MAXINE WATERS, CA
CHAIRWOMAN

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

PATRICK MCHENRY, NC
RANKING MEMBER

May 13, 2019

Memorandum

To: Members, Committee on Financial Services

From: FSC Majority Staff

Subject: May 16, 2019, "Oversight of Prudential Regulators: Ensuring the Safety, Soundness and Accountability of Megabanks and Other Depository Institutions."

The Committee on Financial Services will hold a hearing entitled, "Oversight of Prudential Regulators: Ensuring the Safety, Soundness and Accountability of Megabanks and Other Depository Institutions," at 10:00 a.m. on Thursday, May 16, 2019, in room 2128 of the Rayburn House Office Building. This will be a single-panel hearing with the following witnesses:

- **The Honorable Rodney Hood,** Chairman, National Credit Union Administration
- **The Honorable Jelena McWilliams,** Chairman, Federal Deposit Insurance Corporation
- **The Honorable Joseph Otting**, Comptroller, Office of the Comptroller of the Currency
- **The Honorable Randal Quarles,** Vice Chairman of Supervision, Board of Governors of the Federal Reserve System

Overview

The responsibility for prudential regulation of insured depository institutions is divided among four Federal regulators consisting of the Board of Governors of the Federal Reserve System (Federal Reserve), Federal Deposit Insurance Corporation (FDIC), Office of the Comptroller of the Currency (OCC), and the National Credit Union Administration (NCUA). Section 1108 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) created the position of Vice Chairman for Supervision for the Federal Reserve, and requires the Vice Chairman to testify before the Committee at semi-annual hearings.[1] While the OCC, FDIC and NCUA do not have such mandatory testimony requirements, receiving testimony from all four agencies allows for a comprehensive examination of the state of prudential regulation, supervision, and enforcement with respect to megabanks and other depository institutions, such as community banks and credit unions.[2]

Background

Regulation of depository institutions in the United States has evolved into a system with multiple regulators. Each depository institution is subject to regulation by its chartering authority: state or federal. Even if state chartered, virtually all depository institutions are federally insured, so both state and federal

---

[1] 12 U.S.C. § 247b.

[2] For more information, *see* Congressional Research Service (CRS), "Banking Policy Issues in the 116th Congress" (Feb. 21, 2019), https://www.crs.gov/Reports/R45518; and CRS, "Introduction to Bank Regulation: Credit Unions and Community Banks: A Comparison" (Dec. 14, 2018), https://www.crs.gov/Reports/IF11048. For the most recent annual reports from each of the agencies, *see* Federal Reserve: https://www.federalreserve.gov/publications/annual-report.htm, OCC: https://www.occ.gov/annual-report/, FDIC: https://www.fdic.gov/about/strategic/report/index.html, and NCUA: https://www.ncua.gov/news/annual-reports. *See also* https://www.federalreserve.gov/publications/supervision-and-regulation-report.htm, https://www.federalreserve.gov/publications/financial-stability-report.htm, and https://www.occ.treas.gov/publications/publications-by-type/semiannual-risk-perspective/index-semiannual-risk-perspective.html.

institutions are subject to at least one federal primary regulator that examines the institution for safety and soundness, as well as compliance with federal banking laws. Depository institutions have three broad types of charters—commercial banks, thrifts (also known as "savings and loans"), and credit unions. The Federal Reserve supervises state-chartered banks that are members of the Federal Reserve System, bank and thrift holding companies and their non-depository institution subsidiaries, nonbanking activities of foreign banking organizations, and certain large nonbank financial companies and financial market utilities designated by the Financial Stability Oversight Council (FSOC).[3] The OCC charters and supervises national banks and thrifts as well as federally licensed branches and agencies of foreign banks. The FDIC supervises state-chartered banks that are not members of the Federal Reserve System and insures all bank deposits, and the NCUA supervises all federal credit unions along with certain state credit unions that are federally insured. While the four prudential regulators supervise depository institutions with less than $10 billion in assets for compliance with consumer protection laws, the Consumer Financial Protection Bureau (Consumer Bureau) is responsible for writing consumer protection rules, and supervises depository institutions with more than $10 billion for compliance with such rules.[4]

As of December 31, 2018, there were 5,406 FDIC-insured commercial banks and savings institutions[5] that held a combined $17.9 trillion in assets and $13.8 trillion in deposits. These banks range in size: 9 banks held more than $250 billion in total assets (0.1 percent of all banks),[6] 128 banks had between $10 billion and $250 billion in assets (2.3 percent), 638 banks had between $1 billion and $10 billion in assets (12 percent), and 4,631 banks had fewer than $1 billion in assets (85 percent). There were 149 minority depository institutions (MDIs).[7] Last year, the banking industry made a record $236.7 billion in profit, an increase of 44 percent over the previous year. During 2018, eight new banks were chartered, 259 banks were absorbed by mergers, and there were no bank failures. Bank lending increased by $431.2 billion, or 4.4 percent, last year, with commercial and industry loans increasing by 7.8 percent and consumer loans increasing by 3.9 percent. Community banks hold 42 percent of small loans to businesses.[8]

With respect to credit unions, as of December 31, 2018, there were 5,375 federally insured credit unions with a combined $1.45 trillion in assets and $1.2 trillion in deposits. Credit unions also range in size, though they tend to be smaller than banks. According to data from the NCUA, 25 percent of credit unions held less than $9.2 million in assets, 50 percent held less than $33.2 million in assets, and 75 percent held less than $129.2 million in assets. There were 529 credit union MDIs at the end of 2018.[9] Credit unions added 4.9 million members over the year, with a total credit union membership of 116.2 million by the end of 2018. Credit union lending increased overall by 9 percent last year, with auto loans increasing by 10 percent, credit card balances increasing by 7.5 percent, non-federally guaranteed student loans increasing by 17 percent, and commercial loans increased by 12.6 percent.[10]

---

[3] The leaders of the four prudential regulators are voting members of the FSOC. In the last few years, FSOC has de-designated all nonbank financial companies, removing them from the Federal Reserve's oversight. There are eight FMUs subject to oversight by the Federal Reserve, along with the SEC and CFTC. *See* U.S. Department of the Treasury, "Designations," https://www.treasury.gov/initiatives/fsoc/designations/Pages/default.aspx.

[4] *See* CRS, "Who Regulates Whom? An Overview of the U.S. Financial Regulatory Framework" (Aug. 17, 2017), https://www.crs.gov/Reports/R44918.

[5] In the decades leading up to 1980, the total number of banks fluctuated around 13,000 to 14,000. Since the mid-1980s, there has been a steady decline of banks at a rate of about 300 per year, often through mergers and acquisitions, as many banks took advantage of interstate banking rules in the 1980s and 1990s to expand their geographic footprint. *See* Sarah Edelman, Director of Housing Policy, Center for American Progress, Testimony before the Senate Subcommittee on Financial Institutions and Consumer Protection, "The State of Rural Banking: Challenges and Consequences," (Oct. 28, 2015), https://www.banking.senate.gov/imo/media/doc/EdelmanTestimony102815FICP.pdf.

[6] For a list of the largest bank holding companies, *see* https://www.ffiec.gov/nicpubweb/nicweb/hcsgreaterthan10b.aspx.

[7] This compares to 215 bank MDIs at the end of 2008. For data and more information about bank MDIs, *see* https://www.fdic.gov/regulations/resources/minority/mdi.html.

[8] FDIC, "Quarterly Banking Profile – Fourth Quarter 2018" (Feb. 21, 2019), https://www.fdic.gov/bank/analytical/quarterly/.

[9] NCUA, "Minority Depository Institution Preservation," https://www.ncua.gov/support-services/credit-union-resources-expansion/resources/minority-depository-institution-preservation.

[10] *See* NCUA, "Quarterly Credit Union Data Summary – 2018 Q4," https://www.ncua.gov/analysis/credit-union-corporate-call-report-data/quarterly-data-summary-reports; and NCUA 2018 Annal Report, https://www.ncua.gov/files/annual-reports/annual-report-2018.pdf.

Supervisory and Regulatory Developments

Since the financial crisis of 2007-2009, financial regulation has evolved significantly. In 2010, Congress passed the Dodd-Frank Act into law to address many of the regulatory failures that contributed to the financial crisis. In addition to implementing Dodd-Frank rules, regulators have implemented the Basel III capital reforms to strengthen the resiliency of the banking system.[11] Since 2017, the Trump Administration has made financial deregulation a top priority, with the Department of the Treasury issuing a series of reports with recommendations for regulatory and legislative reforms.[12] Last year, Congress passed S. 2155 into law, which included various deregulatory provisions, which regulators are in the process of implementing.[13] Below is a brief summary of recent supervisory and regulatory developments.

Oversight of Megabanks: There are eight U.S. banks that have been designated as global systemically important banks (G-SIBs) that hold a combined $11.1 trillion in assets, comprising roughly 50 percent of domestic banking assets.[14] On March 12, 2019, the Committee held a hearing with the now former CEO of Wells Fargo to examine the megabank's repeated violations of the law and consumer abuses.[15] On April 10, 2019, the Committee held a hearing with the CEOs of the other seven U.S. G-SIBs to examine developments over the past decade since the last time the megabank CEOs testified before the Committee.[16] The hearings examined concerns that ongoing regulatory compliance failures by megabanks, many of which result in consumer harm, remain prevalent. U.S. G-SIBs made $780 billion in profits over the last 10 years while paying at least $163.7 billion in fines, though there have been few examples where prudential regulators utilized their extensive authorities to impose more severe penalties.[17]

Capital, Stress Testing and Living Will Requirements: Regulators have advanced several proposals to change bank capital and leverage requirements. In April 2018, the Federal Reserve issued a set of proposals to revise its capital rules for G-SIBs and introduced a "stress capital buffer," or SCB, which would in part integrate the forward-looking stress test results with the Board's non-stress capital requirements.[18] The Federal Reserve joined the OCC in releasing a second proposal to substantially alter the current enhanced supplementary leverage ratio (eSLR) that applies to G-SIBs.[19] The FDIC estimated the eSLR proposal would lower capital requirements for the primary federally-insured bank subsidiary of each G-SIB by a combined $121 billion. In October 2018, the Federal Reserve, FDIC and OCC released proposals to implement S. 2155 that would tailor the application of prudential standards to large banks, proposing to establish four categories of large banks based on asset size and cross-border activity.[20] In March 2019, the Federal Reserve decided not to deploy the countercyclical capital buffer that would

[11] *See* CRS, "Overview of the Prudential Regulatory Framework for U.S. Banks: Basel III and the Dodd-Frank Act" (Jul. 27, 2016) https://www.crs.gov/Reports/R44573.

[12] *See* U.S. Department of The Treasury, "Regulatory Reform," https://home.treasury.gov/policy-issues/top-priorities/regulatory-reform.

[13] *See* CRS, "Economic Growth, Regulatory Relief, and Consumer Protection Act (P.L. 115-174) and Selected Policy Issues" (Jun. 6, 2018), https://www.crs.gov/Reports/R45073 and Americans for Financial Reform, "The Senate's Dangerous Financial Deregulation Bill (S 2155)," https://ourfinancialsecurity.org/senate-financial-deregulation-package-crapo-bill/.

[14] *Supra* note 6; *see also* U.S. Department of The Treasury, "A Financial System That Creates Economic Opportunities- Banks and Credit Unions" (Jun. 2017), https://www.treasury.gov/press-center/press-releases/documents/a%20financial%20system.pdf.

[15] *See* FSC, "Holding Megabanks Accountable: An Examination of Wells Fargo's Pattern of Consumer Abuses" (Mar. 12, 2019), https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=402383.

[16] *See* FSC, "Holding Megabanks Accountable: A Review of Global Systemically Important Banks 10 years after the Financial Crisis" (Apr. 10, 2019), https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=402507.

[17] Democratic Staff of the Committee, "The Case for Holding Megabanks Accountable: An Examination of Wells Fargo's Egregious Consumer Abuses" (Sep. 27, 2017), https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=400807.

[18] *See* Federal Reserve, "Federal Reserve Board seeks comment on proposal to simplify its capital rules for large banks while preserving strong capital levels that would maintain their ability to lend under stressful conditions" (Apr. 10, 2018), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180410a.htm.

[19] *See* Federal Reserve, "Rule proposed to tailor 'enhanced supplementary leverage ratio' requirements" (Apr. 11, 2018), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180411a.htm.

[20] *See* Federal Reserve, "Notices of proposed rulemaking to tailor prudential standards" (Oct. 24, 2018), https://www.federalreserve.gov/aboutthefed/boardmeetings/files/board-memo-20181031.pdf.

require large banks to build additional capital,[21] and made revisions to the stress-testing regime to limit the use of the "qualitative objection,"[22] which may make it easier for large banks to pass their stress tests.[23] In April, regulators proposed easing prudential standards for foreign banks,[24] and modifying large bank resolution plans (referred to as "living wills") so that for many large banks would submit plans every three years.[25] These proposals have received a range of criticisms, including opposition from Federal Reserve Governor Lael Brainard and FDIC Board Member Marty Gruenberg.[26]

Volcker Rule: In May and June of 2018, the prudential regulators, along with the Securities and Exchange Commission (SEC) and Commodity Future Trading Commission (CFTC), issued a joint proposal to significantly modify the Volcker Rule.[27] However, there have been recent news reports that suggest the regulators are considering revising the proposal in response to industry pressure.[28]

Community Reinvestment Act: On August 28, 2018, the OCC issued an Advanced Notice of Proposed Rulemaking (ANPR) related to modernizing the Community Reinvestment Act (CRA),[29] receiving nearly 1,500 comments.[30] While the Federal Reserve and FDIC are working with the OCC to review the ANPR comments, stakeholders have expressed concerns about the ANPR and fears that the OCC may unilaterally make changes to CRA regulations, creating the potential for regulatory arbitrage.[31]

Bank Mergers and Acquisitions: Concerns have been raised about federal financial regulators rubber stamping prior merger and acquisition applications. For example, based on data provided by the Federal Reserve, from January 1, 2006 through December 31, 2017, over 3,800 merger applications were submitted to the agency. During this eleven-year period, however, the Federal Reserve did not reject *any* merger application.[32] Earlier this year, BB&T and SunTrust announced their intentions to merge and create the sixth-largest bank in the U.S. While the Federal Reserve and FDIC recently held two public hearings,[33] a number of concerns persist about the merger's impact on rural and underserved markets.[34]

Financial Technology: Prudential regulators have engaged on financial technology (fintech) in various ways. For example, the OCC established an Office of Innovation and has begun accepting

[21] *See* Federal Reserve, "Federal Reserve Board votes to affirm the Countercyclical Capital Buffer (CCyB) at the current level of 0 percent" (Mar. 6, 2019), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190306c.htm.
[22] *See* Federal Reserve, "Federal Reserve Board announces it will limit the use of the "qualitative objection" in its Comprehensive Capital Analysis and Review (CCAR) exercise, effective for the 2019 cycle" (Mar. 6, 2019), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190306b.htm.
[23] Alan Rappeport and Emily Flitter, "Regulators Move to Ease Post-Crisis Oversight of Wall Street," New York Times (Mar. 6, 2019), https://www.nytimes.com/2019/03/06/business/bank-regulation.html.
[24] *See* Federal Reserve, "Federal Reserve Board invites public comment on regulatory framework that would more closely match rules for foreign banks with the risks they pose to U.S. financial system" (Apr. 8, 2019), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190408a.htm.
[25] *See* FDIC, "Agencies Invite Comment on Modifications to Resolution Plan Requirements; Proposal Keeps Existing Requirements for Largest Firms and Reduces Requirements for Firms with Less Risk" (Apr. 16, 2019), https://www.fdic.gov/news/news/press/2019/pr19035.html.
[26] For example, *see* Hannah Lang, "The Fed's Lael Brainard stands alone," American Banker (May 5, 2019), https://www.americanbanker.com/news/the-feds-lael-brainard-stands-alone and FDIC, "Statement of Martin J. Gruenberg, Chairman, FDIC, Notice of Proposed Rulemaking on Supplementary Leverage Ratio Issued by the Federal Reserve and OCC" (Apr. 11, 2018), https://www.fdic.gov/news/news/speeches/spapr1218.html.
[27] *See* "Federal Reserve Board asks for comment on proposed rule to simplify and tailor compliance requirements relating to the "Volcker rule"" (May 30, 2018), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20180530a.htm.
[28] Jesse Hamilton and Benjamin Bain, "Wall Street Nears a Big Win in the Latest Revamp of Volcker Rule," Bloomberg (Apr. 25, 2019), https://www.bloomberg.com/news/articles/2019-04-25/wall-street-nears-a-big-win-in-the-latest-revamp-of-volcker-rule.
[29] *See* OCC, Advance Notice of Proposed Rulemaking for Community Reinvestment Act (Aug. 28, 2018), https://www.occ.gov/news-issuances/bulletins/2018/bulletin-2018-24.html.
[30] *See* OCC. Public Submissions to Reforming the Community Reinvestment Act Regulatory Framework, https://www.regulations.gov/docketBrowser?rpp=50&so=DESC&sb=postedDate&po=0&dct=PS&D=OCC-2018-0008.
[31] *See* FSC, "The Community Reinvestment Act: Assessing the Law's Impact on Discrimination and Redlining" (Apr. 9, 2019), https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=402505.
[32] *See* Letter from Chairman Powell to Senator Warren regarding bank mergers and acquisitions (May 10, 2018), https://www.warren.senate.gov/imo/media/doc/Powell%20Response%20re%20Mergers.pdf.
[33] *See* Federal Reserve, BB&T/SunTrust Application and related materials (May 10, 2019), https://www.federalreserve.gov/foia/bbt-suntrust-application-materials.htm.
[34] *See* Letter from Chairwoman Waters to Federal Reserve Board Chairman Powell and FDIC Chairman McWilliams regarding proposed merger between BB&T and SunTrust (May 8, 2019), https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=403735.

applications for a Special Purpose National Bank Charter from fintech companies, though state banking regulators have challenged the OCC's authority to issue such charters.[35] The Federal Reserve issued a proposal to create a real-time payments system.[36] The FDIC is setting up an innovation office, and is considering an applications from a fintech company for an Industrial Loan Corporation (ILC) charter.[37]

Credit Union Reforms: There have been a number of regulatory proposals and reforms NCUA has advanced in recent years, including extending the examination cycle for well-capitalized and well-managed credit unions, modernizing NCUA's field of membership rules, and modifications to centralize NCUA's appeal process for credit unions.[38] In addition, in October 2018, NCUA amended its 2015 risk-based capital rule to delay the effective date until January 1, 2020, and raise the asset threshold from $100 million to $500 million in assets.[39]

Regulatory Guidance after a Government Shutdown: On January 11, 2019, the prudential regulators issued a joint statement to provide guidance to financial institutions, encouraging them to help consumers affected by the shutdown.[40] Coming in response to a letter Chairwoman Waters sent to the regulators the previous day,[41] the guidance did not come until the 20th day of the shutdown. Regulators issued similar guidance on October 9, 2013,[42] the 9th day of that government shutdown.

Legislative Proposals

The Committee will also review several legislative proposals:

- Discussion Draft of Megabank Oversight Act, which would require U.S. G-SIBs to annually report and testify before Congress on their activities.
- Discussion Draft of Prudential Regulator Oversight Act, which would require the Federal Reserve, OCC, FDIC and NCUA to semi-annually report and annually testify before Congress on their supervisory and regulatory activities. The Federal Reserve Vice Chairman for Supervision would continue to testify semi-annually before Congress, though the new annual testimony mandate would satisfy one of the semi-annual requirements.
- H.R. 2290, Shutdown Guidance for Financial Institutions Act (Wexton), which would require regulators to issue guidance to encourage financial institutions to help consumers and businesses affected by a shutdown in a manner consistent with safety and soundness.

[35] *See* OCC, Responsible Innovation, https://www.occ.treas.gov/topics/responsible-innovation/index-innovation.html and Alan Kaplinsky, "State Regulators File Second Lawsuit Opposing OCC Fintech Charter," Consumer Finance Monitor (Oct. 29, 2018), https://www.consumerfinancemonitor.com/2018/10/29/state-regulators-file-second-lawsuit-opposing-occ-fintech-charter/.
[36] *See* Federal Reserve, "Federal Reserve Board seeks public comment on potential actions to facilitate real-time interbank settlement of faster payments" (Oct. 3, 2018), https://www.federalreserve.gov/newsevents/pressreleases/other20181003a.htm.
[37] *See* Neil Haggerty, "FDIC to launch innovation office to help banks compete with fintechs," American Banker (Oct. 23, 2018), https://www.americanbanker.com/news/fdic-to-launch-innovation-office-to-help-banks-compete-with-fintechs.
[38] *See* NCUA, "NCUA Board's Partnership Transformed Regulatory Structure" (Mar. 2019), https://www.ncua.gov/newsroom/press-release/2019/ncua-boards-partnership-transformed-regulatory-structure.
[39] *See* NCUA, "Risk-Based Capital Rule to Become Effective in 2020; Asset Threshold Raised" (Oct. 2018), https://www.ncua.gov/newsroom/news/2018/risk-based-capital-rule-become-effective-2020-asset-threshold-raised.
[40] *See* Federal Reserve, "Regulators encourage institutions to work with borrowers affected by government shutdown" (Jan. 11, 2019), https://www.federalreserve.gov/newsevents/pressreleases/bcreg20190111a.htm.
[41] *See* FSC, "Waters Urges Regulators to Protect Americans Experiencing Financial Hardship Due to Trump Shutdown" (Jan. 11, 2019), https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=401715.
[42] *See* FSC, "Waters Supports Regulators' Action to Protect Shutdown Victims" (Oct. 9, 2013), https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=383034.