STATEMENT BY

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on

“Oversight of U.S. Financial Regulators: Accountability and Financial Stability”

before the

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

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

My statement reports on the state of the banking industry and the condition of the FDIC's Deposit Insurance Fund (DIF). The testimony provides an update on FDIC resolution activities and discusses the release of a paper reaffirming the FDIC's preparedness to apply the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) Title II[1] framework in the resolution of a global systemically important bank (GSIB). In addition, I discuss improvements in regulation and bank supervision that could help prevent bank failures like those that occurred in the spring of 2023 or mitigate their impact in the future, such as initiatives to improve banks' management of liquidity and funding risks and a rulemaking to strengthen corporate governance at larger banks.

My testimony discusses other important regulatory activities at the FDIC, including an update on the Basel III Notice of Proposed Rulemaking, the release of an FDIC request for information and comment on revisions to the FDIC's Statement of Policy on Bank Merger Transactions, and steps taken to initiate a joint rulemaking on incentive-based compensation.

First and foremost, my testimony will discuss my top priority, addressing workplace culture issues at the FDIC.

[1] 12 U.S.C. §§ 5381, *et seq.*

FDIC Workplace Culture

I am deeply committed to the FDIC and its mission, as well as to the people on whom that mission depends. I love this agency, and its people must be protected.

That is why, when news reports of harassment, discrimination, and other misconduct first surfaced last year, it was essential to gain a deeper understanding of the agency's workplace culture. At my direction, the FDIC initiated an independent, third-party review to determine the depth and extent of these issues. Last week, the results of that review, which was conducted by the law firm of Cleary Gottlieb, were released.[2] The review found that for an extended period of time, the FDIC has failed to provide a workplace safe from sexual harassment, discrimination, and other personal misconduct.

I accept the findings of the report and, as Chairman, I take full responsibility. To anyone who has experienced sexual harassment or other misconduct at the FDIC, I again want to apologize and express how deeply sorry I am. I also acknowledge my own failures as Chairman, both in failing to recognize how my temperament in meetings impacted others and for not having identified deeper cultural issues at the FDIC sooner. I am personally committed to addressing these issues. We accept all of the recommendations of this report and are incorporating them into our existing Action Plan for a Safe, Fair, and Inclusive Work Environment.[3]

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[2] See PR-35-2024, *FDIC Special Review Committee Releases Independent Report on Workplace Misconduct and Culture* (May 7, 2024) available at https://www.fdic.gov/news/press-releases/fdic-special-review-committee-releases-independent-report-workplace-misconduct

[3] See *Action Plan for a Safe, Fair, and Inclusive Work Environment* (Updated December 4, 2023), available at: https://www.fdic.gov/about/diversity/pdf/action-plan-12-4-23-v1.pdf.

To restore credibility with our workforce, we must act swiftly on the report's recommendations and demonstrate a commitment to making fundamental change. For this reason, we have already begun implementing several key recommendations.

The report recommends that we identify and appoint a transformation monitor who will monitor, audit, and report on our implementation of the recommendations. We have already begun that process and will issue a Request for Proposals for this purpose as early as this week.

The report also recommends that we engage an independent third-party expert to support our efforts. We have begun that process and will also issue a Request for Proposals for this purpose as early as this week.

The report recommends fundamental change to the agency's structure and procedures for receiving and investigating complaints, and taking disciplinary action against misconduct in light of the failures of the existing offices delegated those duties. We will do this by proposing the establishment of an independent Office of Professional Conduct, which will report directly to the FDIC Board of Directors. It will be charged with fulfilling these responsibilities, including through the use of outside third-parties to conduct investigations. The transformation monitor and independent third-party expert will advise us on this proposal.

Since December, the FDIC has been focused on implementing its Action Plan to address all aspects of the issues raised in the news reports. The Action Plan represents an agency-wide effort, with participation by employees at all levels.

Many of the recommendations outlined in the report are already encompassed by the agency's Action Plan, and in some instances, our Action Plan goes beyond the recommendations in the report. The Action Plan is focused around three core elements - providing more support

and resources to victims, strengthening our process for reporting and investigating complaints, and improving accountability for anyone who is found to engage in misconduct, including through separation from the agency. The proposal to establish an independent Office of Professional Conduct would advance all of these goals.

It is my privilege to lead and work alongside everyone at the FDIC. Our employees are extraordinarily dedicated to the agency and its mission. The work they do day-in and day-out is critical to maintaining stability and confidence in our banking system, whether by strengthening the safety and soundness and resolvability of U.S. financial institutions, responding to the bank failures of last year, or through financial literacy and inclusion efforts. They deserve to have a workplace where all feel safe, valued and respected. There is no higher priority for me than delivering on that commitment.

State of the Banking Industry

The banking industry has shown resilience after a period of liquidity stress in early 2023. Full-year 2023 net income remained well above levels reported before the pandemic, overall asset quality metrics were favorable, and the industry's liquidity was stable as of the end of 2023. However, banks reported lower net interest margins and higher funding pressures. Some loan portfolios, such as credit cards, auto loans, and non-owner-occupied commercial real estate loans, are exhibiting increasing delinquency and charge-off rates. Although unrealized losses on securities declined in the fourth quarter, they remain elevated compared to historical levels. While the FDIC Quarterly Banking Profile data will not be available until later this month, early reports from the first quarter of 2024 indicate that net interest margin pressures continued, and

higher market interest rates likely have reduced bank securities values, increasing unrealized losses.

In the fourth quarter of 2023, domestic deposits increased for the first time in seven quarters, driven by growth in time deposits. The industry's insured deposits increased by 0.5 percent. Uninsured deposit growth was masked by one large bank that eliminated a significant amount of intercompany deposits. Excluding that bank from the calculations, the industry increased uninsured deposits in the quarter by $92 billion, or 1.4 percent, and growth was widespread among bank size groups. This would have been the industry's first increase in uninsured deposit levels after seven consecutive quarters of decline.

The banking industry continues to face significant downside risks from the continued effects of inflation, volatility in market interest rates, and geopolitical uncertainty. Moreover, the economic outlook remains uncertain, despite sustained economic growth in 2023 that exceeded expectations. These risks could cause credit quality and profitability to weaken, loan growth to slow, provision expenses to rise, and liquidity to become more constrained. Commercial real estate (CRE) loan portfolios, particularly loans backed by office properties, face challenges when loans mature as demand for office space remains weak and property values continue to soften. The FDIC will continue to closely monitor these risk as well as the broader prevailing trends in the banking industry over the coming year.

Condition of the Deposit Insurance Fund

As of December 31, 2023, the Deposit Insurance Fund (DIF) balance declined to $121.8 billion, down $6.4 billion (5.0 percent) from year-end 2022, primarily resulting from an increase

in loss provisions associated with five bank failures during the year.[4] Following the failure of two large banks in March of 2023, the banking industry experienced outflows of total deposits, but also experienced strong insured deposit growth. This growth in insured deposits, coupled with the decline in the DIF balance, resulted in a decline in the reserve ratio of 10 basis points from 1.25 percent as of December 31, 2022, to 1.15 percent as of December 31, 2023.[5]

Philadelphia-based Republic First Bank was closed on April 26, 2024, resulting in an estimated loss of $667 million. This is the only bank to fail so far in 2024 and is not reflected in the DIF balance stated as of December 31, 2023. A total of five banks failed in 2023, resulting in a combined estimated loss at December 31, 2023, of $40.4 billion.[6] As of December 31, 2023, the FDIC estimated the cost for the failures of Silicon Valley Bank (SVB) and Signature Bank to total $23.6 billion. Of that estimated total cost, the FDIC estimates that approximately $20.4 billion was attributable to the cost of covering uninsured depositors as a result of the systemic risk determination made on March 12, 2023, following the closures of SVB and Signature Bank. By statute, that estimated $20.4 billion cost of covering uninsured depositors must be recovered through a special assessment, which was finalized in November 2023.[7] Accordingly, the impact on the DIF from the five bank failures in 2023 is estimated as a loss of $20 billion as of December 31, 2023,[8] which excludes the cost of protecting uninsured depositors

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[4] The decline in the DIF balance does not include the cost of protecting uninsured depositors pursuant to the systemic risk determination announced following the failures of Silicon Valley Bank and Signature Bank in March 2023, as the FDIC is required by statute to recover those losses through special assessments. *See* 12 U.S.C. 1823(c)(4)(G)(ii).

[5] The reserve ratio is calculated as the ratio of the net worth of the DIF (fund balance) to the value of the aggregate estimated insured deposits at the end of a given quarter. See 12 U.S.C. 1813(y)(3).

[6] Information on all bank failures is available at: https://www.fdic.gov/resources/resolutions/bank-failures/failed-bank-list/.

[7] See *Final Rule on Special Assessment Pursuant to Systemic Risk Determination*, available at https://www.govinfo.gov/content/pkg/FR-2023-11-29/pdf/2023-25813.pdf.

[8] Only the remaining estimated loss from SVB and Signature Bank of $3.2 billion, combined with the estimated losses of the three other banks that failed in 2023, directly impact the December 31, 2023 DIF balance. The three other banks that failed in 2023 include First Republic Bank of San Francisco, CA, at an estimated loss of $16.7

as a result of the systemic risk determination. It should be noted that as with all failed bank losses, loss estimates are periodically adjusted as the FDIC, as receiver of the failed banks, sells assets, satisfies liabilities, and incurs receivership expenses. The final cost will be determined when the FDIC terminates the receiverships.

As required by the Federal Deposit Insurance Act (FDI Act),[9] the FDIC has been operating under a restoration plan since September 15, 2020,[10] which aims to restore the DIF to the statutory minimum reserve ratio of 1.35 percent within eight years. Notwithstanding the growth in insured deposits and recent losses due to bank failures, including the April 2024 failure of Republic First Bank, the DIF remains on track to meet the statutory minimum reserve ratio of 1.35 percent by the eight-year deadline of September 30, 2028.[11]

Bank Receiverships

Republic First Bank

On April 26, 2024, Republic First Bank (doing business as Republic Bank), Philadelphia, Pennsylvania, was closed by the Pennsylvania Department of Banking and Securities, which appointed the FDIC as receiver. As of January 31, 2024, Republic Bank had approximately $6 billion in total assets and $4 billion in total deposits. To resolve the bank, the FDIC entered into a Purchase and Assumption Agreement with Fulton Bank, National Association of Lancaster, Pennsylvania, to assume substantially all of the deposits and purchase substantially all the assets of Republic Bank.

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billion, Heartland Tri-State Bank of Elkhart, KS, at an estimated loss of $54.2 million and Citizens Bank of Sac City, IA, at an estimated loss of $14.8 million. Loss estimates are as of December 31, 2023.

[9] Section 7(b)(3)(E) of the Federal Deposit Insurance Act, 12 USC 1817(b)(3)(E), available at https://www.fdic.gov/regulations/laws/rules/1000-800.html#fdic1000sec.7b.

[10] 2020 FDIC Restoration Plan, 85 FR 59306 (Sept. 21, 2020), available at https://www.fdic.gov/news/board-matters/2020/2020-09-15-notice-dis-a-fr.pdf.

[11] Section 7(b)(3)(E) of the FDI Act, 12 USC 1817(b)(3)(E).

2023 Regional Bank Receiverships

Since last appearing before the Committee in November 2023, the FDIC, as Receiver, has continued to make progress in managing and selling the assets retained in receiverships of the three regional banks that failed in 2023.[12] The following highlights some significant recent asset transactions.

Silicon Valley Bank

On January 11, 2024, the FDIC, as Receiver, successfully completed a structured sale of a $36 billion purchase money note issued to the receivership by the acquiring institution, as well as a structured sale of approximately $12.4 billion of Ginnie Mae Project Loan Securities to the Federal Financing Bank (FFB), a government corporation under the general supervision and direction of the Secretary of the Treasury. These transactions generated approximately $42 billion in net proceeds, which were paid to the DIF, the most senior claimant in the receivership. In brief, the FDIC, as Receiver, retained approximately $90 billion of assets and, as of March 31, 2024, has disposed of approximately $85 billion of assets.

Signature Bank

In December 2023, the FDIC, as Receiver, completed the disposition of approximately $33 billion in commercial real estate (CRE) loans from Signature Bank. This portfolio represents substantially all remaining loans retained in the Signature receivership, which totaled approximately $60 billion at the time Signature failed. The majority of the $33 billion in the

[12] On March 20, 2023, the FDIC entered into a purchase and assumption agreement for substantially all deposits and certain loan portfolios of Signature Bridge Bank, National Association, by Flagstar Bank, National Association, Hicksville, NY, a wholly owned subsidiary of New York Community Bancorp, Inc., Westbury, NY. On March 26, 2023, the FDIC entered into a purchase and assumption agreement for all deposits and loans of Silicon Valley Bridge Bank, National Association, by First–Citizens Bank & Trust Company, Raleigh, NC . On May 1, 2023, the FDIC entered into a purchase and assumption agreement with JPMorgan Chase Bank National Association, Columbus, OH, to assume all the deposits and substantially all the assets of First Republic Bank, San Francisco, CA.

CRE loan portfolio is comprised of multifamily properties, primarily located in New York City. A large portion (approximately $15 billion) of the CRE loans are secured by multifamily residences that are rent controlled or rent stabilized (RCRS).

To complete the disposition, the FDIC, as Receiver, conveyed the majority of Signature Bank's CRE loans to joint ventures, three of which included the RCRS loans. The joint venture structure allows the FDIC, as Receiver, to retain a majority ownership interest in the future cash flows of loans contributed to the joint venture. A portion of the equity in each joint venture (between 5 and 20 percent) was widely marketed to banks and non-bank financial institutions through the FDIC's financial advisor, Newmark & Company Real Estate Inc. The winning bidders for each joint venture are responsible for the management, servicing and disposition of loans in the joint venture.

The FDIC, as Receiver, disposed of Signature Bank's CRE portfolio in accordance with its statutory obligations required in the disposition of receivership assets, including the obligations to maximize the net present value return from the sale or disposition of such assets; and, in the case of the RCRS joint ventures, to maximize the preservation of the availability and affordability of residential real property for low-and moderate-income individuals.[13] The winning bidder for the RCRS joint ventures is obligated to facilitate the financial and physical preservation of the underlying collateral, subject to comprehensive monitoring by the FDIC, as Receiver.

In brief, the FDIC, as Receiver, retained approximately $87 billion of assets and, as of March 31, 2024, has disposed of approximately $58 billion of assets.

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[13] See, 12 U.S.C. § 1811(d)(13)(E).

Resolutions under Title II of the Dodd-Frank Act

The ability of the FDIC and other regulatory authorities to manage the orderly resolution of large complex financial institutions remains foundational to the stability of the U.S. financial system. While recognizing the progress that has been made toward enabling such a resolution and ending "too big to fail," the FDIC also recognizes that the resolution of a GSIB has not yet been undertaken. When it becomes necessary to do so, carrying out such a resolution will come with a unique set of challenges and risks. However, an orderly resolution is far more preferable to the alternatives, particularly the alternative of resorting to public support to prop-up a failed institution or to bail-out investors and creditors. Last month, the FDIC released a paper entitled, "Overview of Resolution Under Title II of the Dodd-Frank Act,"[14] which reaffirms that, should the need arise, the FDIC is prepared to apply the resolution framework that it has worked so hard to develop in cooperation with other domestic and global regulatory authorities. Setting out clear expectations regarding how the FDIC will handle its role in managing failures of systemically important financial institutions is itself a key component supporting the execution of an orderly resolution. The FDIC stands ready to engage with all interested parties to address questions and build further understanding of the FDIC's plans and preparedness for executing our Title II Dodd-Frank Act resolution responsibilities for GSIBs.

Efforts to Strengthen the Regulation and Supervision of Banks

Improving the Management of Liquidity and Funding Risks by Banks

Since the regional bank failures in the spring of 2023, the FDIC has focused on several initiatives to improve liquidity and funding risk management at insured financial institutions.

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[14] See, *Overview of Resolution Under Title II of the Dodd-Frank Act* (April 2024); available at https://www.fdic.gov/sites/default/files/2024-04/spapr1024b_0.pdf.

The agency continues to emphasize the importance of sound liquidity risk management practices and robust contingency funding planning for institutions to manage through liquidity stress. Institutions are expected to assess the stability of their funding and maintain a broad range of funding sources that can be accessed during adverse conditions. Contingency funding plans should consider a range of stress scenarios. The FDIC encourages institutions to incorporate the Federal Reserve's discount window as part of their contingency funding arrangements. Effective contingency funding planning encompasses the development of operational capability to use secondary sources, including the discount window, testing these arrangements regularly, and ensuring that collateral is available. Finally, institutions should revise their contingency plans periodically and more frequently as conditions and strategic initiatives change. To underscore and reemphasize these points, the FDIC issued an update to the *Interagency Policy Statement on Funding and Liquidity Risk Management* in July 2023.[15]

Additionally, the FDIC continues efforts to improve the supervision of interest rate and liquidity risk management, asset growth, and reliance on uninsured and less stable deposits. While the FDIC has regularly monitored uninsured deposit trends across the banking industry, the 2023 bank failures highlight the potential vulnerabilities posed by elevated reliance on uninsured deposits. Across the large regional banks, the FDIC relies on a combination of off-site monitoring and on-site supervisory activities to monitor uninsured deposit concentrations. Since the 2023 bank failures, the FDIC has continued to expand our suite of tools using regulatory reporting data to assess deposit trends across individual banks, develop views of risk posed by uninsured deposits to individual banks, and prioritize supervisory activities. The FDIC has

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[15] See *Updated Guidance: Interagency Policy Statement on Funding and Liquidity Risk Management on the Importance of Contingency Funding Plans* (July 28, 2023) available at https://www.fdic.gov/news/financial-institution-letters/2023/fil23039.html.

observed many large regional banks reassessing uninsured deposit outflow assumptions used in internal liquidity stress testing informed by the outflow experiences of the bank failures in 2023. Other observations include the establishment by large regional banks of more granular depositor concentration monitoring and efforts to evaluate the impact of social media and new technologies on deposit stability.

Examiner guidance has been updated to be more explicit about analyses of uninsured deposit concentrations and reemphasize to examiners the importance of forward-looking indicators of risk, such as high growth rates and breaches of internal risk limits. The agency also provided examiner training and guidance on interest rate risk and liquidity risk management, including information on discount window operations.[16] The FDIC continues to coordinate with the federal banking agencies and other financial regulators on liquidity and interest rate risk supervision, training, and policy responses to the stress encountered in the spring of last year.

Strengthening Corporate Governance

The financial crisis of 2008 and the 2023 regional bank failures have taught us that, among other things, IDIs with poor corporate governance and risk management practices are more likely to fail. Reports examining the underlying causes of the 2023 failures noted that poor corporate governance and risk management practices were contributing factors.[17] It is important

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

[17] The FDIC report on the failure of Signature Bank in 2023 found that the root cause of the failure was poor management without adequate risk management practices and controls. The institution's management did not prioritize good corporate governance practices (*FDIC's* Supervision of Signature Bank, April 28, 2023, p. 2; available at: https://www.fdic.gov/sites/default/files/2024-03/pr23033a.pdf.) The Board of Governors of Federal Reserve System's report on the failure of Silicon Valley Bank also identified governance and risk management deficiencies that led to the failure. (*Review of the Federal Reserve's Supervision and Regulation of Silicon Valley Bank*, April 2023, p. 1; available at: https://www.federalreserve.gov/publications/review-of-the-federal-reserves-supervision-and-regulation-of-silicon-valley-bank.htm.) Similar findings are contained in the Office of the Inspector General, Board of Governors of the Federal Reserve System, Consumer Financial Protection Bureau's September 25, 2023 *Material Loss Review of Silicon Valley Bank*; available at: https://oig.federalreserve.gov/reports/board-material-loss-review-silicon-valley-bank-sep2023.htm.

to note that the failure of an IDI usually imposes costs on the DIF and negatively affects its customers, employees, shareholders and the public as a whole.

In October 2023, the FDIC published a Notice of Proposed Rulemaking to add a new Appendix C to the FDIC's safety and soundness regulation, 12 CFR 364 (Corporate Governance NPR),[18] to incorporate guidelines on corporate governance and risk management for FDIC-supervised IDIs with consolidated assets of $10 billion or more.[19] The FDIC accepted public comments through February 9, 2024 and is currently reviewing the comments received.

An effective governance framework is necessary for an IDI to remain profitable, competitive, and resilient through changing economic and market conditions. The FDIC's current safety and soundness standards for FDIC-supervised IDIs, as set forth in Appendix A of the safety and soundness regulation and supervisory guidance on corporate governance and risk management, provide baseline corporate governance and risk management expectations for IDIs of all sizes.

However, the FDIC believes larger, more complex IDIs require more sophisticated and formal corporate governance and risk management structures and practices. The proposed guidelines would clarify the FDIC's longstanding expectation that corporate governance and risk management frameworks need to evolve along with the growth, complexity and changing business models and risk profiles of larger IDIs.

In drafting the Corporate Governance NPR, staff studied both the OCC's and the Federal Reserve Board's rules and guidance, and these Proposed Guidelines are intended to be generally consistent with the goals communicated through the Office of the Comptroller of the Currency's

[18] 88 F.R. 70391 (October 11, 2023).
[19] The NPR was issued under the safety and soundness authority provided by Section 39 of the Federal Deposit Insurance Act, which authorizes the FDIC to take formal action if an institution fails to submit and implement, upon FDIC request, an acceptable plan to achieve compliance with safety and soundness standards.

(OCC)[20] and Federal Reserve Board's[21] published issuances in an effort to harmonize corporate governance and risk management requirements for covered institutions that present a higher risk profile with those applicable to entities supervised by the other Federal banking agencies. A notable difference is in the application of the requirements to IDIs over of $10 billion where the other agencies' apply requirements to entities over $50 billion. While the FDIC has long expected that larger banks do need more sophisticated risk management and governance systems and should not wait to develop them, the FDIC is aware and will consider commenters' thoughtful views on this important topic and others before finalizing the guidelines.

The experience of the three large IDI failures last spring demonstrate the need for meaningful action to improve the corporate governance and risk management processes of large IDIs. The governance and risk management standards put forward in this Corporate Governance NPR would be a significant step in that direction.

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[20] See OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches; Integration of Regulations, 79 FR 54518 (Sept. 11, 2014), https:// www.federalregister.gov/documents/2014/09/11/ 2014-21224/occ-guidelines-establishing-heightenedstandards-for-certain-large-insured-national-banksinsured; OCC, Comptroller's Handbook—Corporate and Risk Governance, https://www.occ.gov/ publications-and-resources/publications/ comptrollers-handbook/files/corporate-riskgovernance/index-corporate-and-riskgovernance.html.

[21] See 12 CFR 252.22, subpart C—Risk Committee Requirements for Bank Holding Companies with Total Consolidated Assets of $50 Billion or More and Less Than $100 Billion. The Federal Reserve Board initially set the application of risk committee requirements under Regulation YY, among other requirements, for banks with total consolidated assets of $10 billion or more pursuant to Section 165 of the Dodd-Frank Act of 2010. 79 FR 17239, 17248 (Mar. 27, 2014). This threshold was raised from $10 billion to $50 billion pursuant to changes made under the Economic Growth, Regulatory Relief, and Consumer Protection Act of 2018. 84 FR 59032, 59055 (Nov. 1, 2019). 9See SR 16–11: Supervisory Guidance for Assessing Risk Management at Supervised Institutions with Total Consolidated Assets Less than $100 Billion (June 8, 2016; revised and reposted February 17, 2021, p. 3). SR letter 95–51, Rating the Adequacy of Risk Management Processes and Internal Controls at State Member Banks and Bank Holding Companies (Nov. 14, 1995; revised Feb. 26, 2021) remains applicable to state member banks and bank holding companies with $100 billion or more in total assets.

Basel III Proposal

On September 18, 2023, the FDIC, the OCC and the Federal Reserve published a Notice of Proposed Rulemaking (Basel III NPR) that would revise and strengthen the capital requirements applicable to the largest banking organizations.[22]

The Basel III NPR is a continuation of the federal banking agencies' efforts to revise the regulatory capital framework for our nation's largest financial institutions, which were found to be undercapitalized and over-leveraged during the global financial crisis of 2008. Following the 2008 crisis, the federal banking agencies strengthened the banking system through an initial set of revisions to the capital framework.[23] Those revisions raised the quality and quantity of risk–based capital and included the introduction of an enhanced supplementary leverage ratio for our largest, most systemic banking organizations. However, there remained areas of the regulatory capital framework that need improvement.

The Basel III NPR would make important changes to address the capital weaknesses identified in the 2008 financial crisis, enhance the resilience and stability of the banking system, and enable the banking system to better serve the U.S. economy. For example, the proposal would address critical areas of the risk–based capital framework related to credit risk, operational risk, market risk, and financial derivative risk. Taken together, these changes would bolster the financial resilience of our nations' largest banking organizations.

The agencies extended the comment period until January 16, 2024 to allow interested parties additional time to analyze the issues and prepare their comments.[24] The agencies have

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[22] 88 F.R. 64018 (September 18, 2023).
[23] See, for example, *Regulatory Capital Rules, etc.*, 78 F.R. 55340 (September 10, 2013).
[24] 88 F.R. 73770 (October 27, 2023).

received over 400 unique comments. The comments have been very helpful in identifying areas of the proposal that may warrant changes in a final rule. For example, concerns have been raised related to the proposed treatment for residential mortgage exposures, certain tax credit equity investments, trading activities, and banking activities that generate large amounts of fee-based revenue. The FDIC continues to consider the comments and engage with our fellow regulators in developing a final rule.

Long-Term Debt and Resolution Planning Proposals

The FDIC, together with the Federal Reserve and the OCC, issued a Notice of Proposed Rulemaking on September 19, 2023, entitled *Long-Term Debt Requirements for Large Bank Holding Companies, Certain Intermediate Holding Companies of Foreign Banking Organizations, and Large Insured Depository Institutions*. (LTD Proposal).[25] The proposed long-term debt requirement could mitigate resolution challenges encountered in the failure of large regional banks and bolster financial stability. Long-term debt would absorb losses before the depositor class – uninsured depositors and the FDIC – take losses. This would decrease the incentive for uninsured depositors to run. Long-term debt would protect the DIF, helping to make large regional bank resolutions more orderly, and creating additional options for the FDIC in resolution. Long-term debt would make it more likely that a resolution transaction could satisfy the statutory least-cost requirement without the need for a systemic risk exception, whether by a closing weekend sale or the use of a bridge depository institution.

[25] 88 F.R. 64524 (September 19, 2023).

The LTD Proposal's comment period was extended to January 16, 2024.[26] The agencies received 48 comments on the LTD Proposal, which FDIC staff is considering as we work with our colleagues at the Federal Reserve and OCC to finalize this proposal.

In addition to comments received on the LTD proposal, the FDIC is carefully considering comments related to proposed changes to IDI resolution plans,[27] and with the Federal Reserve, the FDIC is carefully considering comments related to proposed guidance for certain firms that submit Title I resolution plans.[28]

Other Regulatory Initiatives

Reviewing the Bank Merger Process

On March 21, 2024, the FDIC Board approved a revised Statement of Policy on Bank Merger Transactions (Proposed Statement of Policy) for publication in the Federal Register for a 60-day comment period.[29] [30] The Proposed Statement of Policy would update, strengthen, and clarify the FDIC's policies related to the evaluation of bank merger applications subject to FDIC approval under the Bank Merger Act (BMA).[31] The Proposed Statement of Policy reflects legislative and other developments that have occurred since the last amendment in 2008, including the establishment of the statutory factor regarding the risk to the stability of the United

[26] 88 F.R. 83364 (November 29, 2023).
[27] *Resolution Plans Required for Insured Depository Institutions With $100 Billion or More in Total Assets; Informational Filings Required for Insured Depository Institutions With at Least $50 Billion But Less Than $100 Billion in Total Assets,* 88 FR 64579 (September 19, 2023).
[28] *Guidance for Resolution Plan Submissions of Domestic Triennial Full Filers,* 88 F.R. 64626 (September 19, 2023); and "*Guidance for Resolution Plan Submissions of Foreign Triennial Full Filers*," 88 F.R. 64641 (September 18, 2023).
[29] FDIC Press Release *FDIC Seeks Public Comment on Proposed Revisions to its Statement of Policy on Bank Merger Transactions* (March 21, 2024); available at: https://www.fdic.gov/news/press-releases/2024/pr24017.html.
[30] In a separate Federal Register notice, the FDIC, as part of its obligations under the Paperwork Reduction Act of 1995, invited comment on the renewal of the existing information collection found in the FDIC Supplement to the Interagency Bank Merger Act application form. 89 F.R. 17848 (March 12, 2024).
[31] Section 18(c) of the FDIC Act, 12 U.S.C. § 1828(c).

States banking or financial system. The Proposed Statement of Policy is more principles based; addresses each statutory factor separately; and highlights other relevant matters and considerations, such as related statutes pertaining to interstate mergers, and applications from non-banks or banks that are not traditional community banks.

The Proposed Statement of Policy reflects consideration of comments received in response to the FDIC's 2022 *Request for Information and Comment on Rules, Regulations, Guidance, and Statements of Policy Regarding Bank Merger Transactions* (2022 RFI).[32] The 2022 RFI solicited comments regarding the effectiveness of the existing framework of the laws, practices, rules, regulations, guidance, and statements of policy in meeting the statutory requirements of the BMA.

Rulemaking Implementing Section 956 of Dodd-Frank – Preventing Misaligned Incentive-Based Compensation

Section 956 of the Dodd-Frank Act[33] addresses an important lesson from the financial crisis of 2008: poorly designed financial institution compensation programs can provide incentives for short-term risk taking that can jeopardize the safety and soundness of the institution. Misaligned incentive-based compensation for executives continues to play a role in the failure of banks. Material Loss Reviews of the 2023 regional bank failures identified common weaknesses that included an excessive focus on growth and short-term profitability, and a lack of risk metrics in compensation policies and practices that may have encouraged excessive risk taking.[34]

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[32] See, 87 F.R. 18740 (March 31, 2022).
[33] Pub. L. No. 111-203, 124 Stat. 1376 (2010).
[34] See, for example, FDIC Office of Inspector General's *Material Loss Review of Signature Bank of New York* (October 23, 2023), available at https://www.fdicoig.gov/sites/default/files/reports/2023-10/EVAL-24-02.pdf.

This month, the FDIC took steps to initiate a joint rulemaking implementing Section 956 by approving for publication a notice of proposed rulemaking (Section 956 NPR), as required by statute.[35] Implementation of the section will provide a critical tool to control excessive risk taking by financial institution executives by aligning their compensation with the long-term safety and soundness of their institutions rather than short-term profits.

The Section 956 NPR re-proposes the rule text previously proposed in June 2016,[36] along with proposed alternatives and questions in the preamble. The proposal uses a tiered approach corresponding to the size of the institution.[37] One of the key provisions applicable to larger covered institutions would require deferral of a certain minimum amount of compensation of senior executive officers and other employees who can expose the institution to material levels of risk, known as significant risk-takers. The proposal would also require those deferred amounts to be considered for forfeiture and downward adjustment and clawback, in the event of undue risk taking. Deferral provides an important mechanism to discourage inappropriate risk-taking by allowing time to pass to evaluate the outcomes of risk-taking behavior and to adjust incentive-based compensation accordingly. The FDIC looks forward to reviewing and considering public comments on the Section 956 NPR.

Implementing the CRA Final Rule

On October 24, 2023, the FDIC, together with the Federal Reserve and the OCC, finalized the first comprehensive rewrite of the Community Reinvestment Act (CRA)

[35] Section 956 of the Dodd-Frank Act requires the FDIC, OCC, Federal Reserve, National Credit Union Administration, Securities Exchange Commission and Federal Housing Finance Agency to jointly issue regulations or guidelines to implement the provision. Once all six agencies have approved the Section 956 NPR, it will be published in the Federal Register with a comment period of 60 days following publication.
[36] 81 F.R. 37670 (June 10, 2016).
[37] "Covered financial institutions" are financial institutions with at least $1 billion in assets. Section 956(e) of the Dodd-Frank Act.

Regulations in 25 years. The CRA, since its enactment in 1977, has been the foundation of access to credit, investment, and basic banking services on a responsible basis for low- and moderate-income communities and communities of color in the United States. The new CRA rule issued by the federal banking agencies adapts CRA to the changing nature of the banking business and strengthens its provisions to carry out its critically important public purpose. The FDIC is firmly committed to the support of the rule and believe it is entirely consistent with the statute.

Protecting Consumers from Misrepresentations about Deposit Insurance

To protect consumers from misrepresentations by some crypto companies regarding FDIC insurance, in 2022, the FDIC issued an advisory to FDIC-insured institutions and published consumer educational materials on deposit insurance.[38] In December 2023, the FDIC updated its regulation entitled, *Advertisement of Membership, False Advertising, Misrepresentation of Insured Status, and Misuse of the FDIC's Name or Logo*.[39] The regulation requires the use of signs that differentiate insured deposits from non-deposit products and that disclose that "non- deposit products" are not insured by the FDIC, are not deposits, and may lose value. Among other changes, the amended regulation now includes crypto assets in the regulatory definition of "non-deposit product."

In connection with crypto-related activities, in 2023 and 2024, the FDIC issued a number of direct letters demanding persons or entities cease and desist from making false or misleading

[38] See, *Advisory to FDIC-Insured Institutions Regarding Deposit Insurance and Dealings with Crypto Companies, FIL-35-2022;* available at: https://www.fdic.gov/news/financial-institution-letters/2022/fil22035.html; and *Fact Sheet: What the Public Needs to Know About FDIC Deposit Insurance and Crypto Companies*; available at https://www.fdic.gov/news/fact-sheets/crypto-fact-sheet-7-28-22.html.

[39] 12 C.F.R. 328 Advertisement of Membership, False Advertising, Misrepresentation of Insured Status, and Misuse of the FDIC's Name or Logo.

representations about the existence of deposit insurance, misusing the name or logo of the FDIC, or knowingly misrepresenting the extent and manner of deposit insurance.[40]

Eliminating Unnecessary Regulatory Burden – the EGRPRA Process

The FDIC remains keenly aware of the regulatory burden that community banks currently face. In its assessment of regulatory burden in the current environment, the FDIC is cognizant of the importance of balancing safety and soundness and consumer protection regulation with the legitimate business interest of the banks. The FDIC, together with the OCC and the Federal Reserve, initiated the third decennial review under the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA)[41] that requires the agencies to review their regulations to identify those that are outdated, unnecessary, or unduly burdensome and to eliminate such requirements to the extent appropriate.

To facilitate this review, the agencies divided their regulations into 12 categories. On February 6, 2024, the agencies published a solicitation for comment on three categories of regulations*: Applications and Reporting, Powers and Activities, and International Operations*,[42] asking the public to identify regulations they believe are outdated, unnecessary, or unduly burdensome. The comment period remained open for 90 days and closed on May 6, 2024. Over the next two years, the agencies will request comment on the regulations in the remaining categories. In addition, the agencies also plan to hold outreach meetings where interested parties may comment on applicable regulatory requirements directly to the agencies.

[40] See, for example, *FDIC's Letter to Organo Payments, Inc.* (January 19, 2024): https://www.fdic.gov/resources/regulations/laws/section-18a4-of-fdi-act/letters/2024-01-19-ogpay.pdf; and *FDIC's Letter to Horizon Globex GmbH* (January 19, 2024): https://www.fdic.gov/resources/regulations/laws/section-18a4-of-fdi-act/letters/2024-01-19-upstream.pdf.
[41] 12 U.S.C. § 3311.
[42] 89 F.R. 8084 (February 6, 2024).

At the conclusion of the review, the agencies will publish in the *Federal Register* a summary of the comments received, identifying and discussing the significant issues raised; and submit a report to Congress shortly thereafter. The report will address any significant issues raised by the public, the relative merits of such issues, and whether the agencies have the ability to address regulatory burden through regulation, or whether such burdens must be addressed by legislative action. The FDIC stands ready to address the issues raised during this process in a manner consistent with bank safety and soundness, the protection of consumers and financial stability.

Enhancing Examiner Resources

In the FDIC Chief Risk Officer's report on the FDIC's supervision of Signature Bank, the Chief Risk Officer identified examiner resources as one of the challenges affecting the timeliness and quality of examinations of Signature Bank. Since the issuance of the Chief Risk Officer Report, to insure adequate examination resources going forward, the FDIC has taken a number of actions. To enhance the attractiveness of dedicated examiner positions, the FDIC elevated several positions and instituted incentive payments for certain key staff. To address the high cost of living in San Francisco, New York, Seattle, and Los Angeles, the FDIC is offering a payment supplement in those areas. Additionally, to address higher attrition rates among pre-commissioned examiners in 2021 and 2022, the FDIC increased the commissioning payment in return for a two-year service commitment. Finally, the FDIC is making use of retention payments to retain its retirement-eligible examiner cadre while staffing is bolstered.

These steps are showing positive results, with reduced attrition among pre-commissioned examiners in 2023. The FDIC has also continued to see strong interest among candidates for

entry level positions with two of the largest groups of qualified applicants received in the last six months. The FDIC continues to bring in a substantial class of examiner candidates each year.

Conclusion

I appreciate the opportunity to appear before you today to report on our efforts to address the workplace culture of the FDIC, create a workplace where every FDIC employees feels safe, valued and respected, and fulfill the FDIC's core mission to maintain stability and public confidence in the U.S. financial system through its responsibilities for deposit insurance, banking supervision, and the orderly resolution of failed banks.

I look forward to answering your questions.