STATEMENT OF

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on

IMPLEMENTATION OF THE ECONOMIC GROWTH, REGULATORY RELIEF, AND CONSUMER PROTECTION ACT

before the

COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS
U.S. SENATE

September 13, 2018
538 Dirksen Senate Office Building

Chairman Crapo, Ranking Member Brown, and members of the Committee, thank you for the opportunity to testify today on, the Economic Growth, Regulatory Relief, and Consumer Protection Act (the "Act"), which was signed into law on May 24th. I want to congratulate Chairman Crapo and other members of the Committee who worked hard to craft this strong, bipartisan legislation, and former Chairman Shelby for his prior work in the area. The Act includes a number of directives that will help reduce the regulatory burden on small banks, while preserving the ability of financial regulators to ensure the safety and soundness of banks and the banking system. The Act also makes significant progress in appropriately tailoring regulations to the size and risk profile of particular institutions, especially with respect to small banks.

When I testified during my confirmation hearing, I told you that one of my top priorities would be the health of the Nation's community banks and their ability to effectively serve their communities. Community banks play a pivotal role in their local economies, and our regulatory regime must do what it can to ensure their continued vitality. Implementation of the Act will play a key role in delivering on this priority.

My testimony will describe actions that the FDIC has taken or plans to take to implement the Act's reforms, along with a description of other initiatives and priorities aimed at rightsizing the regulatory requirements for community banks.

Implementation of the Act's Reforms

Interagency Statement

The FDIC has taken a number of actions to implement the Act. With respect to interagency provisions that were effective immediately upon enactment, on July 6, 2018, the FDIC, the Office of the Comptroller of the Currency (OCC), and the Federal Reserve Board (FRB) (collectively, the "agencies") issued a statement describing the positions the agencies would take to implement statutory changes while working to amend existing regulations. Simply put, the statement made clear that we will not enforce existing regulations in a manner inconsistent with the Act.

Among the issues addressed in the statement is the agencies' position on the company-run stress testing requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). For depository institutions with average total consolidated assets of $100 billion or less, the agencies extended the deadlines for such stress tests until November 25, 2019, thereby eliminating requirements related to the Dodd-Frank Act company-run stress testing. This action was taken to avoid unnecessary burden for depository institutions and to maintain consistency between bank holding companies and depository institutions.

The interagency statement also addressed a number of other issues, including resolution planning, the Volcker Rule, risk weighting of high volatility commercial real estate (HVCRE) exposures, the examination cycle for small banks, the treatment of municipal obligations under the liquidity coverage ratio (LCR), and an exemption from appraisal requirements for certain transactions.

Section 103: Appraisals for Residential Loans in Rural Areas

Section 103 of the Act became effective immediately upon enactment and exempts certain loans secured by real property from the agencies' appraisal requirements. The exemption applies to federally related transactions under $400,000 and secured by a lien on properties located in rural areas. The exemption does not apply if a federal financial institution's regulatory agency requires an appraisal for safety and soundness purposes or if the loan is a "high-cost mortgage," as defined in the Truth in Lending Act. The agencies are currently working on changes to existing regulations.

Section 201: Small Bank Leverage Ratio

Section 201 of the Act directs the agencies, in consultation with applicable state bank supervisors, to develop a community bank leverage ratio of not less than 8 percent and not more than 10 percent. Under the law, community banks that exceed the community bank leverage ratio will be considered compliant with all other capital and leverage requirements. This will substantially simplify compliance with capital rules for qualifying banks. This community bank leverage ratio will only be available to certain banks with total consolidated assets of less than $10 billion. The agencies are working expeditiously to develop a proposed rule to implement this provision.

Section 202: Reciprocal Deposits

Section 202, which became effective upon enactment, provides that, under certain circumstances, reciprocal deposits will not be considered funds obtained, directly or indirectly,

by or through a deposit broker under section 29 of the Federal Deposit Insurance Act. Reciprocal deposits are defined as deposits that a bank receives through a deposit placement network with the same maturity (if any) and in the same aggregate amount as deposits the bank submitted for placement through the deposit placement network. The FDIC, working with the Federal Financial Institutions Examination Council (FFIEC) members, revised the Call Report Instructions to reflect the reporting change from brokered to non-brokered treatment of specified reciprocal deposits for the June 30, 2018 Call Report. Additionally, on September 12, 2018, the FDIC issued a Notice of Proposed Rulemaking (NPR) to conform its brokered deposit regulation to section 202.

Sections 203 and 204: Volcker Rule

Section 203 of the Act amends the definition of "banking entity" under section 13 of the Bank Holding Company Act to alter which institutions are subject to the requirements of the Volcker Rule. The term "banking entity" is defined under the Bank Holding Company Act to include an insured depository institution or a company that controls an insured depository institution. Following the passage of the Act, the term "insured depository institution" does not include an institution (A) that functions solely in a trust or fiduciary capacity (subject to certain conditions) or (B) that does not have and is not controlled by a company that has (i) more than $10 billion in total consolidated assets and (ii) total trading assets and trading liabilities that are more than 5 percent of total consolidated assets.

Section 204 revises the statutory provisions related to the naming of covered funds, effective on the date of enactment. This revision removes certain naming restrictions on covered

funds in a manner than enables hedge funds or private equity funds to share the same name as a banking entity that is an investment adviser to the fund under certain conditions.

Section 205: Short Form Call Reports

Section 205 of the Act requires the banking agencies to issue regulations that allow for a reduced reporting requirement in the first and third quarter Call Reports for "covered depository institutions" that have less than $5 billion in total assets and satisfy other appropriate criteria established by the agencies. The agencies are developing a proposed rule to implement section 205 that we intend to issue for comment in the very near term.

The agencies' efforts to implement section 205 will build on the work already done by the FFIEC's Community Bank Call Report Burden-Reduction Initiative, which includes the introduction of a streamlined Call Report that, at present, is generally applicable to institutions with domestic offices only and total assets of less than $1 billion. The shorter Call Report reduced the length of the report for eligible small institutions from 85 to 61 pages, removed approximately 40 percent of the nearly 2,400 data items required, and reduced the reporting frequency for approximately 100 additional data items. In implementing section 205, in addition to raising the asset threshold and expanding the number of eligible institutions, the agencies are exploring ways to further streamline Call Reports.

Section 210: Examination Cycle

Section 210 of the Act raises the total asset threshold from $1 billion to $3 billion for well-capitalized insured depository institutions to be eligible for an 18-month examination cycle, setting a longer examination cycle for a larger number of "1-rated" institutions and authorizing the agencies to make corresponding changes for "2-rated" institutions. On August 23, 2018, the FDIC issued an IFR with the OCC and the FRB to conform existing rules and to make the corresponding change for 2-rated institutions. Under the IFR, up to 420 additional institutions will benefit from an 18-month examination cycle. Comments on the IFR were requested within 60 days of publication in the *Federal Register*.

Section 214: Revised Definition for HVCRE

Prior to the enactment of the Act, the regulatory capital treatment of HVCRE exposures was a concern for many institutions. Under the standardized approach, banks were required to assign a 150 percent risk-weight to any loans that met the definition of HVCRE. Section 214 provides that the agencies may only require a bank to assign a heightened risk weight to such an exposure if it is an "HVCRE ADC Loan," as defined in the statute. While banks are currently able to report their HVCRE exposures using this new definition, the FDIC must amend its capital rules to align with the definition provided in the Act. On September 12, 2018, the FDIC issued a Notice of Proposed Rulemaking (NPR) to conform its capital regulation to section 214.

Section 403: Municipal Obligations as High-Quality Liquid Assets (HQLA)

Section 403 of the Act requires the agencies to treat certain municipal obligations as HQLA for purposes of their final rules establishing the LCR and in other regulations

incorporating the term HQLA. The section also requires the agencies to amend their liquidity regulations to implement these changes no later than 90 days after enactment. On August 22, 2018, the FDIC issued an IFR jointly with the OCC and the FRB that amends the agencies' LCR rule to treat liquid and readily-marketable, investment grade municipal obligations as HQLA. Comments on the IFR were requested within 30 days of publication in the *Federal Register*.

Additional FDIC Initiatives

In addition to implementation of the Act, the FDIC is also looking at additional ways to improve the effectiveness and efficiency of its supervision and regulation and to enhance its processes and communications.

Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA)

EGRPRA requires the agencies to conduct a joint review of regulations every 10 years and consider whether any of those regulations are outdated or unnecessary. The most recent EGRPRA cycle resulted in a Joint Report to Congress, submitted by the banking agencies and the National Credit Union Administration (NCUA) in March 2017. Through this process, the agencies began to address issues related to regulatory burden, including reporting requirements, capital rules, and appraisal requirements. As a few examples stemming from the review, the agencies have implemented a short form call report, issued an NPR to simplify certain aspects of the regulatory capital rules, and raised the threshold for commercial real estate loans exempt from appraisal requirements.

Future Initiatives

Since becoming Chairman, I have focused on reviewing the FDIC's organization and processes, approach to supervision, and existing regulations and policies. The FDIC has commenced work on a number of new initiatives, and others will be introduced in the near future. A few of my initial priorities include improving (1) the transparency and accountability of the agency, (2) the examination process, and (3) the *de novo* application process.

Improving transparency at the FDIC will be a core component of my Chairmanship. Yesterday, the FDIC issued a request for comment on how the FDIC disseminates information to regulated institutions, and how to make these communications more effective, streamlined, and clear. Additionally, on September 10, 2018, the FDIC proposed to rescind more than 50 percent of the Financial Institution Letters (FILs) related to safety and soundness issues after determining they are outdated or that the information can be found elsewhere on the FDIC's website. We also plan to retire more than half of FILs related to consumer compliance as well. Overall, my goal is to make sure that supervisory guidance we provide is as clear and concise as possible, and that outdated or superseded supervisory communications are archived.

As the current chair of the FFIEC, the FDIC is leading an Examination Modernization Project to minimize burden to banks where possible, principally by reevaluating traditional processes and making better use of technology. Additionally, the FDIC has undertaken separate internal projects to improve the effectiveness, efficiency, and quality of community bank safety and soundness processes. These projects are focused on improving the examination planning

process and further risk-focusing or tailoring examinations to a bank's business model, complexity, and risk profile.

The FDIC is currently looking at how we can further improve the application process to encourage more *de novo* activity while ensuring that prospective banks are strong enough to survive, especially given industry consolidation over recent decades. Since January 2010, the number of insured depository institutions has declined by nearly 2,500, which includes mergers of non-affiliated banks (41 percent); consolidations within the same organization (27 percent); bank failures (15 percent); acquisitions of banks on the problem bank list (11 percent); and self-liquidations (6 percent). Meanwhile, during that same time period, only 11 new charters have been approved and opened, most in the past 15 months .[1] To ensure the long-term vibrancy of the banking industry, it is important to attract new start-ups and new capital. It is also important to clarify that the FDIC does not have a standard initial capital figure for *de novos*, but rather a prospective bank is expected to propose initial capital sufficient to support its business model.[2]

The FDIC is also planning to address a number of additional regulatory priorities in the coming months, including revisiting those regulations that have not received recent or comprehensive public input. One example is a comprehensive look at the regulatory approach to brokered deposits and national rate caps, which will include seeking public comment later this year. The banking industry has undergone significant changes since these regulations were put

[1] This number does not include shelf charters (new banks formed to acquire a failed bank or another bank), conversions (which includes credit unions converting into banks, or new banks that are spin-offs of existing banks), or a new subsidiary by a banking organization that already has an affiliated bank.

[2] The FDIC's *Statement of Policy on Applications for Deposit Insurance* states that normally, the initial capital of a proposed depository institution should be sufficient to provide a Tier 1 capital to assets leverage ratio (as defined in the appropriate capital regulation of the institution's primary federal regulator) of not less than 8.0% throughout the first three years of operation. In addition, the depository institution must maintain an adequate allowance for loan and lease losses. Initial capital should normally be in excess of $2 million net of any preopening expenses that will be charged to the institution's capital after it commences business. Overall, the amount of capital will be dependent on the prospective bank's size and proposed business model – there is no standard dollar amount required.

into place, and we will consider the impact of changes in technology, business models, and products since the brokered deposit requirements were adopted.

Conclusion

Thank you again for the opportunity to appear before you today, and I look forward to your questions.