elect to operate as a "covered savings association." A covered savings association would have the same rights and privileges and be subject to the same duties and restrictions as a similarly located national bank but would retain its charter and existing governance framework.

The Act, together with the OCC's rulemaking, will provide federal savings associations with additional flexibility to adapt to evolving economic conditions and business environments and allow them to better serve the changing needs of their customers—without the burden and expense of changing charters. The public comment period on the NPR is open until November 19, 2018.

HVCRE. Section 214 of the Economic Growth Act provides that the agencies can require an institution to assign a heightened risk weight to a high volatility commercial real estate (HVCRE) exposure only if it meets the Act's new definition of an HVCRE acquisition, development, and construction loan. To address conflicts among this provision, existing rules, and relevant Consolidated Reports of Condition and Income (Call Report) instructions, the Interagency Statement provides that institutions can choose either to rely on the Act's definition when risk-weighting and reporting HVCRE exposures or to continue to risk-weight and report HVCRE exposures consistent with current Call Report instructions. On September 18, 2018, the agencies jointly issued an NPR to implement the statutory definition.[3] The public comment period is open until November 27, 2018.

Examination cycle. On August 23, 2018, the agencies jointly issued interim final rules implementing changes to their examination cycles.[4] Section 210 of the Act increases the asset

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[3] Joint Release, OCC NR 2018-100, *Agencies Propose Rule Regarding the Treatment of High Volatility Commercial Real Estate*; 83 Fed. Reg. 48990 (Sept. 28, 2018).

[4] Joint Release, OCC NR 2018-82, *Agencies Issue Interim Final Rules Expanding Examination Cycles for Qualifying Small Banks and U.S. Branches and Agencies of Foreign Banks*; 83 Fed. Reg. 43961 (Aug. 29, 2018).

threshold for certain well managed and well capitalized insured depository institutions that are eligible for an 18-month examination cycle from institutions under $1 billion in total assets to institutions under $3 billion. Under the interim final rules, the extended examination cycle is now available to a larger number of qualifying 1- and 2-rated institutions. This change, together with parallel changes to the on-site examination cycle for U.S. branches and agencies of foreign banks, will allow the agencies to better focus their supervisory resources on financial institutions that present capital, managerial, or other supervisory issues and thus enhance safety and soundness collectively for all financial institutions. The public comment period is open until October 29, 2018.

High quality liquid assets (HQLA). Section 403 of the Economic Growth Act directs the agencies to treat certain municipal obligations as HQLA for purposes of their regulations, including the liquidity coverage ratio (LCR). It further directs the agencies to amend their liquidity regulations to implement these changes within 90 days of enactment.

In anticipation of this rulemaking, the agencies announced in the Interagency Statement that they will not require an institution subject to the liquidity regulations to exclude from the definition of HQLA those municipal obligations they believe meet the statutory criteria for inclusion in HQLA. Subsequently, on August 22, 2018, the agencies jointly issued interim final rules to implement this statutory provision, under which covered institutions will have additional flexibility in meeting the LCR requirements.[5] The public comment period on this rulemaking is open until October 1, 2018.

[5] Joint Release, OCC NR 2018-81, *Agencies Issue Interim Final Rule Regarding the Treatment of Certain Municipal Securities as High-Quality Liquid Assets*; 83 Fed. Reg. 44451 (Aug. 31, 2018).

C. Additional Actions Underway to Implement the Economic Growth Act

The agencies, working both jointly and independently, continue to move forward with the remaining steps to fully implement the Economic Growth Act. The OCC is participating actively in interagency consultations related to the rulemakings and other efforts underway by the Bureau of Consumer Financial Protection (BCFP) to implement the Act's changes to federal consumer financial protection laws. We are reviewing several other provisions of the Economic Growth Act to determine whether further action is necessary. We are also participating in interagency discussions on a rulemaking to implement the exemption in section 103 from the appraisal requirements for certain rural real estate transactions. As described below, we are also working diligently to address changes to the regulatory capital regime and the preparation of Call Reports. I expect that we will take action on all remaining rulemakings by the end of the year.

Community bank leverage ratio. The agencies are working to implement section 201 of the Act, which addresses the complex and burdensome process—particularly for highly capitalized community and mid-size institutions—of calculating and reporting regulatory capital. In addition to providing much needed clarity regarding the capital treatment of HVCRE exposures (discussed above), the Act directs the agencies to draft regulations that allow certain institutions—those that exceed a "community bank leverage ratio" (tangible equity to average total consolidated assets of 8 percent to 10 percent) and engage only in traditional banking activities—to be deemed in compliance with current leverage and risk-based capital provisions.

Staffs of the agencies are meeting frequently to develop rules to implement this provision, which represents an important new direction in capital regulation. A number of complex issues remain outstanding, including how to harmonize this provision of the Act with statutory provisions unaffected by the Act, and the agencies are working to resolve these issues. I am confident that a thoughtful implementation of this provision will lead to a substantial reduction in regulatory burden for highly capitalized, qualifying institutions while ensuring that these institutions continue to maintain appropriate capital levels.

Asset threshold for short form Call Report. Section 205 of the Act provides for reduced reporting requirements on Call Reports for the first and third quarters for institutions with less than $5 billion in total consolidated assets. This change expands the number of community institutions that can benefit from the reduced burden associated with the short form Call Report, freeing up employees and other resources to serve customers and the operational needs of the institutions. The agencies are meeting regularly to discuss a framework to implement this change.

Periodic stress testing. In addition to the changes to the company-run stress testing thresholds discussed above, section 401 of the Act amends the required frequency of stress testing from annual to periodic and reduces the required number of scenarios from three to two. These agencies are working to implement all of these changes, which will reduce burden while maintaining this important supervisory tool. Stress testing serves a critical function for both regulators and financial institutions by ensuring that financial institutions consider potential economic events that could cause significant balance sheet disruptions and prepare to mitigate such disruptions if necessary.

Supplementary leverage ratio. Section 402 of the Act directs the agencies to revise the leverage ratio requirements applicable to the largest U.S. banking organizations engaged in custody, safekeeping, and asset servicing activities. The agencies are determining how best to implement these changes, particularly in the context of other, proposed changes to the leverage ratio calculations.

D. Additional Efforts to Promote Economic Growth and Job Creation

In parallel with our efforts to implement the Act, the OCC is considering additional ways that we can reduce unnecessary burden on the banks we supervise, an endeavor that we believe is consistent with the purpose of the Act and will fuel job creation and economic opportunity.

Additional capital framework changes. The OCC is meeting with the Board and the FDIC to consider other options for reducing the compliance burden associated with the capital framework, including the changes described in the October 27, 2017 joint NPR.[6] The NPR was issued in response to the agencies' commitment to Congress pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996 to meaningfully reduce regulatory burden.[7] The proposed changes include allowing smaller, non-complex institutions to apply a simplified regulatory capital treatment to mortgage servicing assets, certain deferred tax assets, investments in the capital of unconsolidated financial institutions, and certain minority interests held by third parties. These changes would allow these institutions to more efficiently and effectively serve their customers.

Recovery planning. On September 19, 2018, the OCC issued an NPR to increase the threshold for the agency's enforceable guidelines establishing standards for recovery planning, which currently require a bank with average total consolidated assets of $50 billion or more to prepare a recovery plan.[8] The proposal would raise the threshold for banks subject to the guidelines to $250 billion or more, providing regulatory relief to the mid-size banks currently covered by the guidelines. The public comment period is open until November 5, 2018.

[6] 82 Fed. Reg. 49984.

[7] Federal Financial Institutions Examination Council, Joint Report to Congress: Economic Growth and Regulatory Paperwork Reduction Act (March 2017).

[8] 83 Fed. Reg. 47313.

III. Other Agency Priorities

I would also like to take this opportunity to update the Committee on some of the other important work taking place at the OCC.

Community Reinvestment Act of 1977 (CRA). While the communities that banks serve will benefit greatly from the economic opportunities that the Act makes possible, such progress does not always require congressional action. One area in which the agencies can achieve additional reforms on their own is the modernization of the CRA regulatory framework. I have seen firsthand how CRA activities reinvigorate financially distressed areas through community development and reinvestment, but stakeholders from all perspectives acknowledge the limitations of the current framework. Despite the best of intentions, the CRA regulatory framework, which has been pieced together over the past 40-plus years, is outdated, ambiguous, overly complex, and unnecessarily burdensome. These problems hinder banks' ability to fulfill the statute's goals.

To continue the burden reduction and economic empowerment that Congress made possible with the Act and to address concerns about the CRA framework, on August 28, 2018, the OCC issued an Advance Notice of Proposed Rulemaking (ANPR) to solicit ideas to modernize the implementation of the CRA.[9] A modernized framework would strengthen the CRA by encouraging more lending, investment, and activity where it is needed most—fulfilling the ultimate purpose of the CRA. We can achieve these goals by providing greater clarity regarding CRA-qualifying activities; establishing clear and objective measures to assess CRA performance; rethinking the concept of the "communities" that banks serve in a more comprehensive manner; facilitating more consistent, timely, and transparent performance

[9] OCC NR 2018-87, *OCC Seeks Comments on Modernizing Community Reinvestment Act Regulations*; 83 Fed. Reg. 45053 (Sept. 5, 2018).

evaluations and CRA ratings; and encouraging increased community and economic development in low- and moderate-income areas. The public comment period on the ANPR is open until November 19, 2018. I look forward to reading the stakeholder comments we receive and working with my regulatory colleagues and other stakeholders as we move forward.

Innovation. At the end of July, the OCC announced that it will accept applications for special purpose national bank charters from financial technology (fintech) companies that are engaged in the business of banking but do not take deposits, provided they meet the requirements and standards for obtaining a charter.[10] This decision reflects the OCC's understanding that responsible innovation will enable banks to meet consumers', businesses', and communities' evolving needs; operate in a safe and sound manner; provide fair access to financial services; and treat customers fairly. Responsible innovation is important in order for banks to continue to promote economic opportunity and job creation going forward. Let me reiterate, however, that the OCC will supervise special purpose national banks like other similarly situated national banks. They will be held to the same high standards applicable to any other national bank, including with respect to capital, liquidity, and financial inclusion commitments as appropriate.

The OCC's decision to consider applications for special purpose national bank charters followed extensive outreach by the OCC over a two-year period. It also is consistent with bipartisan government efforts at the federal and state levels to promote economic opportunity and support innovation that can improve the provision of and access to financial services.

In addition, fintech companies that provide banking services in innovative ways deserve the opportunity to pursue that business on a national scale as federally chartered banks. Contrary to what some have suggested, I believe that a special purpose national bank charter supports and

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[10] OCC NR 2018-74, *OCC Begins Accepting National Bank Charter Applications From Financial Technology Companies*, July 31, 2018.

enhances the dual banking system. A federal charter provides companies interested in banking with another choice, alongside others such as becoming a state bank, operating as a state-licensed financial service provider, or pursuing a partnership or business combination with an existing bank. Competition between these options yields a wider range of products and services available to consumers, lower regulatory costs, and more effective supervision.

Short-term, small-dollar lending. On May 23, 2018, the OCC issued a bulletin encouraging banks to offer responsible short-term, small-dollar installment loans to help meet the credit needs of consumers.[11] The bulletin reminds banks of the core lending principles for prudently managing the risks associated with this type of installment lending and is consistent with the OCC's support for responsible innovation by banks. Encouraging banks to offer these products will bring borrowers back into the regulated marketplace and will help improve their access to additional mainstream financial products, which will benefit these borrowers and the economy.

Bank Secrecy Act and Anti-money laundering (BSA/AML). The OCC has taken a leadership role in coordinating discussions among the FDIC, Board, NCUA, U.S. Department of Treasury (Treasury), and Financial Crimes Enforcement Network (FinCEN) to identify ways to improve the efficiency and effectiveness of BSA/AML regulations, supervision, and examinations. The financial institution regulators are working closely with Treasury and FinCEN to identify ways to enhance the risk-focused supervisory process while continuing to support law enforcement and reducing unnecessary burden currently associated with BSA/AML compliance. The agencies also encourage the use of innovative technologies and practices to assist financial institutions in achieving AML compliance. These proactive efforts

[11] OCC Bulletin 2018-14, *Installment Lending: Core Lending Principles for Short-Term, Small-Dollar Installment Lending*.

towards BSA/AML reform are meant to yield efficiencies while improving the ability of the federal banking system and law enforcement to safeguard the nation's financial system from criminals and terrorists.

Guidance. Finally, in response to recent inquiries suggesting the agencies clarify the differences between supervisory guidance and laws and regulations, on September 11, 2018, the OCC, FDIC, Board, NCUA, and BCFP issued a statement to explain the role of supervisory guidance and to describe policies related to the agencies' approach to supervisory guidance.[12] This statement makes clear that guidance does not have the force and effect of law and that examiners may not criticize financial institutions for "violations" of guidance. At the OCC, we will reinforce this message by continuing to set clear expectations for how our examiners use guidance on examinations and the proper role that guidance plays in the supervisory process.

IV. Conclusion

I appreciate the opportunity to update the Committee on the OCC's work to implement the Economic Growth Act and to share with you the progress we have made in other areas. I believe that consumers, businesses, and communities alike will benefit from these efforts for many years to come. The OCC looks forward to keeping the Committee apprised of our work.

[12] Joint Release, OCC NR 2018-97, *Agencies Issue Statement Reaffirming the Role of Supervisory Guidance*.