STATEMENT BY

MARTIN J. GRUENBERG

CHAIRMAN

FEDERAL DEPOSIT INSURANCE CORPORATION

on

"Oversight of Prudential Regulators"

before the

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

November 15, 2023

2128 Rayburn House Office Building

Washington, DC

Chairman McHenry, Ranking Member Waters, and Members of the Committee, I am pleased to appear at today's hearing on "Oversight of Prudential Regulators." I appreciate the opportunity to report on the Federal Deposit Insurance Corporation's (FDIC) recent work in protecting insured deposits, supervising state chartered banks that are not members of the Federal Reserve system for safety and soundness and consumer protection, and in resolving failed insured depository institutions.

My statement discusses the lessons learned from the regional bank failures this spring and proposed improvements in regulation and bank supervision that could help prevent similar bank failures or mitigate their impact in the future. In addition to proposals focused on large regional banks, my testimony discusses other important regulatory activities at the FDIC, including the publication of the Basel III Notice of Proposed Rulemaking (NPR) and the adoption of the final rule modernizing and strengthening the Community Reinvestment Act (CRA). Finally, I will discuss the FDIC's efforts to support Minority Depository Institutions (MDIs) and Community Development Financial Institutions (CDFIs).

State of the Banking Industry

The banking industry has proven to be quite resilient despite the period of stress earlier this year. In the second quarter, key banking industry measures of performance remained favorable. Net income remained high by historical measures, asset quality measures were stable, and the industry remained well capitalized.[1] However, banks reported lower net interest margins and higher funding pressures for a second consecutive quarter. Higher market interest rates and

[1] In the second quarter, the banking industry's net income was $70.8 billion, a decrease of $9.0 billion from first quarter. But after excluding nonrecurring accounting gains on failed bank acquisitions that occurred in the first and second quarters, net income was roughly flat from the prior quarter—and in fact from fourth quarter 2022 as well. See FDIC *Quarterly Banking Profile*: Second Quarter 2023 available at https://www.fdic.gov/analysis/quarterly-banking-profile/.

mortgage rates caused market values for debt to generally fall during the second quarter, resulting in higher unrealized losses on securities.[2] While the FDIC Quarterly Banking Profile data will not be available until later this month, early reports from third quarter 2023 indicate that the banking industry remains profitable and well-capitalized, that asset quality metrics continue to normalize from the historic lows reached during the pandemic, and that funding cost challenges have persisted, especially for small and mid-sized banks.

As of June 30, 2023, deposits continued to decline for the fifth consecutive quarter, as depositors continue to seek higher yields. However, deposit outflows moderated substantially from the large outflows reported in the first quarter when the industry experienced significant stress and two regional banks failed. In the second quarter, uninsured deposits declined by 2.5 percent, far less than the 8 percent decline reported in the first quarter. By contrast, insured deposits increased by 0.8 percent during the second quarter, driven by higher insured brokered deposits and reciprocal deposits.

There has been a great deal of discussion about deposit flows to the nation's larger banks, primarily under the assumption that deposits have flowed from regional banks to the largest banks. While deposit balances may have suggested that such flows occurred on a limited basis toward the end of the first quarter, that does not appear to have been the case in the second quarter. The nation's global systemically important banks reported a decline in total deposits, primarily driven by a decline in uninsured deposits. Rather than a simple story of deposits flowing to the largest banks, the second quarter's deposit story appears to have been more about depositors seeking higher yields, often at nonbank financial institutions, particularly money

[2] Unrealized gains (losses) on securities solely reflect the difference between the market value as of quarter-end and the book value of non-equity securities.

market mutual funds. Many banks have increased deposit rates to compete, resulting in higher cost of funds.

In addition, higher interest rates reduce the value of assets that yield a fixed interest rate. Loans and securities with longer maturities and locked-in lower yields may pressure earnings in coming quarters. These longer-term balance sheet holdings further limit the ability of banks to lend, raise capital, or restructure. Market rates continued to increase through the third quarter, likely putting downward pressure on the value of securities portfolios.

The banking industry continues to face significant downside risks from the effects of inflation, rising market interest rates, and geopolitical uncertainty. Moreover, the economic outlook remains uncertain, despite relatively solid growth and low unemployment so far this year. These risks could cause credit quality and profitability to weaken, loan growth to slow, provision expenses to rise, and liquidity to become more constrained. Commercial real estate (CRE) loan portfolios, particularly loans backed by office properties, face challenges when loans mature as demand for office space remains weak and property values continue to soften. Banks have tightened underwriting standards over the past year across a range of household and business loans, and they may continue to tighten further this year.[3]

The FDIC will continue to monitor prevailing trends in the banking industry and will publicly release data for the third quarter of this year as part of the Quarterly Banking Profile.[4]

<u>Condition of the Deposit Insurance Fund</u>

As of June 30, 2023, the Deposit Insurance Fund (DIF) balance totaled $117.0 billion, down $11.3 billion (8.8 percent) from year-end 2022, primarily resulting from an increase in loss

---

[3] Federal Reserve Senior Loan Officer Opinion Survey on Bank Lending Practices, July 2023. https://www.federalreserve.gov/data/sloos/sloos-202307 htm

[4] See FDIC *Quarterly Banking Profile* available at https://www fdic.gov/analysis/quarterly-banking-profile/.

provisions associated with the failures of Silicon Valley Bank (SVB), Santa Clara, California; Signature Bank (Signature), New York, New York; and First Republic Bank (First Republic), San Francisco, California, in the first half of 2023.[5] The decline in the DIF balance coupled with strong growth in estimated insured deposits resulted in a decline in the reserve ratio of 15 basis points from 1.25 percent as of December 31, 2022, to 1.10 percent as of June 30, 2023.[6]

A total of five banks have failed so far in 2023, resulting in a combined estimated loss of $34.2 billion.[7] As of June 30, 2023, the FDIC estimated the cost for the failures of SVB and Signature Bank to total $18.5 billion.[8] Of that estimated total cost of $18.5 billion, the FDIC estimated that approximately $15.8 billion was attributable to the cost of covering uninsured deposits as a result of the systemic risk determination made on March 12, 2023, following the closures of SVB and Signature Bank. As with all failed bank receiverships, losses will be periodically adjusted as assets are sold, liabilities are satisfied, and receivership expenses are incurred.

By statute, the FDIC is required to recover the $15.8 billion estimated loss through one or more special assessments.[9] Accordingly, the FDIC issued a proposed rule to implement this special assessment.[10] In implementing the special assessment, the law requires the FDIC to

---

[5] The decline in the DIF balance does not include the cost of protecting uninsured deposits pursuant to the systemic risk determination announced following the failures of SVB and Signature Bank in March 2023, as the FDIC is required by statute to recover those losses through special assessments. See 12 U.S.C. 1823(c)(4)(G)(ii).
[6] The reserve ratio is calculated as the ratio of the net worth of the DIF (fund balance) to the value of the aggregate estimated insured deposits at the end of a given quarter. See 12 U.S.C. 1813(y)(3).
[7] Estimated loss as of the end of the second quarter of 2023, except for Heartland Tri-State Bank which closed in July 2023 and resulted in an estimated $54.2 million loss in the third quarter (FDIC PR-58-2023), and Citizens Bank which closed in November 2023 and resulted in an estimated $14.8 million loss in the fourth quarter (FDIC PR-91-2023).
[8] Descriptions of the loss estimates for SVB and Signature Bank and the estimated special assessment amount are available on page 32696 of the *Notice of Proposed Rulemaking on Special Assessments Pursuant to Systemic Risk Determination*, available at https://www.fdic.gov/news/board-matters/2023/2023-05-11-notice-dis-a-fr.pdf.
[9] 12 U.S.C. 1823(c)(4)(G)(ii)(I).
[10] See *Notice of Proposed Rulemaking on Special Assessments Pursuant to Systemic Risk Determination*, available at https://www.fdic.gov/news/board-matters/2023/2023-05-11-notice-dis-a-fr.pdf.

consider the types of entities that benefit from any action taken or assistance provided as well as economic conditions, the effects on the industry, and other factors deemed appropriate and relevant.[11] In general, large banks with large amounts of uninsured deposits benefitted the most from the systemic risk determination. Under the proposal, the FDIC would apply an annual special assessment rate of approximately 12.5 basis points to an assessment base that would equal an insured depository institution's (IDI) estimated uninsured deposits reported as of December 31, 2022, adjusted to exclude the first $5 billion in estimated uninsured deposits from the IDI, or at the banking organization level for IDIs that are part of a holding company with one or more subsidiary IDIs. Under the proposal, no banking organizations with total assets under $5 billion would pay the special assessment. Under the proposal, the FDIC estimates banking organizations with total assets over $50 billion would pay over 95 percent of the special assessment. The effect of the proposed special assessment on the dollar amount of Tier 1 capital is estimated to be minimal, measuring less than one percent, on average. The FDIC Board will consider a final rule later this week.

The remaining estimated loss from the failures of SVB and Signature Bank of $2.7 billion and additional estimated losses of $15.6 billion from the May 2023 closure of First Republic Bank, directly impacted the DIF balance in the first half of 2023.[12]

Despite recent outflows for total deposits, accelerated by the stress experienced in the banking industry in March, insured deposit balances increased by 2.2 percent in the first quarter and 0.8 percent during the second quarter, bringing year-over-year insured deposit growth to 4.7

[11] 12 U.S.C. 1823(c)(4)(G)(ii)(III).

[12] For estimated cost of the failure of First Republic Bank, see page 31 of the FDIC *Quarterly Banking Profile:* Second Quarter 2023, available at https://www fdic.gov/analysis/quarterly-banking-profile/qbp/2023jun/qbp.pdf#page=1.

percent, slightly above the long-term historical average of 4.5 percent.[13] As required by the Federal Deposit Insurance Act (FDI Act),[14] the FDIC has been operating under a Restoration Plan since September 15, 2020,[15] which aims to restore the DIF to the statutory minimum reserve ratio of 1.35 percent within eight years. Notwithstanding the recent losses due to bank failures and growth in insured deposits, the DIF remains on track to meet the statutory minimum reserve ratio of 1.35 percent by the eight-year deadline of September 30, 2028.[16]

Update on Resolution Activities

Regional Bank Receiverships

The FDI Act requires the FDIC, when acting as a receiver, to manage and market assets in a manner that: maximizes returns and minimizes losses; ensures adequate competition and fair and consistent treatment of potential buyers of assets; prohibits discrimination in the sales process; and maximizes the preservation of the availability and affordability of residential real property for low- and moderate-income individuals. To date, the FDIC has made progress toward meeting these statutory obligations in all five of the receiverships from this past year.

Silicon Valley Bank

The FDIC retained securities with a face value of $87 billion (approximately $75 billion market value) and an additional $3 billion of other assets including assets of SVB's foreign branches. To date, the FDIC has collected $1.1 billion in regular principal payments by securities issuers and undertaken a gradual and orderly sale of nearly $74 billion (face value) of

[13] Long-term historical average is from 1991 through 2019.
[14] Section 7(b)(3)(E) of the Federal Deposit Insurance Act, 12 USC 1817(b)(3)(E), available at https://www.fdic.gov/regulations/laws/rules/1000-800 html#fdic1000sec.7b.
[15] 2020 FDIC Restoration Plan, 85 FR 59306 (Sept. 21, 2020), available at https://www.fdic.gov/news/board-matters/2020/2020-09-15-notice-dis-a-fr.pdf.
[16] Section 7(b)(3)(E) of the FDI Act, 12 USC 1817(b)(3)(E), available at https://www.fdic.gov/regulations/l/rules/1000-800.html#fdic1000sec.7b.

the securities while minimizing the potential for adverse impact on market functioning by taking into account daily liquidity and trading conditions. The FDIC expects to substantially conclude sales of the securities by the end of the year. The FDIC is also monitoring the shared loss agreement with the acquiring institution covering approximately $61 billion of outstanding commercial loans and up to approximately $50 billion of unfunded commitments.

Signature Bank

With respect to the resolution of Signature Bank, approximately $60 billion of the bank's loans and $27 billion in securities were retained by the FDIC. Receivership staff have been overseeing the servicing and collection of the retained loans and have collected approximately $13 billion in principal and interest payments from borrowers since March 2023, net of advances made to borrowers over the same period. The FDIC has completed the competitive sales of two Signature loan portfolios totaling approximately $19 billion, recovering over 99 percent of the book value of an $18 billion portfolio of "capital call" loans to investment funds and receiving over 85 percent of the book value of a $631 million pool of loans to technology and life science companies backed by venture capital sponsors.

In addition, on September 5, 2023, the FDIC announced the start of a marketing process for the approximately $33 billion commercial real estate (CRE) loan portfolio. This portfolio represents substantially all remaining loans retained in the Signature receivership. Marketing of the former Signature Bank's CRE portfolio is taking place over the fourth quarter of 2023.

The majority of the CRE loan portfolio is comprised of multifamily properties, primarily located in New York City. A large portion (approximately $15 billion) of the CRE loans is secured by multifamily residences that are rent stabilized or rent controlled. As mentioned, the FDIC has a statutory obligation to maximize the preservation of the availability and affordability

of residential real property for low- and moderate-income individuals. Since March, the FDIC has been working closely with city and state authorities, as well as with community organizations where the properties securing these loans are located, to inform them of the FDIC's efforts and seek their input as it develops its marketing and disposition strategy. To help fulfill this obligation, the FDIC will place the rent stabilized or rent controlled loans into one or more joint ventures (JV) with the FDIC retaining a majority equity interest in the JV.

Aside from loans, FDIC retained securities of Signature Bank with a face value of approximately $27 billion. The FDIC has conducted a gradual and orderly sale of approximately $24 billion (face value) of these securities, as of October 5, 2023.

FDIC also competitively marketed Signature's equity investment, trademarks, and contracts related to the "Signet" platform, a blockchain-based digital payments platform. The FDIC sold the trademarks and preferred stock to the highest bidders for a total of $152,000. Bidders included banks as well as non-bank financial firms. No bids were received for the master servicing contract, so it was subsequently repudiated by the Receiver to extinguish the liability.

First Republic Bank

In the resolution of First Republic, the FDIC transferred essentially all of the assets to an assuming institution, which also assumed all of the deposits of the failed bank. The FDIC retained $4 billion of First Republic's assets and entered into a Shared Loss Agreement with the assuming institution, JPMorgan Chase Bank, N.A. (JPMC), on the First Republic loans that JPMC purchased. The Shared Loss Agreement covers approximately $164 billion of commercial and residential loans and $46 billion of unfunded loan commitments.

Heartland Tri-State Bank

Heartland Tri-State Bank of Elkhart, Kansas, was closed by the Kansas Office of the State Bank Commissioner on July 28, 2023 and the FDIC was appointed as receiver. As of March 31, 2023, Heartland Tri-State Bank had approximately $139 million in total assets and $130 million in total deposits. To resolve the bank, FDIC entered into a Purchase and Assumption Agreement with Dream First Bank, National Association, of Syracuse, Kansas, to assume all of the deposits and essentially all of the assets of Heartland Tri-State Bank. The FDIC estimates that the cost to the DIF will be $54 million.

Citizens Bank

Citizens Bank, Sac City, Iowa, was closed on November 2, 2023 by the Iowa Division of Banking, which appointed the FDIC as receiver. As of September 30, 2023, Citizens Bank had approximately $66 million in total assets and $59 million in total deposits. To resolve the bank, the FDIC entered into a Purchase and Assumption Agreement with Iowa Trust & Savings Bank, Emmetsburg, Iowa, to assume all of the deposits and essentially all the assets of Citizens Bank. The FDIC estimates that the cost to the DIF will be $14.8 million.

Efforts to Improve Regional Bank Resilience and Resolvability

The failure of three large regional banks this spring demonstrated clearly the risk to financial stability that large regional banks can pose. The federal banking agencies are taking action to address these vulnerabilities with jointly proposed rulemakings that would facilitate the readiness and resolvability of insured depository institutions in the event of their insolvency and improve the protection of depositors in the event of a failure.

On August 29, 2023, the FDIC Board approved three complementary proposals that together will greatly strengthen the ability of the FDIC to manage a resolution of a large complex

financial institution: Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions;[17] Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets;[18] and Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers[19] and Foreign Triennial Full Filers.[20]

The Long-Term Debt proposal, published jointly with the Board of Governors of the Federal Reserve System (Federal Reserve) and the Office of the Comptroller of the Currency (OCC), would require a layer of loss-absorbing capacity at large IDIs. This long-term debt requirement can mitigate the resolution challenges encountered in the failure of large regional banks and bolster financial stability. The long-term debt absorbs losses before the depositor class – uninsured depositors and the FDIC – take losses. This lowers the incentive for uninsured depositors to run. Protecting depositors and the DIF, helping to make their resolution more orderly, and creating additional options for the FDIC in resolution makes it more likely that a closing weekend sale could comply with the statutory least-cost test and avoid the need for a systemic risk exception.

---

[17] Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions, 88 Fed. Reg. 64524 (September 19, 2023).

[18] Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets, 88 Fed. Reg. 64579 (September 19, 2013).

[19] Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers, 88 Fed. Reg. 64626 (September 19, 2023).

[20] Guidance for Resolution Plan Submissions of Foreign Triennial Full Filers, 88 Fed. Reg. 64641 (September 19, 2023).

The revised resolution plan regulation for IDIs under the FDI Act would improve the FDIC's knowledge of a troubled large IDI and preparation for the resolution of the large IDI. The revised resolution plan regulation would require an IDI with at least $100 billion in assets to provide a strategy that is not dependent on an over-the-weekend sale, including by explaining how the IDI could be placed into a bridge depository institution, how operations could continue while the IDI separates itself from its parents and affiliates, and the actions that would be needed to stabilize a bridge depository institution, among others. The revised resolution plan regulation would also require all IDIs subject to the rule to demonstrate capabilities essential to an orderly resolution, such as establishing a virtual data room and populating it with enough information for interested parties to bid on the bank or certain of its assets and operations.

Finally, guidance for resolution plans required under Title 1 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), proposed with the Federal Reserve, would allow Title 1 resolution planning to better reflect the lessons learned in dealing with domestic and foreign financial firms that are just below the size threshold of the U.S. Global Systemically Important Banks (G-SIBs). The proposed guidance addresses certain capabilities that are essential for firms to have to effect an orderly resolution such as those necessary to project the capital and liquidity needed to carry out their plan; operational capabilities related to payment, clearing and settlement activities; collateral; management information systems; and shared and outsourced services.

All of these proposals, individually and taken together, are tailored to account for the differences that exist among institutions while leveraging the improvements and advances to resolution preparedness and planning that have been made since the financial crisis of 2008. The comment period for these proposals closes on November 30, 2023.

Basel III Notice of Proposed Rulemaking

On July 27, 2023, the FDIC Board approved a Notice of Proposed Rulemaking (NPR) that would revise and strengthen the capital requirements applicable to the largest banking organizations.[21] The proposed framework would generally be consistent with international capital standards issued by the Basel Committee on Banking Supervision, commonly known as the Basel III reforms. The NPR was also approved by the Federal Reserve and the OCC.

The NPR is a continuation of the federal banking agencies' efforts to revise the regulatory capital framework for our nation's largest financial institutions, which were found to be undercapitalized and over-leveraged during the global financial crisis of 2008. Following the 2008 crisis, the federal banking agencies strengthened the banking system through an initial set of revisions to the capital framework. Those revisions raised the quality and quantity of risk-based capital and included the introduction of an enhanced supplementary leverage ratio for our largest, most systemic banking organizations. However, there remain areas of the regulatory capital framework that need improvement.

The NPR would make important changes to address the capital weaknesses identified in the 2008 financial crisis, enhance the resilience and stability of the banking system, and enable the banking system to better serve the U.S. economy. For example, the proposal would address critical areas of the risk-based capital framework related to credit risk, operational risk, market risk, and financial derivative risk. For credit risk, the proposal would eliminate the use of banking organizations' internal models to set regulatory capital requirements and in its place apply a simpler, standardized framework. Similarly, for operational risk, the proposal would introduce a standardized framework in lieu of the existing model-based approach, thereby

[21] Regulatory Capital Rule: Large Banking Organizations and Banking Organizations With Significant Trading Activity, 88 fed. Reg. 64028 (September 18, 2023).

enhancing transparency and comparability. With respect to market risk, the proposal includes a more robust methodology to capture potential stress events, using a so-called expected shortfall methodology. This is in response to significant losses incurred in large banking organizations' trading portfolios during the global financial crisis. Lastly, the proposal would strengthen capital requirements with respect to financial derivative risk. Taken together, these changes would bolster the financial resilience of our nations' largest banking organizations.

A key consideration with respect to these revisions is the scope of application – in other words, which banks are subject to the proposed rule. Historical experience has demonstrated the impact individual banking organizations can have on the stability of the U.S. banking system, in particular large banking organizations. With this in mind, the proposal would apply to banking organizations with total assets of $100 billion or more and to other banking organizations with significant trading activity. Consistent with this scope of application, the proposal would also align the calculation of regulatory capital for large banking organizations; that is, all banking organizations with more than $100 billion in total assets would include net unrealized holding losses on securities categorized as available-for-sale in the calculation of regulatory capital. As the agencies have learned from recent experience with bank failures, this change would help ensure that the regulatory capital ratios of large banking organizations better reflect their capacity to absorb losses. Notably, the NPR would not change the capital requirements applicable to community banks.

By addressing weaknesses in the existing regulatory framework, the proposal is expected to increase capital requirements in the aggregate. It is estimated that the proposal would increase common equity tier 1 capital requirements by 16 percent for holding companies and 9 percent for insured depository institutions. A change to capital requirements comes with associated costs

and benefits. The FDIC, together with the other banking agencies, is carefully considering these trade-offs to inform the various components of the rule.

It is expected that the impact would vary meaningfully by institution, depending on each banking organization's activities and risk profile. The majority of banks that would be subject to the proposed rule currently have enough capital to meet the proposed requirements. For those large holding companies with shortfalls, we estimate that these banking organizations would be able to achieve compliance with the revisions through earnings over a short timeframe, even while maintaining their dividends.

The proposed changes would be phased in over a 3-year transition period. Any final rule, following careful consideration of comments received, is not expected to take effect until July 1, 2025. Taking the effective date and transition period together, the capital requirements under a final rule would not be fully effective until the second half of 2028.

The NPR included a 120-day comment period ending November 30, 2023. The agencies have already started receiving comments from the industry and other related parties and have also begun meeting with industry representatives. For example, we have heard concerns related to the proposed treatment for residential mortgage exposures, certain tax credit equity investments, trading activities, and banking activities that generate large amounts of fee-based revenue. The agencies recently announced an extension of the comment period until January 16, 2024 to allow interested parties more time to analyze the issues and prepare their comments. The feedback to-date has been extremely helpful, and the FDIC looks forward to receiving additional comments and feedback.

Other Enhancements to the Supervision of Large Regional Banks

The three regional banks that failed this spring had different business models and various common attributes that made them vulnerable to disruptions: overreliance on uninsured deposits; rapid growth, and weak interest rate and liquidity risk management; and for two of the banks, unrealized losses. In response to the failures, the FDIC is reviewing options to improve the supervision of these key areas. For example, we are updating examiner guidance to be more explicit about analyses of uninsured deposit concentrations and have reemphasized to examiners the importance of forward-looking indicators of risk, such as high growth rates and breaches of internal risk limits. Additionally, we have strengthened our instructions for examiners on timely escalation of supervisory responses when management has been unable or unwilling to effect corrective action, or when financial conditions deteriorate rapidly, or both. All of these options are consistent with the areas for consideration outlined by the FDIC's Chief Risk Officer in his reports on the failed FDIC-supervised institutions.[22]

Other Regulations and Guidance

Modernizing and Strengthening the Community Reinvestment Act

On October 24, 2023, the FDIC, the Federal Reserve, and the OCC adopted a final rule to strengthen and modernize the CRA. The final rule represents an ambitious effort to adapt CRA to the dramatically changed nature of the banking business since the law's enactment in 1977 and the last major rule change in 1995.

To begin with, banks today no longer serve their customers exclusively through a branch–based network around which CRA assessment areas are currently drawn. While bank

[22] See FDIC's Supervision of Signature Bank (April 28, 2023) available at: https://www fdic.gov/news/press-releases/2023/pr23033a.pdf and FDIC's Supervision of First Republic Bank (September 8, 2023) available at https://www.fdic.gov/news/press-releases/2023/pr23073a.pdf.

branches continue to play a critical role in serving communities, some banks have only one branch or no branch at all. Yet, they engage in large scale lending across the country. Banks increasingly interact with customers either online or through mobile phones in areas in which the banks may not have a physical presence. Lending by banks in such areas is not currently subject to a CRA evaluation.

This final rule adapts to this new banking reality by requiring large banks to establish Retail Lending Assessment Areas (RLAAs) in those geographies outside of their physical footprint where they originate significant numbers of closed–end mortgage loans or small business loans.

Under the final rule, the loans in these new assessment areas will be subject to CRA review and evaluation for the first time, ensuring that large banks serve all segments of the communities in which they are chartered to do business, including low– and moderate–income communities, as the law requires. This represents a critically important adaptation of CRA to the changing nature of the business of banking.

Consistent with this objective, the final rule will give banks credit for community development activities on a nationwide basis, not just in their traditional, branch–based assessment areas. This will recognize banks for their community development financing activities in rural and other underserved areas, including Native Land areas, many of which are so–called "banking deserts." This final rule will give them, for the first time, consideration for channeling capital into areas that may be particularly desperate for banking services.

Second, the final rule establishes a series of metrics and benchmarks against which banks will be measured for CRA performance for lending and community development. This will add important rigor to the CRA evaluation process. It will allow the banking agencies to establish

specific standards for bank performance to achieve a particular CRA rating that will provide an incentive for increased lending to underserved communities. It will also provide greater clarity, transparency, and predictability for the banks and the public, as well as consistency among the agencies.

Third, the final rule tailors CRA evaluations and data collection to bank size, complexity, and business type. All banks are not the same, and all communities are not the same. The final rule tailors the CRA tests and data collection to each bank size category – small, intermediate, and large. For instance, small banks would continue to be evaluated under the existing regulatory framework but would have the option to be evaluated under aspects of the new regulation.

There would be no new data collection or reporting requirements for small or intermediate banks. Overall, the agencies sought to leverage existing data as much as possible. However, large banks with assets over $2 billion will have to collect and report community development data, and large banks over $10 billion in assets will have additional data requirements relating to deposits and retail banking products.

Fourth, the final rule recognizes the importance of minority depository institutions (MDIs), Treasury Department–certified Community Development Financial Institutions (CDFIs), Women's Depository Institutions (WDIs), and Low Income Credit Unions (LICUs) in providing financial access to underserved consumers and communities.

For example, the final rule creates a specific community development definition for eligible activities, such as investments, loan participations, and other ventures conducted by all banks with these institutions, including by other MDIs, WDIs, or CDFI banks. All community development activities conducted by banks with these entities will get credit under the final rule.

Fifth, in furtherance of the agencies' objective to promote transparency, the final rule will require the disclosure of the distribution of home mortgage loan originations and applications of large banks in each of the bank's assessment areas by income, race and ethnicity utilizing publicly available data under the Home Mortgage Disclosure Act (HMDA). This aspect of the final rule is intended to provide transparent information to the public in regard to the bank's lending to communities of color. Although the data disclosed would not have an impact on the CRA ratings of the bank, it would allow the public to compare lending by a bank in those communities to other communities, as well as allow comparisons to other banks.

Sixth, while we know that technology has led to significant changes in the provision of bank services, bank branches continue to play a crucial role for consumers and communities. For example, just over three–quarters of closed–end mortgages originated by large banks in recent years were located in branch–based assessment areas. These branch–based assessment areas remain a foundation of CRA. Under the final rule, each banking agency will be required to evaluate a bank's record of opening and closing branches to inform the degree of accessibility of banking services to low and moderate income communities.

Further, access involves more than the availability of a branch. A consumer must also have access to products and services that are affordable and responsive to their needs. Expanding consumer access to federally insured banks has been a priority of the FDIC. The final rule will provide positive CRA consideration to large banks for the offering and demonstrated consumer usage of low–cost transaction accounts – accounts with low or no minimum balance requirements and no overdraft fees — such as Bank On Certified accounts.

Finally, the rule gives credit to community development activities designed to strengthen disaster preparedness and weather resiliency in low– and moderate– income communities.

Examples of eligible activities could include supporting the establishment of flood control systems in a flood prone area; and retrofitting affordable housing to withstand future disasters or climate–related events.

Since its enactment, CRA has become the foundation of responsible financing for low– and moderate–income communities in the United States. This final rule will significantly expand the scope and rigor of CRA and will assure its continued relevance for the next generation.

Reviewing the Bank Merger Process

Although there has been a significant amount of consolidation in the banking sector over the last thirty years, facilitated in part by mergers and acquisitions, there has not been a significant review of the implementation of the Bank Merger Act (BMA)[23] by the banking agencies in that time. Additionally, the prospect for continued consolidation among both large and small IDIs remains significant.

On March 31, 2022, the FDIC published a Request for Information and Comment on Rules, Regulations, Guidance, and Statements of Policy Regarding Bank Merger Transactions (RFI)[24] that solicited comments regarding the effectiveness of the existing bank merger application framework. The comment period ended on May 30, 2022. The FDIC is evaluating and considering the comments received as it considers changes to the merger review framework, as appropriate.

Finally, the FDIC is coordinating with the Federal Reserve, the OCC, and the Department of Justice regarding an interagency review of the existing laws, regulations, guidance and processes used by the federal banking agencies under the BMA. These discussions, which are

[23] Section 18(c)of the FDIC Act, 12 U.S.C. § 1828(c).

[24] Request for Information and Comment on Rules, Regulations, Guidance, and Statements of Policy Regarding Bank Merger Transactions, 87 Fed. Reg. 18368 (March 31, 2022).

ongoing, are consistent with Presidential Executive Order on Promoting Competition in the American Economy.

Evaluating Financial Risks Posed by Climate Change

On October 24, 2023, the FDIC, Federal Reserve, and OCC adopted interagency guidance on principles for climate-related financial risk management for large financial institutions.[25] The guidance provides a high-level framework for the safe and sound management of exposures to climate-related financial risks and is designed to help financial institutions make progress toward incorporating climate-related financial risks into risk management frameworks in a manner consistent with safe and sound practices. They provide general principles with respect to governance; policies, procedures, and limits; strategic planning; risk management; data, risk measurement, and reporting; and scenario analysis. They also provide guidance on how climate–related financial risks can be addressed in the management of traditional risk areas, such as credit, liquidity, operational risk, and legal and compliance risks.

Although all financial institutions, regardless of size, may have material exposures to climate-related financial risks, these principles are intended for the largest financial institutions, those with over $100 billion in total consolidated assets. The FDIC understands smaller institutions, including community banks, may have limited resources and may experience the impacts of climate-related financial risks in a manner that differs from large financial institutions.

The FDIC's role with respect to climate change is centered on the financial risks that climate change may pose to the banking system, and the extent to which those risks impact the

---

[25] *See,* Interagency Guidance of FDIC, OCC and FRB "Principles for Climate-Related Financial Risk Management for Large Financial Institutions," 88 Fed. Reg. 74183 (October 30, 2023).

FDIC's core mission and responsibilities. As stated in the interagency guidance, the FDIC will not be involved in determining firms or sectors with which financial institutions should do business. These types of credit allocation decisions are the responsibilities of financial institutions. Financial institutions should fully consider climate-related financial risks—as they do all other risks—and continue to take a risk-based approach in assessing individual credit and investment decisions. The FDIC expects financial institutions to manage climate-related financial risks in a manner that will allow them to continue to prudently meet the financial services needs of their communities, including low-and-moderate-income and other underserved consumers and communities.

Evaluating the Risk of Crypto Assets to the Banking System

The FDIC, in coordination with the other federal banking agencies, has taken steps to closely monitor crypto-asset-related activities of banking organizations. For example, the FDIC has issued statements to assist banking organizations in ensuring that they have put in place appropriate measures and controls to identify and manage risks and comply with all relevant laws.

More specifically, in April 2022, the FDIC issued a financial institution letter[26] and requested that all FDIC-supervised institutions that are considering engaging in, or are already engaged in, crypto-asset-related activities notify the FDIC and provide all necessary information that would allow the FDIC to assess the safety and soundness, consumer protection, anti-money laundering/countering the financing of terrorism, and financial stability risks in order to provide supervisory feedback to the institution.

[26] *See* FDIC, "Notification and Supervisory Feedback Procedures for FDIC-Supervised Institutions Engaging in Crypto-Related Activities," (April 7, 2022), available at https://www.fdic.gov/news/financial-institution-letters/2022/fil22016.html.

In addition, the FDIC issued an advisory letter to all FDIC-insured institutions in July 2022 to address concerns about the risks of consumer confusion or harm arising from crypto assets offered by, through, or in connection with insured depository institutions. These concerns were elevated as a result of certain misrepresentations about FDIC deposit insurance by some crypto companies.[27] Inaccurate representations about deposit insurance by non-banks, including crypto companies, may confuse the customers and cause them to mistakenly believe that these investments are protected by deposit insurance. Along with the advisory letter, the FDIC also released consumer education materials advising the public that crypto assets are not deposits insured by the FDIC.[28] Over the course of 2022 and 2023, the FDIC has issued several cease and desist letters that resulted in companies removing misrepresentations about the insured status of crypto products.[29]

More recently, in early 2023, the FDIC, along with the Federal Reserve and the OCC, issued two joint statements on crypto-assets. The first, issued in January 2023, addressed "Crypto-Asset Risks to Banking Organizations," and it enumerated several risks posed by crypto-assets that banking organizations should be aware of including significant volatility in crypto-asset markets; risk management and governance practices in the crypto-asset sector exhibiting a lack of maturity and robustness; and inaccurate or misleading representations or

---

[27] *See* FDIC, "Advisory to FDIC-Insured Institutions Regarding FDIC Deposit Insurance and Dealings with Crypto Companies" (July 29, 2022), available at https://www.fdic.gov/news/financial-institution-letters/2022/fil22035.html.

[28] *See,* FDIC, "FDIC Issues a Fact Sheet to the Public on FDIC Deposit Insurance and Crypto Companies," (July 29, 2022), available at https://www.fdic.gov/news/press-releases/2022/pr22058.html; *see also* FDIC Consumer News, "The Importance of Deposit Insurance and Understanding Your Coverage," (August 2022), available at https://www.fdic.gov/resources/consumers/consumer-news/2022-08 html; *see also* FDIC Podcasts Episode 22, "Deposit Insurance Explained (Part One)," (August 17, 2022), available at https://www fdic.gov/news/podcasts/.

[29] *See, for example,* FDIC, "FDIC Issues Cease and Desist Letters to Five Companies for Making Crypto-Related False or Misleading Representations about Deposit Insurance," (August 19, 2022), available at https://www.fdic.gov/news/press-releases/2022/pr22060 html.

disclosures by crypto-asset companies. This joint statement listed several additional risks.[30] In the second joint statement, issued in February 2023, the agencies highlighted key liquidity risks associated with certain sources of funding from crypto-asset-related entities of which banking organizations should be aware.[31]

The agencies continue to emphasize that banking organizations are neither prohibited nor discouraged from providing banking services to customers of any specific class or type, as permitted by law or regulation.

Supporting Minority Depository Institutions and Community Development Financial Institutions

The preservation and promotion of MDIs remains a long-standing priority for the FDIC.[32] The FDIC supervises approximately two-thirds of the 312 FDIC-insured MDIs and CDFIs (collectively, mission-driven banks). In addition to its supervisory activities, the FDIC's Office of Minority and Community Development Banking supports the agency's ongoing strategic and direct engagement with MDIs and CDFIs.

Over the past five years, six *de novo* MDIs opened their doors (two Asian, one Native American, one African American, and two Multi-racial) and 17 existing institutions became newly designated MDIs due to changes in control or in board composition. These additions to the MDI list mostly offset removals from the list due to mergers, changes in control, or other events that caused institutions to lose their MDI eligibility, resulting in the total number of

[30] *See,* "Joint Statement on Crypto-Asset Risks to Banking Organizations," (January 3, 2023), available at https://www.fdic.gov/news/press-releases/2023/pr23002 html.

[31] See *See* "Joint Statement on Liquidity Risks to Banking Organizations Resulting from Crypto-Asset Market Vulnerabilities," (February 23, 2023), available at https://www fdic.gov/news/financial-institution-letters/2023/fil23008 html.

[32] See Section 308 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. 101-73, title III, § 308. Aug 9, 1989, as amended by Pub. L. 11-203, title III, § 367(4), July 21, 201, 124 Stat. 1556, codified at 12 U.S.C. 1463 note.

FDIC-insured MDIs decreasing from 152 to 147. In support of its statutory requirement to encourage the creation of new MDIs, in 2022 the FDIC issued a Financial Institution Letter that outlines the process by which FDIC-supervised institutions or applicants for deposit insurance can make a request to be designated as an MDI.[33]

As significant new sources of private and public funding have become available to support FDIC-insured MDIs and CDFIs, the FDIC has supported these institutions access to this funding through regulatory changes34 and technical assistance training.

This week the FDIC is hosting an interagency conference with the OCC and the Federal Reserve to facilitate potential partnerships among FDIC-insured MDIs and CDFIs and large and regional banks supervised by the FDIC, OCC, and Federal Reserve. The conference will feature an overview of the new CRA rule and benefits for partnering with mission-driven banks. More than 100 FDIC-insured MDIs and CDFI banks are participating, in addition to over 65 FDIC-insured large and regional banks.

Conclusion

I appreciate the opportunity to provide you with an update of the FDIC's efforts to fulfill its core mission to maintain stability and public confidence in the U.S. financial system through its responsibilities for deposit insurance, banking supervision, and the orderly resolution of failed banks.

---

[33] FDIC Financial Institution Letter, FIL-24-2022, *Minority Depository Institution (MDI) Designation* (May 19, 2022) available at https://www.fdic.gov/news/financial-institution-letters/2022/fil22024.html.

[34] See FDIC, Federal Bank Regulators Issue Rule Supporting Treasury's Investments in Minority Depository Institutions and Community Development Financial Institutions, available at https://www.fdic.gov/news/press-releases/2021/pr21018 html.

The FDIC remains committed to engaging with the public, industry stakeholders, and members of Congress on the policies and priorities outlined in my testimony. I look forward to answering your questions.