

For Release Upon Delivery

10:00 a.m. May 15, 2024

Statement of Michael J. Hsu  
Acting Comptroller of the Currency  
Before the  
Committee on Financial Services  
United States House of Representatives

May 15, 2024

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 present the views of the President.

## Introduction

I am pleased to testify before the Committee on Financial Services to provide an update on the activities underway at the Office of the Comptroller of the Currency (OCC) to ensure that national banks and federal savings associations operate in a safe and sound manner, provide fair access to financial services, treat customers fairly, and comply with applicable laws and regulations.

The OCC charters, supervises, and regulates more than 1,000 national banks, federal savings associations and federal branches and agencies of foreign banks (collectively “banks”). These institutions range in size from very small community banks to the largest, most globally active banks operating in the United States. The vast majority of these institutions have less than \$1 billion in assets, while 55 have greater than \$10 billion in assets. Together, OCC-supervised financial institutions hold more than \$15 trillion in assets, representing nearly 65 percent of all the assets held in commercial U.S. banks.

My written statement provides an overview of the state of the federal banking system, an update on the OCC’s work to advance the four critical agency priorities that I set forth after becoming Acting Comptroller, and a description of recent key regulatory developments.

## State of the Federal Banking system

The overall condition of the federal banking system is sound. OCC-supervised banks in aggregate continue to have strong levels of regulatory capital and sufficient liquidity buffers, though risks from commercial real estate (CRE) and interest rate exposure warrant attention.

The OCC closely monitors the financial condition of the institutions it supervises and engages directly with them to ensure they are appropriately managing their risks. The OCC’s Semiannual Risk Perspective<sup>1</sup> highlights the critical elements of credit, market, operational, and compliance risks that banks are expected to manage. The OCC’s Bank Supervision Operating Plan for 2024<sup>2</sup> identifies the agency’s current examination

---

<sup>1</sup> See [OCC Semiannual Risk Perspective](#) (Fall 2023).

<sup>2</sup> See [Fiscal Year 2024 Bank Supervision Operating Plan, Office of the Comptroller of the Currency, Committee on Bank Supervision \(occ.gov\)](#).

priorities and highlights asset liability management, credit risk and allowance for credit losses, cybersecurity, operational risk, and consumer compliance risk, among others, as key areas of focus.

### Update on Agency Priorities

#### ***Guarding Against Complacency***

It is critical to build and maintain trust in the federal banking system that national banks and federal savings associations guard against complacency. As noted above, key areas banks are expected to manage include capital and liquidity levels and commercial real estate exposures. In recent months, regional and community banks have been particularly vulnerable to risks associated with CRE concentrations and exposures. At the same time, the OCC expects the banks we supervise to remain vigilant and focused on risk management. Banks need to successfully manage traditional risks, such as credit, liquidity, and interest rate risks, as well as prepare for emerging risks and tail risk events.

Another critical area for banks to address is operational resilience, which ensures that banks can adapt to and withstand or recover from disruptions. Both the number of potential disruptions and their possible impact are increasing, and may result from external events like natural disasters, malicious actors, pandemics, or global conflicts, or from weak internal systems, controls, or risk management. These disruptions may impede services, like payments, clearing, and settlement, or adversely impact systems or corrupt data. Ensuring that critical operations and banking services can withstand or recover from disruptive events requires planning, prudent investment, well designed systems, and regular testing. To this end, the federal banking agencies have been engaged in discussions to consider potential changes to the operational resilience framework.

#### ***Promoting Fairness***

Ensuring fairness and addressing discrimination in the federal banking system is an important OCC objective, part of our mission, and critical to safeguarding trust in banks. We remain committed to using all our tools to ensure the institutions we supervise are aware of and comply with their obligations to operate safely, soundly, and fairly.

This April marked the one-year anniversary of OCC guidance to assist banks in

managing the various risks associated with overdraft protection programs.<sup>3</sup> The guidance identified two practices— authorize positive, settle negative and representment—that can result in heightened risk exposure. It also highlighted sound risk management and pro-consumer practices that banks can employ to strengthen their overdraft protection programs. Since the beginning of the OCC’s heightened attention on overdrafts, the overdraft fees charged by OCC-regulated banks in aggregate have fallen over 40%, from \$6.5 billion in 2021 to \$4 billion in 2023.<sup>4</sup> Current supervisory data continue to show declines in overdraft fees quarter over quarter.<sup>5</sup> Among large banks, many have reduced fees and adopted pro-consumer features, such as grace periods.

Importantly, all OCC-supervised large banks have stopped assessing authorize positive, settle negative fees or insufficient funds fees and most have discontinued collecting sustained overdraft fees. OCC-regulated midsize and community banks have made or are in the process of making various pro-consumer changes to their overdraft protection programs. For example, most have eliminated representment fees or started offering de minimis grace amounts or grace periods. This includes those community banks that derive an outsized amount of revenue from overdrafts. Progress with regard to representment has been more challenging due to the critical role played by the core processors. We understand the largest core processors are taking steps that will allow banks to identify and address representment practices. As those plans develop, we will continue to encourage banks and the core processors to take steps to protect and empower consumers.

I also want to recognize the continued progress of the OCC’s Project REACH – or Roundtable for Economic Access and Change – which is focused on removing barriers to financial inclusion. Initiatives targeting credit invisibles have resulted in more than 100,000 new entrants into the mainstream financial system who now have credit scores

---

<sup>3</sup> See OCC Bulletin 2023-12, “[Overdraft Protection Programs: Risk Management Practices](#),” April 26, 2023.

<sup>4</sup> Call report data are available on the [Federal Financial Institutions Examination Council \(FFIEC\) Central Data Repository's Public Data Distribution](#) site. Call report data exclude overdraft-related service charges generated by banks with assets of \$1 billion or less as of the reporting quarter, which are not required to report overdraft-related service charges as a separate line item in their call report data. The data also exclude overdraft-related service charges generated by all credit unions.

<sup>5</sup> Banks under \$1 billion in assets do not report overdraft fee income on the call report, so the data presented do not include those banks.

and access to credit. Investments of more than \$500 million in Minority Depository Institutions (MDIs) have resulted in increased partnerships, exchange programs, training and capital. On May 29-30, 2024, the OCC will host the Project REACH Financial Inclusion Summit at our headquarters in Washington, D.C. to discuss progress made on several workstreams, as well as to launch new initiatives to increase economic mobility within financially underserved and under-resourced communities.

In February, the Federal Financial Institutions Examination Council (FFIEC) released a statement on “Examination Principles Related to Valuation Discrimination and Bias in Residential Lending,”<sup>6</sup> which provides principles for the examination of institutions’ residential property appraisal and evaluation practices to mitigate risks that may arise due to potential discrimination or bias in those practices and to promote credible valuations. The OCC will consider these principles in the context of consumer compliance and safety and soundness examinations when assessing banks’ residential real estate valuation programs.

### *Adapting to Digitalization*

Banks’ relationships with third parties, including financial technology (fintech) companies, continue to expand. The use of third parties has significant potential benefits, but poor third-party risk management can hurt consumers, weaken banks, and contribute to an unlevel playing field.

Last year, the OCC and other regulators jointly issued “Interagency Guidance on Third-Party Relationships: Risk Management,”<sup>7</sup> to remind banks of their responsibility to operate in a safe and sound manner and in compliance with applicable laws and regulations regardless of whether their activities are performed in-house or outsourced. The guidance also recognizes that not all third-party relationships reflect the same level of risk and thus do not require the same level of risk management.

Effective risk management of third-party relationships is challenging for financial institutions of all sizes, but we recognize that community banks, including MDIs and Community Development Financial Institutions Funds (CDFIs), may need to navigate

---

<sup>6</sup> See: [FFIEC News Release](#) “FFIEC Issues Statement on Examination Principles Related to Valuation Discrimination and Bias in Residential Lending.”

<sup>7</sup> See [OCC News Release 2023-53](#), “Agencies Issue Final Guidance on Third-Party Risk Management.”

additional hurdles. Last month, the OCC, Board of Governors of the Federal Reserve System (Federal Reserve), and the Federal Deposit Insurance Corporation (FDIC) sought to address this by publishing “Third-Party Relationships Risk Management: A Guide for Community Banks.”<sup>8</sup> This guide provided community banks with examples of innovative approaches to conducting due diligence and assessing new fintech companies.

The OCC expects banks to approach and manage the use of artificial intelligence (AI) consistent with principles of safety, soundness, and fairness. To date, banks have generally approached machine learning prudently across a range of use cases, though we are starting to see a notable increase in the number of generative AI pilots at some of the larger banks we supervise. AI has the potential to enable improvements across a range of domains, but it also has the potential to perpetuate and exacerbate the biases, discrimination, and unfairness that are embedded in the data feeding AI systems. To guard against this, banks need to have appropriate oversight and governance of the models they use. In addition, banks must be attentive to the risk of AI-enabled fraud.

The OCC also has focused on exploring the tokenization of real-world assets and liabilities. In contrast to crypto, tokenization is driven by solving real-world settlement problems and can be developed in a safe, sound, fair, and compliant manner. Earlier this year, the OCC hosted a public symposium on tokenization to discuss developments, explore legal and risk management foundations, and promote public debate. The symposium sparked robust discussion on these issues and highlighted the innovative potential of tokenization.

### ***Managing Climate-Related Financial Risks***

Consistent with the OCC’s safety and soundness mandate, the agency has continued to be engaged with the large banks it supervises to better understand their climate-related financial risk management capabilities and their efforts to identify, manage and control these risks. In 2023, the OCC initiated discussions with banks with over \$100 billion in total assets to understand their climate-related financial risk management programs.

---

<sup>8</sup> See [OCC News Release 2024-46](#), “Agencies Issue Guide to Assist Community Banks to Develop and Implement Third-Party Risk Management Practices.”

In general, the OCC has observed that large banks have been making progress to incorporate climate-related financial risks into their risk management frameworks and policies. In light of the withdrawal of insurers from higher-risk markets and rising insurance costs, we have recently observed that large banks are considering the impacts of changes in insured limits or deductibles, premium increases, and lack of insurance coverage in credit risk assessments for commercial and residential real estate portfolios in their risk management work. The OCC is committed to open dialogue and constructive engagement with the large banks it supervises around climate-related financial risk management.

#### Update on Other Regulatory Initiatives

The OCC has been engaged in developing and finalizing several proposals to promote the resiliency, resolvability, and inclusiveness of the federal banking system.

#### ***Revisions to Capital Rules for Large Banks***

The OCC remains actively engaged with the Federal Reserve and the FDIC to consider all stakeholder comments received in response to the July 2023 proposal to update the risk-based capital requirements applicable to large banking organizations with significant trading activity. Establishing an appropriate capital framework that adequately captures all of the material risks of these large banks is critically important to the health of the nation's financial system, and the agencies must get it right. The OCC has welcomed the broad range of thoughtful comments received and continues to approach this rulemaking with an open mind.

#### ***Community Reinvestment Act Final Rule***

Last October, the federal banking agencies issued an interagency final rule implementing the Community Reinvestment Act (CRA), which was enacted in 1977, to prevent redlining and to encourage banks and savings associations to help meet the credit needs of all segments of the communities in which they operate, especially low-and moderate-income (LMI) neighborhoods and individuals.

On February 5, 2024, trade groups filed a lawsuit in federal court against the

OCC, FDIC, and Federal Reserve, seeking to block the implementation of the final rule. On March 29, 2024, the presiding district court judge issued a preliminary injunction that currently prevents the federal banking agencies from enforcing the final rule and extends the effective and applicability dates of the final rule while the injunction is in place. The agencies filed a notice of appeal of this injunction with the US Court of Appeals on April 18, 2024, which is currently pending. At this time, the OCC continues to assess banks' CRA performance under its previous regulatory framework.

### ***Business Combinations Under the Bank Merger Act***

The OCC is committed to working with our interagency peers to update our bank merger analytical frameworks, which includes collaboration with the Department of Justice (DOJ) on the competition prong of the Bank Merger Act. This work is ongoing.

In addition, on January 29, 2024, the OCC released a proposal to increase the transparency of the standards that apply to the agency's review of business combinations involving national banks and federal savings associations. The proposal would amend the OCC's procedures and add a policy statement summarizing the principles the OCC uses when it reviews proposed bank merger transactions under the Bank Merger Act.

To provide greater clarity to financial institutions and transparency to the public, the proposed policy statement would outline general principles the agency uses in its review of applications under the Bank Merger Act and the OCC's consideration of the financial stability, financial and managerial resources and future prospects, and convenience and needs factors. The policy statement would also discuss the criteria informing the OCC's decision on whether to hold a public meeting on an application subject to the Bank Merger Act. We recently extended the comment period on the proposal until June 15, 2024, and we encourage all stakeholders to provide comments.

### ***Incentive Compensation***

On May 6, the OCC, FDIC and the Federal Housing Finance Agency (FHFA) approved a notice of proposed rulemaking (NPR) to fulfill Congress' mandate through the Dodd Frank Act to address excessive incentive compensation and compensation that could lead to material financial loss. The NPR is based on the proposed rule text issued in

2016, which was supported by six federal agencies, with a new preamble that acknowledges developments and supervisory learnings and is intended to initiate renewed public dialogue on this topic. While the NPR has not been adopted by all six agencies to inform a joint rulemaking as required by statute, we are accepting comments on the proposal and look forward to continuing to engage our interagency peers and the public on how we can most effectively curtail problematic incentive compensation practices.

### The OCC Supports Community Banks and Minority Depository Institutions

More than 80 percent of the institutions supervised by the OCC are community banks and federal savings associations. These institutions play a crucial role in providing consumers and small businesses with essential financial services and are a source of credit that is critical to economic growth and job expansion.

We recognize that small institutions face challenges as they work to stay competitive in today's increasingly high-tech financial marketplace. Digitalization has put a premium on online and mobile engagement, customer acquisition, customization, big data, fraud detection, artificial intelligence, machine learning, and cloud management. These activities require expertise and economies of scale that many banks, especially community banks and MDIs, may not have access to. We are also aware of the impact of fraud on community banks and in particular, delays in receiving timely responses to their requests for reimbursements associated with fraudulent returns. The OCC recently initiated a process to receive information from community banks about delays in reimbursements resulting from check fraud so we can determine a supervisory response.

Earlier this year, the OCC, Federal Reserve and FDIC published the first notice requesting comment on specific regulations pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). EGRPRA requires the agencies to review their regulations every 10 years to identify outdated, unnecessary, or unduly burdensome regulations applicable to insured depository institutions. This review will include a series of federal register notices as well as public meetings inviting stakeholder comments for agency consideration. I look forward to a robust EGRPRA process and support a fulsome review of our regulations with the goal of eliminating

unnecessary regulatory burden on community banks.

### Conclusion

I am committed to ensuring OCC-supervised banks operate in a safe, sound, and fair manner, meet the credit needs of their communities, treat all customers fairly, and comply with laws and regulations. As we work to ensure that the federal banking system remains a source of strength to the U.S. economy, we will continue to advance key agency priorities to ensure the federal banking system is well positioned to respond to community and consumer needs well into the future.