Office of the Comptroller of the Currency
Minutes of the Meeting of the
Mutual Savings Association Advisory Committee
March 5, 2024

The Mutual Savings Association Advisory Committee (MSAAC) was convened for a virtual meeting at 8:30 a.m. on March 5, 2024.

In accordance with the provisions of the Federal Advisory Committee Act (Public Law 92-463), the meeting was open to the public from 8:30 a.m. to 2:30 p.m.

Advisory Committee Members Present

Peter Abt, David Barksdale, Paul Gilbody, George Hermann (virtual), Thomas Newbern, David Reynolds, Thomas Rudzewick, Steven Sloup, Brian Smith (virtual) and Samuel Wilkinson

OCC Staff Attending

Maria Adams, Jason Almonte, Charlotte Bahin, Julie Blake, Michael Brickman, Michael Chunn, Beverly Cole, Christopher Crawford, Vonda Eanes, Anna Fee, James Gallagher, Daniel Grantham, John Harootunian, Allison Hester-Haddad, Cristina Im, Anne Kerttula, André King, Ernie Knott, Mariya Komartsova, Christopher McBride, Carlo Martinez, Paul Moloney, Erica Onsager, Christopher Sadej, Demetria Springs, David Stankiewicz, Johnny Stanley, Troy Thornton, Tiffany Trotter

Public Meeting
Introduction and General Remarks

Michael Brickman, Deputy Comptroller for Specialty Supervision welcomed the members of the OCC's Mutual Savings Association Advisory Committee to the meeting. He provided a brief overview of the agenda for the day and introduced Daniel Grantham to provide the economics update.

Economic Update

Daniel Grantham, Senior Financial Economist in the OCC's Banking Condition unit gave an economic update.[1] He said that the Advisory Committee members' questions help him develop the discussion of the trends. When discussing the agenda shown on second slide, he noted that 2023 defied expectations. In 2023, all expectations were that a recession was imminent, however because of continued consumer spending, strong labor market rising income, there was no recession.

The consensus forecast of a group of professional economists provides an outlook for the economy for the next two years. Last year, the forecast projected that there would be a one

[1] The references are to the slides in the presentation found on the MSAAC page of OCC.gov.

hundred percent chance of recession. He said that over the past several quarters the contributions to real GDP were extremely strong, especially in the third and fourth quarter. These contributions are broken out by the different components that contribute to the growth, consumption and investment, the pinnacle pieces of the US economy. GDP grew almost five percent in the third quarter and over three percent in the fourth, which is much stronger than over the last 15 years.

Looking forward, Mr. Grantham described the expectation based on the blue-chip consensus for much more moderate growth at around two percent real GDP growth. He said that 2023 was an outlier in terms of strong economic growth. He explained that the growth over a longer time period, for example the second half of the 20th century, GDP growth of around three and a half percent a year on average was extremely fast, especially when compared to the experience after the great recession of 2008 to 2012, where annual GDP growth was a little under two percent.

When this is extrapolated over a number of years, the difference in the growth rate makes a huge difference in the level of economic output. The two and a half percent growth for the full year in 2023 is faster than what was experienced over the last 20 years. He explained a growth theory in which increases production in three main ways. More people working or working longer hours, more or better capital so people are more productive, and accounting for those two factors, the difference would be an increase in technology.

From 1950 to 2007, the growth was broad based across these three metrics. There was an increasing labor market, both from women coming into the labor force as well as the baby boom generation. There was a lot of investment in technology and technology innovations that helped increase productivity. One of the factors that led to the slowdown during the Great Recession was that the demographics are a lot different. The US is older which is constraining the growth in the labor market. Capital investment was a lot lower than it was during the 1950 to 2007 period and the technology portion is lower than it was during the second half of the 20th century. During 2023, a lot of the growth experienced can be contributed to the rise in the labor market.

He turned to slide five and noted that the growth in the labor market is surprising. In 2023, 2.8 million people entered the labor force. He discussed the demographics of the number and noted that the female participation rate is at an all-time high. The likelihood that the labor force could grow another 2.8 million in 2024 is unlikely. There is not a growing population that would support a growing labor force that could potentially increase the GDP just from the labor force.

The numbers of teenagers have dropped. In the past, about 60 percent of teenagers were engaged in the labor force. Today, it is less than 40 percent. Now, conversely the 55- to 64-year-old persons are at all-time highs. Going back to 1948, the plus 65 group has risen over the last 20 or 30 years, but is down from where it was in 1948. If the labor force participation of 16- to 19-year-olds returned to close to 60 percent, there would be another three and a half or 3.6 million people back into the labor force.

The likelihood depends on what happens with wages and other opportunities. Even the number of 65-year-old persons and older is about eight percentage points lower than its historical peak. If the labor force increased with the addition of that group, there would be an additional 4.6 million people. He said in a few slides, he would talk about how the labor market cooled. It

remains historically tight. He asked whether the Advisory Committee members experienced it being easier to attract or gain talent.

An Advisory Committee member noted that there is a competitive market for younger people coming out of universities looking for a career in banking and he asked whether there is a reason for the precipitous drop in that age group from 1996 to the present. Mr. Grantham replied that it has been explored, but nothing definitive has been found. The increasing cost of college and the time it takes to get in may be steering some of this. He said that the teenagers in his neighborhood are not working. They have many extracurricular activities. It is hard to say what really drove the drop.

An Advisory Committee member noted that his bank finds it tough to hire people, they try to do workforce development. He said there are a lot of manufacturing companies in his market, and those companies are working hard to ramp up, but it is still a tight labor market. He said that he is surprised by the numbers of people that were added to the labor market in the last year.

An Advisory Committee member said that his bank has been trying to hire an IT person for four or five months and it has been hard. He reported that they are getting traction in hiring entry level tellers, but the IT and other specialty areas are tough.

Mr. Grantham said that there has been a lot of talk about the Fed Funds rate and the current interest rates being restrictive and maybe impeding or causing a recession. From an economist's point of view, some of the things that they look at to put the economy into perspective, would suggest the economy is actually overproducing or overheating.

He said that is what is known as the US annual output gap or the potential GDP. This is an estimate of what the economy can produce without being inflationary. It has been revised recently, but looking above the line, it would suggest that the US is producing beyond the economy's long-term capacity or potential and that would suggest overheating. Mr. Grantham said that he thinks it is a little bit more apparent in the labor market.

The two metrics would suggest the economy is doing quite well and maybe a little too well. On slide eight, real incomes increase in the three charts as more people are working. These people are earning higher real average hourly earnings. Even adjusting for inflation, the actual wage rate is higher. All of which leads to a boost in real aggregate incomes. Americans have more money at their disposal to spend. Over a longer term, people tend to spend a relative share of their incomes. As the aggregate amount of money in the US increases, it is natural to see a correspondent increase in spending.

Mr. Grantham turned to slide nine and noted that the chart on the far left shows a rise in spending, but spending is rising in line with incomes. He said that if real consumption is indexed, taking out the impact of inflation and compared to disposable income, which is the amount of money earned minus taxes. These two lines grow together as people earn more money they tend to spend a consistent share of it. The real deviation in 2020 to 2022 is where the economy shut down and there was a tremendous amount of stimulus in the US. There was less opportunity to spend it, but for the most part, historically speaking, consumption rises along with disposable

income. Disposable income increases as more people work and earn a higher real wage, all of which is quite positive.

Mr. Grantham said that one of the things that is frequently highlighted is the decline in the personal savings rate. It is lower at four and a half percent than the 30-year average. He said that factors to consider are that the personal savings rate is a flow measure. It is how much is being saved that month. Last year, four and a half percent was saved if the stock of liquid assets available to households is looked at. The data in the chart on the right come from the Federal Reserve and it shows the checking account balances for households relative to their disposable income. At the end of 2023, households had about 20 percent of their disposable income in cash and checking account balances.

Mr. Grantham said that if money markets were added, which increased as interest rates increased, it is about 40 percent. He said that data are available that break this out by income level. Even lower and moderate-income levels have about 20 to 30 percent higher checking account balances than they did in 2019. It is something that is being watched as income rises. Where income rises the most is both at the bottom and at the top end of the wage scales. Even the lower income consumers have seen a disproportionately larger increase in their real wages than have the median income persons.

An Advisory Committee member said that in his bank, consumers are not keeping balances in checking accounts, but they buy CDs. He asked whether as consumption continues to grow to meet elevated levels of liquidity, household cash, is that a hangover from the COVID stimulus money that has not been spent. Mr. Grantham said that it is if the total amount of stimulus is included, it was about 50 percent of GDP. It is still out there. Particularly for lower income consumers, a lot of it was targeted stimulus. They have spent about 30 percent of it, but it still leaves about 30 percent above where they were in 2019.

An Advisory Committee member asked whether there is any arbitrage. He asked whether people moved out of checking accounts. He has heard that that there is an increase in Treasury holdings among households. Mr. Grantham said that there has been competition with Treasuries. He said that is not so common now, but money moving to CDs and then when the CDs reprice it squeezes the net interest margin. It was a record year in fee income because everybody was paying the fee so they could break a one percent CD and jump into a five percent CD. Banks collected the fees and did not let the customers walk. Mr. Grantham asked Mr. Moloney what he was seeing in the smaller banks, they seem more sensitive this cycle than in the last couple of cycles.

Mr. Moloney agreed that there is more sensitivity to pricing than in the past. An Advisory Committee member said that even though rates have flattened out, he is seeing the bank's cost of funds increase. The consumer catches up to that and tries to reposition themselves from a noninterest bearing into interest bearing account via money market or CD. He also said that competition for deposits is not as much from other banks as it is from uninsured entities and credit unions.

The Advisory Committee member asked whether the personal savings rate captures 401K's and other retirement savings, because when he looks at the employees in the bank, most of their savings is tied to either deferred compensation or 401K's. Mr. Grantham said that the money in retirement accounts is not captured in the savings rate. He said that that is another reason that it gets attention, but he does not think it is quite as meaningful an indicator as a lot of the focus suggests. When household balance sheets overall are reviewed, there is less debt and more assets. Some of the decline could be demographic. People are older, there are more assets. People have healthier balance sheets when cash levels are this high across the board, it would make sense to not save as much month to month.

An Advisory Committee member asked where the levels of liquidity from couple years ago went. He said he thinks that consumers are using that money to get by on a day-to-day basis. He noted that there is a lot of money in the system. One of the big differences this cycle versus the government's response in 2009, is that a lot of the money was sent directly to households that have a higher propensity to spend.

Mr. Grantham said that he did not include it in the presentation but wage growth across income tiers is rising and incomes are rising. He said that is lost in the overall story. Those factors are still relatively healthy for consumers as long as the job market remains tight. On slide 10, the metrics or the newspaper stories have a narrative that there has been a dramatic growth in credit card balances and consumers are substituting the debt as a way of making up for lost income or rising expenses. When the data are reviewed, at least from the OCC's perspective, that is not the story. Credit card balances have risen 20 to 30 percent, inflation has risen, 20 to 24 percent, depending on which metrics are used.

Mr. Grantham said that as an economist nothing is better than looking at long time trends relative to something. The natural thing that they like to look at is relative to incomes. Credit card debt as a share of disposable income has risen over the last 18 months. But historically the red line chart on the left is still relatively low, especially compared to the early 2000's. The utilization rates have gone up, but historically they are still relatively low. A lot of the growth economists have seen is on a loan-by-loan basis, the chart on the far right comes from the Philadelphia Fed and it uses loan level data. Revolving balances have grown but the numbers of consumers who pay off their balances every month have increased, at least as a percentage of transactions.

He said that they look at the propensity to use some of these credit products that could potentially make up for a shortfall in income or rising living expenses. There is no evidence to date that would suggest that consumers are doing that in mass. There may be smaller segments of the population who are, but it is really in credit cards where there is large growth. He said that it has to do with today's rising cost of living. People are spending a commensurate amount above, or, in line with inflation. Debt levels have come down quite a bit. On the mortgage side refinancings have all but disappeared. He asked the Advisory Committee members whether they are seeing anything in terms of loan demand, either in credit cards, autos, personal loans, anything that would make them suggest that consumers maybe overstretched and looking for a lifeline.

An Advisory Committee member said that his bank does only real estate loans and in his market the housing costs are high. The inventory has not come back and the cost of living between that and the increase in the cost of housing has completely frozen the residential market. The entire residential market, not only in the owner-occupied, but even on the investor-owned one- to four-family loans. There is a big population of investors that is scooping up the one- to four-family residences throughout New York. Other Advisory Committee members agreed. Mr. Grantham said the Fed is increasingly focused on the cost of housing, particularly for rental properties. Advisory Committee members said that anecdotally, they hear that rents have moderated, but not in all locations. Local laws are putting pressure on free market apartment rents and people are migrating. Also. there is a potential for payment shock. The majority of mortgages today are fixed-rate, but there has been an explosion in both real estate taxes as well as the cost of personal insurance and property insurance.

Advisory Committee members also said that states and localities have eliminated all of the incentives to build new housing. Many developers have moved to other locations to do new work. The cost of materials to build puts plans on building homes on hold for a lot of consumers.

On the multifamily side, developers are moving to other areas and that has helped stabilize at this point. The question is whether with all the new building on the rental side, new construction is going to be able to be absorbed. It has continued to be absorbed, but it almost defies logic at this point.

An Advisory Committee member said that there continues to be migration from urban areas to more suburban or rural areas because the remote work activity is still strong. Office buildings in Manhattan have tremendous vacancy levels. Employees do not have to come to the office, they can move further away where housing is more affordable, or if they only have to commute three days a week as opposed to five, they move.

An Advisory Committee member said that a lot of people are moving into his area from adjacent states as well other parts of the county. Part of the reason is that insurance is harder to get, and the costs have increased so they move to where it is more affordable. There is still a supply and demand problem, but the prices have not gone through the roof like they have in other markets. The builders are pricing everything off Covid pricing, and they are not able to get any supplies. When there is supply, prices are increasing. He said that his bank is making mortgages and writing checks for cars. He said that he wonders where all the money is coming from. It may be Covid money.

Another Advisory Committee member said that in his area there is a plethora of vacant office buildings, especially "class a" office space. Also, there is a million square feet of vacant office space, and there is a huge lack of supply of rental units and housing. Municipalities, governments and builders are trying to figure out how to transition this office space to apartments or homes. There are nice buildings and great areas that would be in high demand if they were apartments, townhouses, or condos. But the cost to transform them is really difficult. It is cheaper to build a new building down the street. Another Advisory Committee member said that there is no

warehouse or industrial space at all available in his area. The rates that the people are paying for that space have almost doubled.

Mr. Grantham turned to slide 11 and said that as he has alluded to throughout, from a very high-level households have been insulated from higher rates this cycle. He said that it has to do with the lack of adjustable-rate mortgages that were originated prior to 2020. The total share of adjustable-rate debt as a percent of total household debt is relatively small, especially on a historical basis. There has been a lot of de-leveraging over the last 20 years of household balance sheets, debt to income ratios, both for as a total as well as across the income spectrum. Household balance sheets are a lot stronger than they have been, and that leads to more resilience.

On the consumer side, a labor market shock would cause pain, but he said that it would be less than what has been seen in previous cycles because of the strength of the consumer. He asked whether Advisory Committee members have started to see any consumer deterioration. He said that there has been an uptick in credit card delinquencies as well as auto delinquencies, at similar levels that were seen pre-covid. The trend is going up. He asked whether Advisory Committee members are starting to get nervous or concerned about the uptick.

Advisory Committee members said that they are not concerned at this point. They continue to see excellent credit and people paying on time across the board in consumer residential mortgages. In commercial loans they have a little bit of concern, but if customers are lagging a little bit to make those payments and a phone call or two and gets the payments in.

An Advisory Committee member said that on the origination side in real estate, the thresholds are much higher and that the bank turns down a lot more applications than they have in the past. Customers cannot qualify and the bank's processes have become more front loaded to determine whether an application will be approved before it goes through the full system. That freezes the refinance and the purchase markets because borrowers cannot qualify. He thinks that consumers are being more careful with the debt that they do have. He said that it is another reason why they are not coming to get mortgages. Another question is whether there has been a change in the amount of cash used to purchase for homes. Inventory continues at all-time lows and with where rates are right now, is surprising that there is a lot of cash out there buying.

An Advisory Committee member said that he has seen an abatement in the bidding wars where someone thinks about putting their house on the market and they receive four cash offers in an afternoon. That activity has slowed down. He said that he thinks of his customers during the low interest rate environment, and asked whether there is a percentage of the market that has mortgages at low rates right now. It is like cash in the bank and their payments are low versus what they were over a 30-, 40-, 50-year period. Consumers have locked in low fixed rates and the propensity to move has diminished quite a bit. The only areas, at least geographically, where there has been an increase in homes for sale inventory has been in the southeast. There has not been a correspondent decrease in home prices that might be expected to see with a rise in inventory.

Mr. Grantham said that has heard that a lot of people who have been purchased homes in the last year at the higher rates have stretched their income with the intention to refinance the loan at a lower rate in a year or two when the Fed cuts rates. He turned to slide 12. He said that in terms of rates, there has been some cool down in the labor market, but historically, the labor market still remains extremely tight. There are two measures, both job openings per unemployed person. There are more job openings today than there are unemployed people and that has come down from when there were over two positions per unemployed person. If he looks at when this data started in 2001, the levels are where they have not been seen before. While the trajectory is good, the overall level remains incredibly tight. As it relates to hourly earnings there has been a cool down or a decrease in the amount that wages have been increasing, but it is still higher than four percent and is not in line with the Fed's target of a two percent targeted inflation rate. These measures are closely watched both by the Fed and the markets for an indication of where inflation could be headed. Progress has been made as it relates to inflation. Slide 13 shows the Fed's preferred inflation measure. There are two that are frequently discussed, the CPI, but the Fed focuses more on core PCE, as they think it is more representative.

They think of the consumer experience with inflation. The blue line measures the 12-month percent change, it has dropped quite a bit, it was close to six percent and is now closer to three percent, but it is still above the Fed target. However, progress has been made over the last month or two. There are some inflation reports that have surprised the markets. On the upside, inflation came in a little hotter than what was originally anticipated. Slide 14 shows that the market is pricing in fewer Fed rate cuts in response to some of the latest inflation readings. Mr. Grantham focused on the chart on the right. The dark blue line is what the Fed projects and puts in their economic forecast.

The chart shows a comparison to the futures markets at different points. The green line would be the futures markets for Fed funds, going back to the middle of January. The middle of January was the most exuberant period, at least in terms of rate cuts, the expectation in the market was seven Fed rate cuts this year, which is quite dramatic. Lowering the Fed funds rate from five and a quarter to 3.6 percent. Chairman Powell's FOMC press conference tamped some of those expectations and the red dotted line shows the expected Fed rate cuts dropped from seven to four percent. The January CPI came out and further reduced the market's expectations for Fed rate cuts. There has been a decline in the expectation for where the Fed Funds rate will end the year, from extremely exuberant for seven rate cuts to where it is today at two or three.

Mr. Grantham said that it would be interesting to see what the FOMC does later in the month. He said that there is a little bit less exuberance in terms of market Fed funds rate cuts. He thinks that it has to do with inflation as well as the relative strength of the US economy. Because the fourth quarter GDP number came in strong it is an early indication for a strong first quarter GDP as well. At these rates, the Fed is typically inclined to cut rates if they think the economy needs a boost or that they are at too elevated levels. But the economy is quite resilient at these higher levels of interest rates. To conceptualize an appropriate level for the Fed Funds, the main rule in the public domain would be the Taylor rule.

Slide 15 shows how the Taylor rule looks at current inflation relative to the Fed's target and looks at how the economy is performing and comes up with a suggested rate to both achieve the Fed's full mandate of stable prices as well as full employment. Looking at data through the end of 2023, the suggested Fed Funds rate based on the original Taylor rule would be six percent. There are different variations, and it is possible to come up with reasonable estimates. The reasonable estimates through the end of 2023 would range to a Fed Funds rate at about four and a half percent to seven and a half percent. It is in line with expectations. If the data keep coming in as hot as it has been, Fed rate cuts will become less likely. Given some of Chairman Powell's testimony, both to Congress as well as the press conference, indications are that they are willing to hold here for longer than anticipated even six weeks ago. He asked the Advisory Committee members whether they think the Fed will cut rates at least two or three times this year.

The Advisory Committee members estimate that there may be two rate cuts. An Advisory Committee member asked whether the Taylor rule is still applicable. He said that it is as close today as it has been since 2015. Mr. Grantham said that the Fed continues to include the Taylor rule in their monetary policy report that is submitted to Congress twice a year. He said that he thinks that internally within the Fed it has been less of a metric that they have tracked. Historically looking at the Taylor rule, inflation has been within these bounds.

There has been a lot of debate and he said that the surprise this cycle has been that rates have remained north of five percent. On the consumer side, there has not been a slowdown in terms of consumer spending wage growth. There has been very little impact on the household side from rising rates and even some of the traditional metrics, for example residential fixed investment. It is a smaller share of GDP today than it has been historically, but because there is a structural housing shortage, there is not a real decline in residential fixed investment either. It may be less applicable. The Fed might say it is when they provide their projections. A lot of the market would say the 5.3 percent is restrictive.

He said that one of the central tenets within economics is that people respond to incentives. There have been large increases in real wages. Was that enough to entice people back? Or was it necessary? The big surprise has been the dramatic increase in the labor force, and he would not expect that to continue into next year, but he did not expect it last year either. If wages continue to increase, maybe more people will be enticed back into the labor market, which will boost GDP and some of the employees affected by the Covid years who were sitting on the sidelines may come back.

There have been so many more regime or structural breaks over the last 10 years. A lot of it is untraditional. A 50 percent stimulus both from the Fed and Congress is quite unusual. Where it was targeted was unusual and monetary policy has changed. There are a lot of social demographic changes, and there are many different changes that continue and it is hard to try to isolate the different factors that may lead or contribute to those factors.

Slide 16 provides a conclusion of the expectation for the consensus, which is almost always wrong, that the GDP returns to the two percent trend. The three and a half percent annual growth rate would solve a lot of problems, both in terms of the budget deficit as well as some other

structural factors in the economy. He thinks the real takeaway is that the Fed's battle of inflation may not be over. There are some areas where there are still challenges. Core PCE takes out food, energy and housing, there has been some reluctance or some stickiness for inflation coming down. That is an area to continue to watch. The hardest part of the Fed's battle was not getting from eight to four percent or six to four percent. It is going from that four percent inflation rate to two percent. There might be rates higher for longer. He said that he has heard that is has plateaued. In concluding, he asked for comments or questions on the consensus forecast.

Liquidity Update

Mr. Brickman introduced Chris McBride, the OCC's Director for Treasury and Market Risk in the Bank Supervision Policy line of business. Mr. McBride noted that 2024 is a much different year than 2023. He said that a year ago, he thought the SVB, Signature Bank and First Republic Bank failures were the start of another crisis, and a year has made a difference.

He said that he would like to talk about liquidity and specifically what the OCC is seeing. He said he would also talk about interest rate risk and general market risk. He said that the regulatory agencies have been focused for the past probably 18 months or so on the stability of the funding base. Depositor behavior showed some interesting things over the past couple of years. In the past, pre-pandemic, there was a general malaise in the market. There were low rates for a long time where everybody was faced with keeping the lights on.

Mr. McBride noted that any yield that banks could pick up were beneficial and the deposit base was remarkably stable. It had not changed much over the prior 10 years since the previous crisis. There was a preference for bank funding and stability. Then the pandemic occurred and banks experienced things the industry had not been through before. For example, all the money that came into the system pumped up uninsured deposits. Then the failures occurred in March 2023 and the industry saw what a difference 15 years makes. The deposit base is one that banks took for granted, but after the dislocation that happened in March 2023, and the covid issues occurred, banks had to take a look back at the deposit base.

He said that one thing that the OCC can talk about is the non-maturity deposit assumptions that the agency now puts out every six months to highlight, provide feedback and peer review where banks are in relation to peers with non-maturity deposits. But there had been a general influx of depositors that displaced other sources of funding, the Federal Home Loan Banks started lending to insurance companies and some REITs and doing other things with their funding to make money, because banks' deposit base had been so strong. In March 2023, everything changed with the rate structure in the market and banks needed to replace funding.

He noted that for mutual savings associations, there are deposit concentrations as well. One of the reasons for the major concentrations is that depositors are "owners." "Owners" is a loose defined term, but there is concentration. In SVB's base, there were concentrations in IT companies and in venture capital. The entities were interconnected. Selling the investment portfolio of the bank caused other entities to run. The concentration issue is what the OCC has looked at lately, especially through the National Market Risk Committee.

He said that concentrations on the asset side related to lending are often studied, but there is also concentration or concentrations in the depositor bases. Banks still have that risk. The OCC talks concentration in the Liquidity Handbook and where banks are seeing how it plays through the rest of the funding structure. Additionally, there was an uninsured deposits issue. Mr. McBride asked the Advisory Committee members whether they have large numbers of uninsured deposits. He said that he assumes there are some, but not to the extent that SVB had them.

Uninsured deposits were one of the biggest concerns in the recent failures and the OCC has looked at trying to get behind the uninsured depositors to see where they are because banks typically think of core and non-core deposits. The agency looked at friction and friction less deposits. Because if the bank has a deposit that has friction inherently in its payroll, a bank cannot move payroll money overnight. There is a different stability function than would exist if the deposits were friction less. Another issue that has more friction but has more ability to be pulled is escrow accounts. There are some issues going on in the market right now related to escrow monies, and similar to that is public money.

He said that one thing the OCC looked past was the ability of deposits to move quickly. When the agency looked back at what happened with SVB, it looks back at the non-maturity deposit assumptions to figure out how did those foreshadow or correlate to movements. Because bankers know their deposit risk of repricing better than the OCC does. That is why the agency likes to get bank's non-maturity deposit assumptions to see what is going on in them.

Mr. McBride said that deposits are one of the OCC's bigger issues because of their stability. Mutual savings associations have different entanglements than other banks. The depositors consider themselves "owners" of the bank, and it is interesting to talk to mutual savings associations because of the different expectations of their depositors and borrowers as well. An Advisory Committee member said that when SVB and Signature failed, new depositors came to his banks and told him that they would put their money in the mutual bank because they know the mutual is not going to be in the middle of the crisis. As a mutual, the ownership structure gives a sense of security for the depositors, knowing that if management is of the same mindset with a conservative outlook on growth, the bank will survive the type of debacles that happen.

The Advisory Committee member said that when banks see deposit rates that shifted so wildly over the last four years from covid and stimulus money, he finds it a stabilizing factor now that rates are back to normalized levels. He said that he thinks it is important for examiners to understand that the increases that occurred in those deposits were an anomaly. He said that now that banks are back to more of a stabilized deposit flow, that although they have plenty of competition, management of the institution is important. The mutual model does not look for a huge windfall, he said that mutual bankers kept the money in overnight until it left. That is a different scenario than most examiners see.

Another Advisory Committee member echoed the thought. He said that one thing mutuals have is legacy deposits. When the bank has been around for years, there are legacy deposits, and liquidity is back to what it was pre pandemic. He said that from a regulatory perspective they manage the lines that are available and make sure that collateral is in place. He said ideally they

want to be a hundred percent invested and have the liquidity the bank needs. He noted that in discussing uninsured deposits they make sure they have more than enough availability in lines to cover uninsured deposits. He said that he does not necessarily get the feeling from the OCC that they are getting the credit for having the lines and managing liquidity in the same manner as they did in a pre-pandemic situation.

Mr. McBride referred to the Advisory Committee member's comment that the deposits came in after the failures of larger banks and he said that one thing the OCC has been seeing is those friction deposits. He explained that that is a new term. It means that banks cannot just immediately move the deposits. For example, a depositor may have money at a large bank, and within 24 hours, they can pull it into a different bank. There is nothing keeping it there. There is no escrow account, there is no payroll that the depositor has to make. That is the depositor's money. The term is not an official OCC term.

Mr. McBride asked the Advisory Committee members whether the competition from the rate environment impacted their depositors. Did the banks see customers chasing rates or did they deposit funds and forget them, and depositors understood the mutual that they bank with. An Advisory Committee member said that it depended on what they saw. If the rate chasers, with time deposits started to move out, they slowed down lending. He explained that is a benefit mutuals have with a tremendous amount of capital. They do not have to chase the rate or the markets. Mutuals can be much more selective and more controlled on how they take mortgages in and then they do not have to worry about the deposits going out as much.

An Advisory Committee member agreed that is the key to the mutual model. They are not chasing money and what is troubling is when he sees competitors that chase mortgages or try to find funding opportunities through deposit rates, they get themselves into trouble. He also mentioned that credit unions grow just to grow. It is about controlled growth. It is about controlling expenses, so banks understand where their margins are. He said that when he sees credit unions become 10 times as large as they were in 10 years, it makes absolutely no sense.

Mr. Mc Bride asked whether others from the mutual side have any pressures on deposit rates. An Advisory Committee member said that they had pressures and what they saw see was a big change in the deposit mix. A year and a half or two years ago, a lot less time money moved into the liquid funds, the money market savings checking. His bank has seen a 10 to 12 percent change in the deposit mix from time money versus non-time. Mr. Bride asked whether there was a demographic that switched accounts more than others. An Advisory Committee member said that younger customers do not understand what a time deposit is. Because in their 20 years of existence in the adult world, there have not been time deposits. He said that here was not any differentiation based on ages, but broad scope. Mr. McBride said that there is a perception that younger customers do not like time deposits.

An Advisory Committee member said that one of the biggest things that the banks looked at and transitioned after they looked at all the deposit activity, was the available contingent sources. Contingencies sources are varied, the Federal Home Loan Banks, the discount window and in the news lately, repurchase agreements and the investment portfolio.

Mr. McBride said that a lot of investment portfolios today are not the most efficient method for getting liquidity. There has been an idea that monetization is very difficult. In the example of SVB, monetization was very difficult and very dangerous. The investment security is a primary source of liquidity for first and secondary earnings. He said that the OCC looked at third-party contingent sources and one of the important examples was the prepositioning of collateral at the Federal Home Loan Banks. The Federal Home Loan Banks will often take a member bank's loan book, blanket line against a loan book, and then they will come in and they will take the paper if they need to grab the paper. But each FHLB has a different balance sheet with different limitations.

If the bank is a member of the FHLB in New York, there is an issue, because the FHLB lends 60 percent of its money to insurance companies. Insurance companies take the money for long periods of time, and they do not ever repay it because they hold it against commercial real estate or whatever else there is. It is important to understand the contingent source and where the money comes from. Because if the bank looks at its contingency funding plan and for example, if it has a $10 million run tomorrow, that it will go immediately go to the FHLB, the member bank might get that money shorter than if you can go to a larger FHLB.

Mr. McBride noted that understanding the capacity of the FHLB of which the bank is a member is probably more important than having the line at the FHLB because the FHLB may have other stressors that they have to address. There are all kinds of stressors in the closed system of the financial markets, everybody thinks it is an open system, but it is actually closed. It is something the OCC talks about in the Liquidity Handbook. Getting the line is absolutely the most important, but understanding the restrictions on that line is important as well. The OCC does not have any problems with the FHLB, but banks need to need to make sure that they understand that the FHLB is funding many different organizations.

Mr. McBride said that the logistics of being able to move collateral from the FHLB to the discount window are very complicated. The Bank Term Funding Plan expires on Monday. He asked how many Advisory Committee members participated in that program. An Advisory Committee member said that his bank does, but they have several months before the advances expire, but there are no new advances. He said that he moved collateral to the Fed to participate in the program but did not use it and has to move collateral bank to the Federal Home Loan Bank.

An Advisory Committee member said that his bank opened up a Fed line so that they have the ability to pull from both if needed. Because the Fed line the discount window borrowing rates are not always the most efficient. He noted that the discount window can be punitive, but it is a viable source.

Mr. McBride said that it is a viable source, and the Acting Comptroller has said several times to ignore the stigma from the discount window, because the discount window will be there. Several of these things have come up about the FHLB System in the FHFA report of the Federal Home Loan Bank System at 100. The report was published in November of 2023. It contains a lot of

recommendations and a couple of them are surprising because they were restrictive. Mr. McBride encouraged the Advisory Committee members to look at it if they had not already.

Mr. McBride noted that there has been general stability in the funding sources, reliance on wholesale funding had dwindled and deposits are fairly stable. New technology was introduced that gave depositors ability to move money around. A year ago, there were deposits at low rates, with long-term investments at low rates then all of a sudden overnight 10-year bonds were at four and a half, 5 percent but they did not go too much above that and came right back down. Market risk was stable, and the benign environment drastically changed overnight about a year and a half ago. That change highlighted the things that banks and the OCC had not been focused on as an industry recently related to the stability of the funding sources and the reliance on low yielding long-term investments, which, in turn, highlighted the issue with the contingent sources.

He asked whether the banks' accountants ask any questions banks' ability to hold to maturity. He said that it is a question the agency has because under the accounting definition of held to maturity, the bank has to have the ability to hold it to maturity. Because of the prevalence of held the maturity in certain banks and what that did because it was not an accumulated other comprehensive income, the banks still had unrealized losses. The impact on the balance sheet at a point in time is like an economic value of equity analysis.

Mr. McBride asked whether the Advisory Committee members use banks or public deposits or anything atypical as contingent sources. He said that he thinks that as mutuals, the balance sheets do not have the same pressure that other banks might have, but he is curious if there are other things that the OCC has not thought about. An Advisory Committee member said that they do not have any municipal deposits or public deposits. He noted in New York State, there is a lot of pressure from the state senate to start a public bank. and there is also another group working on a similar project for municipals that would be competition for small community banks. He also said that New York doesn't allow mutuals to accept municipal deposits. But the public bank option is going through a white paper review right now, and that is pretty concerning in New York State.

Mr. McBride said that in talking about deposit base, funding side and contingent sources, contingency funding plans and scenarios are important. One of the most interesting things was watching everything happen a year ago and seeing the contingent funding planning. If a bank meets all of its contingent funding plans, is there a break the bank scenario. It is hard to figure out where the bank is most vulnerable. That is why concentration is important.

He said he thinks the majority of outflows are met by contingent line usage. He asked whether the Advisory Committee members go to their contingent lines on the CFP. One of the biggest issues that comes from the OCC CFP funding process is identifying that the bank understands funding base. Because if an LCR bank has to show that it is going to have outflows of three percent on retail deposits, which is really low, why would the bank's funding base not be that. He said that a bank's average depositor might have $1,100, and there might be 17 million accounts, for a total of $1.7 billion. That juxtaposition against the contingent funding plan identifies that the bank understands the deposit and funding base. It is not that the bank was told to put 10

percent down because the OCC guidance says to, the bank understands that the customer is not going to behave in a certain manner. But at the same time, the bank also understands what pressures the customer might have. It is an understanding of the pressure points that the funding base could experience, rather than just saying 10 percent are going to run out tomorrow because we all generally have an idea from the non-maturity deposits that most of the mutuals see a 33 percent repricing rate in a hundred basis points up.

The CFP is a great document when banks understand how it might work, but the benefit of the CFP is understanding why a bank does not have certain risks that other banks have. The ability to say that because there was a little bit of malaise in the 2010's because of how low rates were. It is understanding where the pressure points are in the bank's strategy and structure. He asked whether there are any atypical stressors that that the Advisory Committee members might see in their CFPs.

An Advisory Committee member said that in a lot of ways it is like what his bank has done on the loan side for years of looking at concentrations. He said that his bank is a little more diverse, but he worries as the bank has grown. It is perceived as kind of a national bank in the market, a large consumer bank. As a result, they do not have as many sticky deposits as they had 25 years ago. Also, in looking at the comments about kids or younger consumers, there are so many ways that they gather funds and move funds that are not through a bank. They may touch the bank a little bit. They may have their home loan at a bank, but he said he is having a harder time getting them as customers. He said that he wonders whether in 15 years it will be worse. He said that he does not see a lot of concentrations in the funding sources. He said that before the SVB failure they had not looked at uninsured deposits, but now they have, and it is about 10 percent.

Mr. McBride asked whether there are any other questions on liquidity that he should address. He asked whether any of the Advisory Committee members see things changing with the Federal Home Loan Bank System as a result of some of the things in the report. He said that when he read the report, some of the recommendations and how deep the report was surprising. Because the FHLB System has been a good source of funding for the banking system for so long, he was surprised by the plethora of recommendations and the perspectives they took in the report.

He said that when he thinks about why the FHLB System was formed, the report is interesting. He does not know whether as an agency the OCC has a position on the report. He said that he thinks the FHLB System is still a good source of money, but discussion of the benefits of the discount window continues at the agency. The discount window goes out to 90 days and that is very different from the five years at a FHLB.

An Advisory Committee member said that he did not think the FHLB System is broken that we needed this extent of a study to do it on top of the other 5,000 pages of regulation that the banking industry is dealing with that has been released in the last couple years.

An Advisory Committee member asked whether the term friction account is different than an operating account or is it more expansive. Mr. McBride explained that it is not a term that the agency has defined. Sometimes an operating account is a friction account. A depositor cannot move an operating account, it takes time to move an operating account. He said that an Advisory

Committee member had use the term "sticky" and a sticky deposit would inherently have more friction in it in contract to money sitting at a large bank has zero friction.

He said that it takes a blink of an eye if he wants to move all of his money out of a large bank. That is the difference. He asked where banks have more stability to slow down money leaving the bank and that an amount as large as $40 billion would have been friction, but that was not the case. The idea is that a bank has an entanglement the customer can but will not run away. He said that he thinks that mutual savings associations will have some of that entanglement because of the way their depositors see their relationship with the bank.

But when a bank cuts off a Netflix account and Uber account and other services that are tied to that checking account, that is friction. There is a difference between business operating accounts and consumer operating accounts. He thinks both types of accounts have stickiness to them. A customer has to consider what they will get or why they move a checking account. The consumer may get a lot of headaches to move everything. It is very difficult to move a customer's primary checking account.

Mr. McBride turned to a discussion of interest rate risk. He explained that for the past 10 years or so, the OCC has been doing an interest rate risk process project, where the agency takes all the data from supervised banks interest rate risk reports and reviews them. The OCC learns from them, also learns what different vendors do and publishes the information. He said that an interesting thing is the richness of the data. There are about 700 banks in the dataset and that can be a bit messy at times because it is reviewed on exam cycle rather than at a specific date.

He said the richness of the data is really interesting. But when the agency first started looking through the data, staff back tested the data, with what the agency actually saw in the industry. One thing that was really easy to back test against was the insurance books and the investment books. What the agency found was that the investment book analysis was almost perfectly correlated with what actually happened in reality. It was really interesting to see. It is just mathematics. But it was interesting and neat to see that the information that banks are getting from the reports is fairly accurate when the non-maturity deposit assumptions are take out.

He said because the non-maturity deposit assumptions are what changes everything. But it was illuminating and interesting to see that the information was remarkably rich and accurate. It was beneficial to the agency. And then when the non-maturity deposit assumptions are layered on, that becomes a $64,000 question. What is the right deposit assumption?

He said that every six months the agency publishes a new cut of the data, and it shows exposures, policy limits, and non-maturity deposit assumptions. The information helps the agency understand how the industry is moving and provides historical context. The agency wants to see that in the aggregate that non-maturity deposit assumptions are getting less and less stable. They are still fairly stable and typically mutual savings associations are more stable in their non-maturity deposit assumptions than non-mutual savings associations, which is understandable. He asked whether the average life of deposit account is about 17 years.

Mr. McBride said there is some stability there, but it is really interesting for the agency because it has been able to see how the industry is moving and just learning so much from it. Another thing the agency looks at is that because mutual bank's non-maturity deposit assumptions are more stable than other banks, mutuals have less interest rate risk. So even if a mutual bank were to look at its balance sheet, the mutual savings associations tend to be more interest rate risk competitive, just on balance sheet alone, not making any judgment because of the stability of the deposit base, a lot of the interest rate risk is negated. For banks that were formerly OTS regulated, it would be called that deposit intangible that the OTS model used to show.

He suggested that the Advisory Committee members look at the report. It is interesting that a lot of the largest banks call in and say they really like this report, even though they know it is looking at banks that are much smaller. Mr. McBride asked whether the Advisory Committee members have any concerns about interest rate risk for the next 12 to 18 months.

An Advisory Committee member said that he does not think that the fees are getting any choppier, but he does not think they are in calm waters either. As mutuals, they have long term fixed rate mortgages, and that is tough on a shifting a one-year-old balance sheet. He does not feel like it is getting any worse, but it is something they worry about. It is interesting to watch the rate environment and seeing it kind of subside, because rates were pressing at least five percent. He thought rates would go higher but maybe not and does not know where it was going to stop. Then it stopped and now banks have a hard time treading water above four percent for the 10 years. He said that on the deposit side, within the last few months, he is starting to see a lot of financials come down a little bit on their time rates.

An Advisory Committee member agreed and said that it is not just the banks that have backed off raising rates, but also the non-bank deposit companies or FinTechs have also slowed in marketing accounts. He said that he does not see demand being at that high number yet, but he agreed that the industry is not in calm waters with long-term debt that banks hold.

CRA Update

Mr. Brickman introduced Vonda Eanes, the OCC's Director for CRA and Fair lending policy in the Bank Supervision Policy line of business to talk about the recently issued CRA rule and to answer any questions.

Ms. Eanes said that she would talk about the changes between the proposal and the final CRA rule and could not talk about the current litigation. She said that the final rule was issued on October 24, 2023. It was published in the Federal Register on February 1, 2024. The effective date for the entire rule is April 1, 2024. Most of the provisions, and all of the provisions related to the exam process go into effect on January 1, 2026, except for large bank reporting. Large banks, under the rule, must comply and report by April 1, 2027. That is the one exception, but otherwise, anything that is related to the exam process goes into effect on April 1, 2026. The final rule was designed to meet the objectives of the original proposal, and that was to strengthen the achievement of the core purpose of the statute while reflecting changes in the banking industry, including the expanded role of mobile and online banking, to provide great greater clarity and consistency in how the OCC applies the regulations across the agencies and within

our agencies to tailor the performance standards to account for differences in bank size and business models and local conditions, and to tailor the data collection and reporting requirements and use existing data wherever possible.

The last two objectives were to promote transparency and public engagement and to promote a consistent regulatory approach that applies to banks regulated by all three agencies. Ms. Eanes said one of the biggest complaints the agencies heard, in the industry and among agency staff, is they are just not consistent in how they apply the rules and that the current rules and the current guidance are less definitive.

The key differences between the final rule and the proposed rule include a change in the weighting between how retail activities and community development activities are weighted in the final rating. That is primarily for large banks. Small banks have one test, so everything relies on the lending test unless they ask to be evaluated on their community development services and investments, which is as it is under the current rule. For the intermediate banks, it is 50 percent lending and 50 percent CD activities, which is how it is how they are evaluated now under the current rule. But to clarify, large banks are defined as $2 billion in assets under the final rule.

An Advisory Committee member asked how the asset size for a large bank was determined. Ms. Eanes explained that economists used various sources to reach the number. She said the preamble to the final rule gives a better explanation. The key point is that the thresholds under the final rule are higher than the thresholds under the current rule to be a small bank. Under the revised rule, a bank with $600 million in assets is small bank.

So, it almost doubled the asset size of banks that are intermediate banks that are now in the small bank pool. The threshold for those intermediate banks rises to $600 to less than $2 billion. So that pool also increases, and the pool of large banks decreases.

She described that the proposal had included weighting of activities for larger banks that was more heavily slanted towards the retail test. In the final rule, the retail lending test and the CD financing and investment test are each weighted 40 percent. The retail services and products test and the CD services test each have 10 percent weighting. The final rule has an equal 50/50 between retail and CD. The agencies also changed the parameters for determining which large banks would be subject to the new retail lending assessment areas.

If a bank does less than 80 percent of the bank's retail lending in the assessment areas, the bank is not subject to the retail lending assessment areas. In addition, if the bank originates at least 150 home mortgage loans or 400 small business loans in an MSA or a statewide non MSA area of metropolitan area where it has no branches it does not have a retail lending assessment area. That dramatically drops the pool of large banks that are subject to those retail lending assessment areas. It also drops the number of assessment areas for those banks. The final rule also reduces the number of product lines. If a bank's retail lending assessment area is defined by small business, the agency will look at small business in that area. If it is determined by home mortgage, the agency is going to look at home mortgage.

Also the final rule limited the types of institutions subject to evaluation outside their retail lending area. The outside retail lending area is a single area. For large banks, it is that geographic area nationwide, where the bank has no facility-based assessment areas and no retail lending assessment areas. It captures everything outside of those areas. If the bank is an intermediate bank, over 50 percent of the lending has to be in an assessment area to be considered. Small banks are not subject to the outside retail lending area unless they ask to be.

The deposit products and credit products considered under a retail services and product test only get positive consideration. If examiners look at responsive deposit products or responsive credit products, that can only help a rating. It cannot hurt a bank's rating. Another important change in the final rule was that the agencies reverted back to how they address discriminatory or practices. If there is evidence of discrimination in credit practices, that can have a negative impact on a bank's final rating, but it is limited back to credit practices rather than that broader scope that was proposed.

Ms. Eanes explained that the transition period was extended for one year from that proposed. Another change is the addition of another test for large banks. The agencies are looking at the same types of activities under all of these exams, but they are broken out differently. There is a retail lending test. There are the community development loans that are currently evaluated under the retail test now moved to this community development financing test and are coupled with community development investments. There is no longer a single investment test. Retail services and products have their own test and community development services have their own test.

She said that there are no requirements to collect data in a specific form or format and provide it to the agencies in a specific form or format.

There have been few changes for small banks, they are still subject to the same lending test. And the only change is that they have an added benefit if they ask the OCC to review or to consider their community development activities, they are no longer limited just to their assessment area. For example, if a small bank is making a loan on an affordable housing, a multifamily housing project in the county adjacent to their assessment area, and they have not pulled that in, but it is serving residents in the assessment area, the OCC can consider it, that is not always captured under the current rule.

Ms. Eanes also said that the strategic plan remains open to all banks, but there are some substantive differences in the strategic plans. Limited purpose banks, which now includes wholesale banks, continue to be evaluated only on their community development activity, but only on their community development investment. Currently, the agencies are considering that lending, investments and services can be evaluated. They can ask to have their community development services considered if they have at least a satisfactory rating on their financing test.

She said that the retail lending assessment areas are new. The agencies retain the facility-based assessment areas, but with a new name. Rather than assessment areas, generally under the current rule, which are built around a bank's branches and other deposit taking facilities, predominantly the old rule or the current or legacy rules, call them ATMs. They do not refer to other remote facilities. The final rule refers to those assessment areas as facility-based

assessment areas to differentiate them from the retail lending assessment areas. The final rule also has the outside retail lending area, which technically is not an assessment area. It is a retail lending area where the agencies are going to look only at retail lending activity.

The agencies clarified community development. There had been a lot of criticism over the years of our 70 plus page interagency set of questions and answers. They are not particularly specific, but some of them very helpful. Others maybe not be so helpful because the agencies tend to want to leave the opportunity for flexibility and judgment. But in doing that, the document is not particularly clear or transparent. In the final rule, the agencies have established 11 specific types of community development activities. The criteria for those are very specific and they are very clearly delineated. There will also be an illustrated list of examples of what kinds of activities qualify under those 11 criteria. There is a confirmation process whereby banks can submit to their agency and ask if the activity qualifies and meet the criteria.

The relevant agency will respond back and say yes or no, and it might be added to the list depending on the activity itself. It is very bank specific or very borrower specific. It is not something that is likely to go on the list because the agencies do not want to create any privacy concerns. But if the activity is something that could apply broadly, then it would go onto that list. It will be a joint illustrative list. All three agencies will decide what goes on the initial list and what goes on the list as it is updated. All three agencies will have a consultative process so that the things that come into each agency, particularly those things that are unique or unusual, can be discussed and consistent responses given.

Ms. Eanes said that the final rule is very specific about how activities for operating subsidiaries or other affiliates are considered. Currently, affiliates are included at the bank's option. Under the final rule, activities of any operating subsidiaries are automatically considered in the bank's CRA exam. And there are some additional data collection, maintenance and reporting requirements for large banks. That is primarily to make sure that the agencies are gathering the information they need to determine peer measurements over time. It is related to community development activities. There is a deposit reporting requirement, but only for banks over $10 billion in assets.

An Advisory Committee member asked if a bank is in a smaller community and large banks in that area are basically in deposit mode but looking for checking accounts and loans, what she thinks will change with large banks in the areas that they bank other than large metropolitan cities. She said that cannot make a prediction and that she does not have an opinion. The rule is very clear that examiners will continue to consider performance context, bank specific performance context, under every test and in every assessment area. There are a great number of things that under the final rule are very similar to the current rules. The agencies look at the same types of activities. There are more metrics and benchmarks under the final rule for large banks and for the intermediate banks in retail. There is also consideration of performance context and other qualitative factors.

An Advisory Committee member said that he would have to take a little bit more time to digest the rule. He said that he has had conversations with the bank's senior leadership team and

compliance teams, and they are trying to get an idea of where the bank, as a mutual with six locations, is going to have to make adjustments, especially in some of the donations that the bank has been making to organizations. He said that the rule changes the bank's perspective on how it is going to be serve the overall market. It is going to take a little time to figure that out.

Ms. Eanes encouraged the Advisory Committee members to share any questions they have with their supervisory office and the supervisory offices are encouraged to share those questions up to the OCC's policy division. Her team was heavily involved in the rulemaking process, and they are leading the implementation process for the agency and working with the other agencies.

She said that the OCC staff working on the implementation are very interested in hearing from banks what questions they have, what are the things banks need have answered. There are a lot of questions the agency cannot answer immediately because of the way the rule will phase in over the implementation period. She said that from a practical perspective for most banks in any rulemaking, the data collection and maintenance requirements are important, because they need to know what the agency is going to ask for and in what form. She said that the agency is keeping an inventory of those questions so that staff can circle back and answer them, if possible. She also said that staff continues to meet with bankers in these types of forums and other outreach to answer those types of questions as they have answers.

She urged the Advisory Committee members to submit those questions, to let the supervisory office know what questions they have. An Advisory Committee member asked whether she could clarify any changes to the community development opportunities. She replied that the community development criteria cover essentially the same four areas that the agencies have under the current rule. They are affordable housing targeted to lower and moderate-income individuals, community services targeted to low- and moderate-income individuals, economic development by financing small businesses, and the revitalization or stabilization of targeted areas. The final rule breaks those down into 11 specific factors. Affordable housing has its own and it is broken down into four or five different components, and they are very specific. An Advisory Committee member said that one of the concerns the banks have had over the years is that the agencies do not tell banks what "affordable" means. Ms. Eanes replied that the final rule included an affordability standard for for multifamily properties which are not related to government programs. She encouraged the Advisory Committee members to look at the rule for that definition.

She said that the final rule does a good job of laying out all of those criteria. The agencies have planned webinars for bankers and for examiners on specific areas and the community development activities certainly will receive that attention. She encouraged the Advisory Committee members to look at the preamble or submit questions about those criteria. The examples in the illustrative list that will be published will be helpful and will answer a lot of questions. The confirmation process also will be helpful to be able to submit through to the agency and ask questions about whether the agency thinks something will or will not qualify. Those questions can be specific to a specific type of loan or a loan to a specific company, business or nonprofit.

Member Roundtable Discussion

Mr. Brickman introduced the Member Roundtable portion of meeting. He noted that three of the OCC's Midsize and Community Bank Supervision Deputy Comptrollers, and Beverly Cole, the Senior Deputy Comptroller for MCBS are at the meeting. He reminded the Advisory Committee members that this is the OCC's opportunity to hear from them about what they are experiencing, either through direct examination experience, with OCC field staff or if there are policy or other issues that are on their minds. He noted that, as always, OCC staff like to hear specific things that affect mutual savings associations.

An Advisory Committee member asked about the proposed changes to the merger rules that have been issued by several the banking agencies. He said that he knows that because they are out for comment, OCC staff cannot comment but he wants to make a point that in discussions of certain business combinations, that the possible elimination of the expedited approval could have an effect on smaller institutions and mutuals. He said that he wants to make sure that as the proposal goes through the process, that the agencies do not forget about the mutual charter type and some of the unique things that they look at potentially doing as they look to compete.

An Advisory Committee member followed up by saying that as margins continue to be squeezed and mutuals look for other ways to survive, shared services are probably the most, accommodative way to keep costs down. He had talked to mutuals that had been through a merger or were in a holding company with multiple subsidiaries. He said that consolidation of back-office functions in areas of compliance, call centers, BSA, and other regulatory requirements was helpful in managing costs. The expedited merger process is an option that should be available.

An Advisory Committee member asked another question. He asked a question that is less about mergers or combinations but that focuses on shared services. He acknowledged that the Advisory Committee has talked about the topic over the years. For example, the situation in which there is not a business combination but an opportunity to share services with a competitor or a peer to leverage a third-party relationship and share a staff person or offer products and services. He said that there seemed to be resistance to that idea, and he asked whether for mutuals that viewpoint changed. He asked whether the landscape is shifting more toward, how do mutuals merge using a holding company model with mutuals benefitting from the arrangement.

He referred to the 2015 White Paper on collaboration published by the OCC. An Advisory Committee member added that for small institutions it is important to consider the alternatives. He said that he thinks the willingness is there, and that whatever obstacles existed before based on competition and within the peer group, have resolved themselves because they all talk to each other and know where there is competition and where there is not. They need help with the regulatory compliance, not on the sales side, but in the back-office. For example, activities like BSA, loan servicing, and compliance auditing are where they can share resources. An Advisory Committee member said shared services is a conversation now. The trade organizations, the mutual groups within the trade organizations are talking about it.

An Advisory Committee member said that another merger topic of concern is the acquisition of banks by credit unions. He said that he thought it was an anomaly, but it is more common now and that is a huge concern, especially when we talk about CRA, liquidity and other pressures that regulated institutions face. He said that he does not know how the NCUA supervises its institutions. He hears more and more presidents of mutuals say that they have been approached by a credit union.

Mr. Brickman said that when the biggest credit union is on the front page of the news, mishandling loan applications that should raise a couple eyebrows. He said the importance of having the round table is that OCC staff can pass that the information on to the Acting Comptroller. He has a relationship with the head of the NCUA and has regular conversations with him. He said that the OCC cannot get into a turf war with them over charter choice, but OCC is keenly aware that there is not a lot of movement in the other direction, and we have had concerns about that, willingness to accept charter conversions, but not allowing charters to do the same in reverse. It is a longstanding conversation and OCC continues to express that concern and pass it along to the Acting Comptroller as well.

He said that he has a question because of the reference the White Paper on Collaboration. He recalled that when the agency issued the white paper, a lot of that impetus came from the Advisory Committee and that the MDIs were very interested in it as well. He asked whether the white paper from the standpoint of the OCC position on shared services is enough. He said that he hears the Advisory Committee members need something else from the OCC now and would like to know what it is. An Advisory Committee member said that they are taking the temperature as the paper is 10 years old.

Mr. Brickman said that in his discussions with Beverly Cole that he has not heard that the agencies are opposed to shared services, if done correctly. He said that it is like participation loans. The OCC has to do its own due diligence, but there is not a change in thinking.

An Advisory Committee member said that he knows that the Acting Comptroller sits on the FDIC board and the FDIC proposed rule that is an example of one regulatory body as it creeps into the entities regulated by another agency. Similarly, it starts as a $10 billion threshold tends to creep down to threshold below $10 billion. The FDIC proposal on corporate governance includes bad policy. He has a list of issues, but it is the FDIC statement that says they can choose to apply the requirements to those institution with less than the $10 billion threshold. As the Acting Comptroller sits on the board, the proposal arose from issues at Silicon Valley and Signature Bank. He asked whether if the rule had been in place would Signature and SVB still have failed.

Mr. Brickman said that he thinks they would have because it was bad decision making and lack of enforcement of regulatory requirements that drove the failures. Had they been enforced maybe they would not have failed. The Advisory Committee member said that there are a lot of objectionable things in the governance rule proposed by the FDIC. The worst one is that the boards select executive management, not the CEO, but executive management. That is not their job. Their job is to hire the CEO and then it is his or her job to fill their team. Typically, particularly community bank boards are not comprised of bankers. They do not know the skillset

or the team dynamics that need to be hired. He said that he thinks that it is bad policy when the FDIC asks bank boards to hire the executive management team, and he asked that the Acting Comptroller give that message to the FDIC.

Mr. Brickman said that the OCC gets a lot of concerns from community bankers on trickle down of regulations that are intended to apply to a larger or more complex banks. The OCC gets a lot of concern, but not a lot of actual direct, measurable examples of examiners actually misapplying some of large bank or larger bank guidance at the community bank level. He asked whether as a group, if the Advisory Committee members have any examples of where they think that OCC exam staff has actually gone too far in terms of applying something that was intended to be applicable to a large bank in the community bank space, because that is where OCC needs information, but the fear is recognized.

Mr. Brickman said that the concern has always existed at the community bank level, and as an agency, the OCC has been fairly consistent that it does not want that to happen. The OCC wants to be very explicit. The agency wants the level of a bank's control structure, expectations from examiners to be commensurate with the level of risk of the bank, its size and complexity. The more specific examples of where it is actually happening are the ones that the agency can take action on to fix, but OCC does not hear a lot of those. He said he knows it is putting the Advisory Members on the spot, but if they do have those specific examples, the OCC would like to hear them.

He said that the OCC will continue to pay attention and sometimes it is easier to solve the problem once someone points it out in real practice. There have been some examples. He said that one of the areas that the agency has been working on for larger institutions has been climate, and it has been surprising the number of community bankers that have wanted OCC to do outreach on climate. OCC has talked to the examiners about banks asking a lot of questions about climate and the agency says it is not focused on community banks for this. For example, when an examiner started talking about climate at an CEO outreach because it was requested, one of a bank's board members called the Acting Comptroller and said the OCC had said that it was not going to talk to community banks about climate. The agency wants to be responsive.

Mr. Stanley added that in real time there is an opportunity if Advisory Committee members are experiencing issues where the exam staffs are looking at things and were questioning banks about issues that the agency said it would not necessarily apply immediately to community banks, there is always a real time opportunity to bubble that up, fairly quickly and can get the person to myself or Mr. Thornton who could address the issue quickly. There are Associate Deputy Comptrollers who are responsible for supervisory offices, and there are mechanisms where bankers can get to staff fairly quickly, where staff could try and address those issues.

An Advisory Committee member said that he had done that in the past. In his most recent exam, there was a HMDA miscoding and bank staff was able talk to the Examiner in Charge quickly. It made it to Mr. Thornton and was resolved. Ms. Cole agree that said that if a bank feels like expectations are too much, and are large bank focused on the bank, make a phone call to the Deputy Comptroller and get them involved.

Mr. Brickman said those topics are not limited to just trickle-down issues from large bank rules and guidance. OCC has continued to reiterate to examiners, there is mutual specific guidance when it comes to looking at earnings, interest rate risk, liquidity, and other issues. The bigger challenge examiners are facing nowadays is even within the mutual population, there has been some divergence, there are more mutuals that have elected to operate as covered savings associations. So even looking at a mutual peer group may lead examiners to the wrong conclusion, when it comes to earnings if the examiner is comparing a traditional mutual to a mutual covered savings association. The OCC is trying to be as explicit as possible in educating examiners. The agency is certainly interested in any feedback if you think examiners are misapplying some of the traditional guides OCC has already established that are specific to mutuality, and the importance of how examiners should look at the balance sheet structure and how it is impacted by the current rate and environment. Because there should be differences in how examiners would assess the risk of earnings deterioration or capital, for a mutual today than the agency would for a national bank or a federal savings association in stock form. Keep that in mind as well. It is not just a large bank trickle down issue. It is also a trickle across and amongst the community bank populations that do have very different balance sheet structures and risk profiles.

An Advisory Committee member asked about overdraft fees. He said that larger banks can get on TV and say that they do not charge fees, but for smaller mutuals, those fees are a major portion of the bank's income. To give them up would affect the banks. Ms. Cole said there are some institutions where a huge percentage of their income is in fees. That is probably more concerning than a bank offering a service or collecting a reasonable fee for the services that the bank provides. There are some institutions, not many in the community bank space where the agency has looked at the amount of fees that they are charging and collecting, and it has been somewhat excessive. That is a concern.

The reality is the agency wants banks to be aware of the impact of those overdraft fees on their consumers. Some of the horror stories about representment fees where a check or a charge can be represented four or five times and banks continue to charge a fee when the customer has no idea it is being represented and the bank fully knows the consumer would not keep running it through if they had a choice. That is where it gets to be abusive. Are all those fees continuing to hit that individual who in many cases may or may not be able to afford them or the ability to stop it from happening.

Ms. Cole said the agency does not see a lot of that in the community bank space. A lot of it happens in the bigger institutions where they have a whole slew of those transactions happening and they cannot get the data to show when the abuses are happening. It starts to manifest itself in customer complaints and in other ways. For a bank that is not getting customer complaints, which has a reasonably designed overdraft product that gives the customer clear disclosure on when they would get an overdraft fee and allows that customer to react to that, to either not overdraw or to make a decision not to have an account that has that feature, that is the way the OCC would expect the system to work. She said that the biggest challenge OCC has heard in the community bank lane is just the reporting aspect.

If a bank is running transactions through a core service provider, sometimes the core service providers are not producing the data necessary to understand if there is a harmful impact happening to consumers. A bank has to look at alternative means to figure that information out again, look at the bank's customer complaints, and reassess the fundamentals of the overdraft program. But at the end of the day, philosophically there is a product there that for an informed consumer can be a valid and legitimate product and banks should not shy away from that. But banks have to be careful about overextending and getting so caught up in the fees and the income it provides that the bank loses sight that it could be causing harm. So, it is a balancing act and within the community bank space, the OCC has been pleasantly surprised that the industry does not have a lot more exposure.

Mr. Brickman said that he thinks that an advantage of the community bank model is that the banks care about their customers far more than some large banks where the customer is a number on a form. If a community banker sees a customer that has a dozen overdrafts over the course of six months, typically the bank will have a relationship manager pick up the phone, call that customer and figure out if there is a better product or service that will help get them out of the potential cycle of debt. The customer may say that because they know that is what they intended, and they like to use this product. There may be another instance where they say no, they are really struggling, and the bank can help them.

Mr. Thornton agreed with the point. He said that a bank needs to be cognizant of what activities are taking place for those individual customers. The Deputy Comptrollers are starting to have conversations with the banks about their overdraft programs. For those customers who are using the program, look at those fees and ensure there is not any representment, ensuring there is no authorized positive settle negative type of activity to ensure that there is no customer harm. So that is the kind of conversation OCC has with the bankers - do you have an overdraft program, the OCC is not looking at the bank because it has a high amount of fees coming from this particular program. However, the bank needs to be cognizant of what is going into the bank's system because oftentimes the bank is relying on core providers and the coding may not reflect, representment or authorize positive settle negative. Understanding the customer relationship with the core provider is providing the coding as well within the system and ensuring that there is not any customer harm.

Mr. Brickman said that the challenge he has as he is responsible for the OCC's novel bank supervision group, is the community banks are heavily invested in financial technology partnerships or other kind of novel activities. There are bad actors who make the headlines and who end up under the consent order. A host of bad practices are made public. The thing the OCC tells most of the novel banks that it supervises is pay attention to those enforcement actions as they come out because that is the list of things you can do to do this well. It is what the agency expects to see if the company wants to engage in those third-party relationships.

He said that there is a public document saying, do it this way instead and that is a tremendous source of information. He also recommended the OCC's third-party risk management guidance, that has been pretty stable over time. The agency has reiterated some of the messaging and reissued some interagency clarifications. The OCC says the bank can outsource the function, but

the bank cannot outsource the risk. The bank has to pay attention to that relationship. The bank has to understand the nature of what it is getting into, the bank has to understand how that relationship scales over time and how the internal controls can be modified and adapt to the scale of the new FinTech relationship. The people who have screwed it up the most have been the ones where they go from zero to a hundred and overnight, they have a volume of customer transactions that the BSA program or whatever other program the bank has in place as a check and a balance is overwhelmed.

He said that is where banks and the agency see people really running into trouble. Having those things answered upfront, for example how far does the bank allow this to scale before it pulls back and reassess what the control structure is, how it can adapt, how it can grow to compensate for some of the growth that we are seeing as part of the third-party relationship.

Mr. Stanley said that it is important to understand what that relationship looks like going in and what an exit potentially looks like. Oftentimes, one of the things the agency sees is the bank gets into it, and everything is rosy and peachy on the front end, but then divorcing gets ugly, kind of like a core. What does an exit strategy look like. That is one of the things that he talked about with companies coming from San Francisco. There was lots of interest in leveraging those partnerships. But the infrastructure has to be built out ahead of time. There was some conversation earlier about third-party risk management, how critical that really is an understanding those relationships.

At the end of the day, the OCC is going to look at the bank, the OCC is not going to look at that third party. The agency will look at the bank or the institution to manage the relationship appropriately. Third party risk management and going from zero to a hundred are the big issues. And third party risk management is the guidance that that pertains to that. BSA/AML is really the issue that is the stickiest. When the bank goes from zero to a hundred or zero to 10 even, and it assumes that the FinTech partners are taking care the bank from a BSA perspective, without making sure that they are taking care of the bank from a BSA perspective is a big mistake.

Mr. King said that the National Bankers Association, working with Project REACh, developed a FinTech playbook that gives banks some things to consider when they enter into a relationship with a FinTech. So that may be information to get banks started. It gives some information, guidance, and perspective to take into consideration when partnering with FinTech.

Mr. Brickman highlighted another important issue in how important the contract management part of these relationships is. Bankers do not always realize what they are obligated to when they sign the contract. The OCC has seen instances where the banks enter into third-party relationships as part of which if they decide to cut off or not onboard additional customers, and it is considered a breach of their contractual terms. They end up with litigation risk or liability to understand the rights as part of that contract the bank is signing. Mr. Stanley made the point of the exit, the breakup fees or the cost of exiting the relationship, but even within the relationship, if it is functioning normally, but the bank wants to put a control in place or wants to stop the activity for a period of time to adjust and to be able to adapt, making sure that the bank has the requirements spelled out in the contract so that it does not end up finding itself in a situation

where contractually it cannot say no, and then the regulator comes in saying, no, the bank is going to have to break that contract because is unsafe or unsound.

Simple contract management, reading the fine print and understanding what are the bank's rights, responsibilities and roles as the banker versus this technology company that has been a stumbling block for several banks that have made mistakes.

Mr. Brickman asked whether there are other potential topics for discussion today. Someone sent in a question about capital and capital treatment for mutuals. He said it might have been about non-withdrawable or pledged deposits or mutual capital certificates. An Advisory Committee member said he raised the question about mutual capital certificates and whether the OCC could provide information about looking at the framework of the original capital certificates. What types of rules and regulations were in place at the time. He said that when he talks to legislators who do not know what a mutual is, it is useful to provide some context about what happened when the instruments were introduced.

He said that he knows that the OCC has an archive of regulatory information. There are legislators that have no idea what a mutual bank is, but they still want to form a new public bank in post offices. The Advisory Committee member tells them that before they start to recreate the wheel, they should look at the wheel that was created a hundred years ago so that they can understand it a little bit better. The documentation would be helpful for the future.

Mr. Brickman said he understood the question. The OCC has received requests for information about the original mutual capital certificates and staff has looked in archived files to see what is available. He noted that there have been many changes since the mutuals were chartered and the capital certificates were issued. It would be great to see how an instrument today would look. The second part of that would be that the OCC's capital policy folks, legal folks are well equipped and ready and willing to have a dialogue with any individual bank that has a proposed capital instrument or tool that they want to consider. We have engaged in multiple of those conversations, giving feedback. In some cases, it has resulted in frustration and in others it has resulted in tools continuing to advance to a point of almost reaching fruition. Every single channel that those requests come in gives us a chance to explore and to continue to think through how that would work going forward and what the regulatory considerations would have to be.

An Advisory Committee member asked a question about what kind of framework or discussions have taken place around Artificial Intelligence. He said that there is talk about a revolutionary change that is going to affect banking.

Mr. Brickman said that in the prior week. the OCC had an artificial intelligence forum just for OCC employees to educate the examiners on the landscape of what is starting to emerge in the public and private sector. Some companies came in and presented how they are using artificial intelligence. The companies showed a lot of the language-based tools where a person can go out to the internet and do various things drawing on the realm of human knowledge that exists on the internet and also showcased and highlighted the positive uses as well as the potential negative consequences. From a fraud perspective, the risk of artificial intelligence is extremely high, from

the speed and efficiency and delivery of products and services, the benefit is equally high, if not more so.

He said that balancing the two and making sure that winners and losers end up being on the right side of artificial intelligence in the uses can be critically important for the OCC as a regulatory agency. He said that David Stankiewicz, the Acting Director of the OCC's Office of Financial Technology, who is joining the meeting after lunch, can provide more specific examples when he joins the meeting of how the agency is looking at AI, especially on the agency's cyber security and BSA side. Mr. Brickman said that he thinks there is great opportunity that the industry can try to get a little ahead of the bad guys as opposed to always playing defense.

Office of Financial Technology

Mr. Brickman introduced David Stankiewicz, who is the OCC's Acting Chief Innovation Officer in the Office of Financial Technology.

Mr. Stankiewicz described the history and the organization of the Office of Innovation. The agency continues to reaffirm its commitment to understanding and grappling with these evolving technologies. He said that he thinks of OFT as the tip of the spear when it comes to various technologies, making sure that the agency is thinking about them, grappling with them, that agency staff is talking to people. OFT considers itself as a clearing house for information. Mr. Stankiewicz said that it is important to talk to the banks, financial technology entities, and advocacy groups to give the agency information about various things happening in the banking industry. It is important for them to know that the banking industry is changing rapidly. It is important for the agency to understand that. There are essentially three things that OFT has been dealing with this year, and it is going to change from year to year.

He said that most of his time is spent on bank FinTech partnerships, artificial intelligence and crypto/tokenization. Nighty percent of the office's time is on those three things. The presentation[2] focuses on bank FinTech partnerships. The OFT staff are happy to meet people and answer questions. On slide 6, there are considerations for to bank/ FinTech partnerships listed. This is sometimes known as banking as a service or BAAS. He said that he prefers the term bank FinTech partnership or bank FinTech arrangement because it is more precise. When he hears "banking as a service," it is not immediately clear what that means. For example, if the bank is looking to grow, it may have a lot of younger customers that are not interested anymore in walking into a bank branch, and they want to do everything online on their phones. He said that the bank asks how to reach them. He said that one way is to partner with a financial technology company or FinTech.

That entity sits between the end customer or the end user, and the bank. From the customer's point of view, they are online and they think that they would like some sort of financial product. They may not be thinking about what they are going to do with the bank. They just want an app or something. They go to a FinTech, and the FinTech says that it will give the customer a deposit

[2] A presentation is on the MSAAC page of OCC.gov.

account and gives the interest rate that it pays. The customer signs up on their phone and is approved in five to 10 minutes.

It is easy and the disclaimers and the banking services are offered by the third party and the consumer may or may not focus on who the bank is. There are some synergies in these arrangements. The FinTech is getting the business. They have an interaction with the consumer. They have a bank that may be a community bank or a bank that has a broader reach, it could be a state or national reach. This is a way, potentially, of getting more customers to the bank, but there risks, because now the bank has a third party involved. There is another entity between the bank and the end user. The bank does not know end user as well as they used to when the customer would meet the bank staff face to face, or at the least know that they were on the bank's own personal app. The calculation of the risk and reward is important, the bank can get a broader reach, but it now has additional complexity in its operating environment. He said that is one flavor of bank/FinTech partnerships, but there are many other kinds, and they are becoming increasingly complex. If the entity is a customer facing entity, there may be hundreds and thousands of customers. The FinTech may have relationships with multiple banks, and it may be routing different customers to different banks.

Alternatively, the bank may want to interact with some of these FinTech entities, but the challenge is that the bank's core system does not immediately match up with the FinTech's core system. In that case there may be an intermediary that is essentially the bank's connection from its core to the intermediary, to the FinTech to the end users. Banks make these arrangements in payments, or in loans. The arrangements can be done in other ways. He said that the Acting Comptroller has discussed the complexity, and it highlights for the agency how the industry is changing. The Acting Comptroller has talked about a supply chain function where the bank has a process of working through the chain until it gets to the end customer.

Mr. Stankiewicz said that whether this is something that a bank is involved in, whether in this precise way or in another way, they have to think about third party risk management. There are well-established principles that banks have been following for a long time. This is true of any topic in financial technology. The well-established basic blocking and tackling of banking applies. It is in a different context. Banking has always evolved. Forty years ago, it was ATMs and banks had to understand how to apply risk management to ATMs.

He described the third-party risk management guidance released by the banking agencies - OCC, FDIC, and Fed. It is essentially an update of the OCC's third-party risk management. The overriding principle is that the bank owns the risk. If a company is performing a service on the bank's behalf, the bank needs to treat that activity as if it were doing it. The bank owns the risk.

It is important to understand who is in charge of what. The guidance addresses what the agencies have identified as they have talked to banks. The first issue is to build a strategic case for the activity. The second issue is whether the bank's technical experts are involved from the beginning. If the bank is bringing in a partnership of any sort, it needs to make sure that it has the right people in the room from the start so that there are no surprises, and it has the right expertise

up front. The bank has to consider how the activity is integrated into the bank's business and operations.

The FinTech needs to understand that now they are in a regulated environment, and they cannot move fast. A cultural conversation is necessary. The bank has to do its own due diligence on the FinTech and needs to consider an exit strategy. Third party risk management is the entire cycle from the beginning through the middle to the end. It is an ongoing process. Slide 8 lists the OCC resources and one of them is a publication on conducting due diligence for FinTech companies, a guide for community banks. It walks the bank through different issues at a high level. It talks about one of the facts that sometimes as a small institution the bank may not always have a good sense of information from some of these newer entities and how to deal with an entity that is newer.

An Advisory Committee member said that as mutual banks, they are very sensitive to who the customers are because they are ultimately the bank's owners. If the bank is a sponsor bank for, as an example, Chime, who is the owner? Is it Chime or is it Chime's customers? Mr. Stankiewicz said that is great question. and he has not thought about it. The Advisory Committee member said that he is usually the only mutual or one of two mutuals at Fintech conferences and the audience talks about banking as a service and if a bank really wants to grow deposits, it can be a sponsor bank for Chime or another company. He said that he has had the concern about who is my customer? Is it Chime? Which is good news, bad news about that, or is it Chime's 50,000 customers and there is good news, bad news about that. The general question of who is the customer is a very important one in the broader context because as the entity is dealing with the bank who is dealing with the third party FinTech, who is then dealing with the end customer. The bank might think of the end customer as is customer and perhaps it should, but it is an excellent question regarding the ownership question.

Mr. Stankiewicz said it is a good question and that he does not mean to oversimplify it but if the third party is using the bank in order to secure deposit insurance for their customer, that means they are basically passing that deposit through to the bank. He thinks that the banks would have to treat them like any other depositor. They would become members of the mutual and they would be Chime customers. The money that they put in the bank is on the bank's balance sheet.

An Advisory Committee member asked whether OFT looks at the structure of the FinTechs and if so, whether there is access for institutions to find out how they are operating. He said that it is similar to the question about core providers. Banks try to choose a core provider based upon the relationships that they have with other institutions, but they cannot get the examination report before signing a contract. That question comes up a lot.

Mr. Stankiewicz said that OFT does not examine the companies, but they talk to many bankers and can provide some information about the companies. He said that banks can talk to their peers. He said that there is a significant service provider supervision portfolio that is in the OCC's supervision risk and analysis group. The companies that are smaller than the cores in the significant service providers are the regional service providers.

Mr. Brickman said that the regional service providers are supervised under MCBS, and he is the deputy comptroller for that line of business. He said that the OCC has to make judicious decisions within that group of who the agency supervises. He said that the agency has debated countless times at what point should the agency provide supervisory information to banks in order to help them make a decision. The OCC has come down on the side of not allowing the information to be shared until the bank is a client. Because as a regulatory agency, the OCC does not want to intervene in kind of the free-market system picking winners and losers.

An Advisory Committee asked whether if a bank were involved with a company like Chime and Chime is not the member of the bank. The individual account holders are the members, whether the OCC would consider that as wholesale funding and concentration. He said that it comes back to the conversation with Mr. McBride about re-envisioning what it means to be a sticky deposit versus one that is more volatile and likely to leave. He asked whether if a bank breaks its relationship with Chime, does that mean that entire portfolio of depositors leaves with Chime at the same time. Banks would look at that differently. It may not have met the classic definition of wholesale funding, but banks need to think differently in this financial technology world where they have an exposure that could lead to a huge change in liquidity in a very short window of time.

Mr. Stankiewicz said that is something that the OCC needs to adapt to. He said that a bank needs to think about the risks of that kind of a partnership. When the agency talks about scalability, for example, how much of that relationship does the bank rely on for growth and can it walk away from that relationship and still sustain the lending that it wants to sustain the community outreach it wants. And what is the backup plan? An Advisory Committee member said that he agreed that having an exit strategy is important, but would it be an issue if is about five percent of the bank's deposits, or if it grows into be 60 percent of deposits over a year's time and how sticky they are.

Mr. Stankiewicz turned the discussion to artificial intelligence. He said that artificial intelligence has been used by banks for a long time in various ways. There was some discussion at one point of maybe the agency should inventory the way AI is being used internally and the examples were every day uses, for example spell check and the use of phones. The reason that artificial intelligence has become more prominent in the past year is because of some advances leading to what is called Generative AI. Generative AI is AI that can create things. The most well-known of these is chat GPT, the large language model.

He said that the web ingested millions and billions of texts. Statistically, if he gave a set of words, what is the next most likely word to show up? When is asked questions, it can reply conversationally, and can create lots of things, but it may not be correct. He said that conceivably like any other automation, it can be used in the back office. It could be used for efficiency purposes. There are other ways of using it that are going to continue to be explored. Over time it may be used for customer facing applications.

An Advisory Committee member asked whether the OCC is looking for some sort of policy framework or is the agency working within a sandbox environment where it can help banks

understand how AI can benefit banks in different scenarios. Mr. Stankiewicz said that the Acting Comptroller has talked about to what extent the agency can get involved in bank run pilots. These are great questions because it is important for the OCC to have a hands-on sense of how the technology works so it can help banks understand exactly how it is going to work out. The agency is grappling with how it can uses AI internally. He said that it also will inform the agency's understanding of how to supervise it and what to do with it. He said that in the meantime, the guidance that the agency has issued uses the bedrock principles. The OCC will come back to those, and at some point, it may put out something that is in the AI context.

He turned the discussion to crypto currency. Recently the OCC had a tokenization symposium. It was livestreamed to the public. Tokenization can be defined in a couple different ways in the area of financial services. FinTech generally has a firm definition, but tokenization is defined as taking real world assets and putting them on a blockchain or distributed ledger. Alternatively, tokenization is taking any assets and breaking down them to their component parts and making them tradeable.

The classic definition of a tokenization is taking a Treasury bond and moving it into a different trading system. Now it is traded on blockchain. Larger institutions are thinking about how to do that. The goal of the tokenization symposium was to try and start to get to arms around some of the ideas.

There are a variety of different types of crypto, and it is important when talking about crypto to make the distinction. Bitcoin is an unbacked asset, and Bitcoin is purely based on speculation. Bitcoin itself has relatively little functionality other than as a payment mechanism or speculative asset. Ether is the second most popular crypto also enables smart contracts, which are essentially algorithms embedded in the crypto or ways of programming the asset. An investor could decide to own Ether because it believes that that smart contract functionality had a potential future benefit versus something else. Stable coin is a crypto asset that is tied potentially one to one. It does not have to be a real-world asset.

Mr. Stankiewicz described the aspects of different kinds of crypto currency and provided background on some of the risks involved. Mr. Brickman said that if the Advisory Committee members want to focus attention on any innovation related topics that the OCC would be able to address the questions, especially as they relate to community banks or mutual banks.

Committee Updates

Mr. Brickman said that there are a couple of important updates in terms of the committee structure for this year. The agency is renewing the charter and the membership for 2025-2026. The charter's two-year term expires in June, and the OCC is working behind the scenes to get all the paperwork together and the approvals necessary within the OCC establish another two-year term for the Mutual Savings Association Advisory Committee.

The existing term of all the current members ends on December 31st. Those members who are in their first two-year term, are welcome to apply for a second two-year term. For those members who are already in the second two-year term, the OCC has a requirement that the members stand

down from this committee and at least have a cooling off period before trying to come back and join the committee.

He said the second topic is that the next meeting tentatively is scheduled for June 24th and 25th. The 24th would be the advisory committee meeting, and the 25th would be the OCC Mutual Forum. We will only invite the federal savings associations to attend the meeting. He asked whether the Advisory Committee members want to continue to have the mutual forum this year.

The Advisory Committee members agreed. He said that the structure would be three quarters of a day agenda where we have a variety of presentations, panel discussions. He asked for topic suggestions. He also asked whether the meeting should be a hybrid virtual and in-person meeting.

The Advisory Committee members said that they support having a hybrid in-person and virtual meeting. Mr. Brickman said that OCC would develop a program and ask for feedback from the Advisory Committee members. The forum will be a private meeting. There will not be a public record. He said the final topic of committee business is getting a pulse check on whether the mutual group and is interested in continuing to try and work with the MDIAC. There have been limited opportunities to start a conversation and the agency can continue to pursue the idea and have a meeting later in the year or there can be an MDI discussion as a panel discussion at the forum.

As Advisory Committee member said that he liked the energy that was created by having the mutual/MDI conversation. Th groups have to figure out where to take it from here. Mr. Brickman said that one of the questions on the table in a previous meeting was whether the groups wanted the agency to form a subcommittee where a group of the members from the Mutual Advisory Committee and a group of members from the Minority Depository Institution Advisory Committee could meet outside of the constraints of a formal meeting and have a conversation about potential accomplishments.

He said that in a subcommittee structure the members could have meetings independent of the OCC, and then the group would report out to the OCC at a public meeting. The OCC could provide scheduling and other support, but the meetings would not be attended by the Acting Comptroller or members of OCC staff. It would be a chance for the committee members to think through ideas of how to better represent the two advisory committees in front of the OCC.

An Advisory Committee member said that he was supportive of setting up a mechanism for the groups to work together. There are similar issues with the groups and energy in the conversations.

Public Comments

Mr. Brickman said that the final agenda item was the public comment period. As this is a public meeting, the public has an opportunity to enter anything into the record. The OCC did not receive any public comments in advance. He asked whether and of the virtual or in-person attendees has a comment.

Will Waller from M3F Inc submitted the following comment:

"Given the significant move up in interest rates over the last two years, the regulators (OCC, Federal Reserve, and FDIC) should focus more on the fair value of assets on bank balance sheets. There have been several examples of bank failures in the last year in which the banks looked well capitalized from a regulatory capital ratio perspective, all the way to the point of the failure. However, if assets were fair valued there was not adequate capital that remained at Silicon Valley Bank, First Republic, and Signature Bank of New York. Leading up to their failures, those banks paid dividends and repurchased stock, even though fair valuing assets would have shown the banks were not adequately capitalized. The capital markets for equity issuance are closed and have been for over a year, with the exception of a few mutual banks that have formed holding companies and raised equity capital. There needs to be fair value reporting related to loan portfolios as well as the assumptions that that go into calculating the fair values disclosed to the regulators and available to the public. For publicly traded (SEC registered companies) some of these disclosures are made, but for mutuals, non-SEC registered holding companies, and privately held banks there needs to be such **disclosure for both depositors and regulators. There will likely be a few more failures driven by** in adequate capital after fair valuing of assets (New York Community in New York which is still allowed to payout a dividend to shareholders and Republic First in Philadelphia which is just under $6 billion in assets are examples that are under pressure now and likely could not raise equity capital given partially a result of this fair value of asset dynamic). Further, the regulators, including the OCC should consider implementing a rule that banks with less than 5% equity/assets when adjusted for the fair value marks on assets cannot distribute capital by repurchasing stock or paying out dividends to share shareholders and Republic First in Philadelphia which is just under $6 billion in assets are examples that are under pressure now and likely could not raise equity capital given partially a result of this fair value of asset dynamic). Further, the regulators, including the OCC should consider implementing a rule that banks with less than 5% equity/assets when adjusted for the fair value marks on assets cannot distribute capital by repurchasing stock or paying out dividends to shareholders (which would allow earnings to replenish capital over time). Many mutual banks have longer dated assets (real estate loans, mortgage-backed securities, etc) that are on the balance sheet at extremely low rates and the fair market value of those assets takes capital ratios in many cases to extremely low or negative levels. I urge the OCC to consider this topic as it is essential for a healthy banking industry going forward and many mutuals that might end up ultimately failing if interest rates go higher."

There were no other public comments.

Mr. Brickman adjourned the meeting at 2:30 p.m.

Certification

/s/

Michael R. Brickman
Designated Federal Officer