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"Regulatory Overreach: The Price Tag on American Prosperity"

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Chairman Barr, Ranking Member Foster and Honorable Members of the Subcommittee, thank you for the opportunity to testify today. My name is Sarah Flowers, and I am a Senior Vice President, Senior Associate General Counsel at the Bank Policy Institute, which is a research and advocacy group supported by banks with more than $100 billion in U.S. assets. Collectively, our banks employ nearly two million Americans, make half of the nation's small business loans and are an engine for economic growth. On behalf of BPI member companies, I appreciate the opportunity to provide input on regulatory overreach in the banking sector, particularly how ineffective bank supervision and improper regulatory tailoring are holding back the banking industry from being able to fully support its customers and the broader economy.

The U.S. has a uniquely versatile and varied banking sector, which fuels its diversified economy. U.S. economic vitality requires local relationship banking, sophisticated consumer services, strong commercial lending and vibrant capital markets. Banks of all sizes play a vital role in fueling U.S. economic growth. Not only is the U.S. banking industry competitive, it is also connected, with large banks providing services to smaller institutions including correspondent banking services, cash distribution, check processing, and international payment clearing.[1]

Excessive regulation is hindering the ability of the banking system to serve its customers efficiently. For mid-sized and regional banks, the problem starts with the federal banking agencies effectively ignoring a statutory mandate, enacted on a bipartisan basis by Congress in 2018, that enhanced prudential standards for banks be appropriately tailored. There is an urgent need to index the thresholds established by the agencies' tailoring regulations for all banks for economic growth and inflation. Economic growth and inflation do not increase systemic risk in the financial system; as the economy expands, various sectors of the economy grow proportionally.

[1] Our member institutions—generally comprising banks with at least $100 billion in U.S. assets—have the scale and sophistication needed to provide small banks and credit unions with vital financial services they need to thrive. Our members count hundreds of small banks and credits unions as customers, representing hundreds of millions in credit commitments. Our members further support smaller institutions by helping them (1) administer their cash flow and advising them on ways to manage excess cash; (2) providing institutional investment advice, including guidance on buying U.S. Treasuries and mortgage-backed securities; (3) navigating foreign exchange markets and international trade logistics; (4) providing loan syndication services (including large bank purchases of residential loans from smaller banks, enabling them to offer traditional mortgages), commercial cards, and foreign and domestic payment services to improve cash flow and reduce financial risk; (5) providing custodial services and investment portfolio management, helping small banks maintain financial health and long-term stability.

To be effective, tailoring of bank regulation must also be accompanied by complementary reforms to bank supervision. Regional banks routinely report that the use of "horizontal reviews" by the agencies results in their being held to the same standards as GSIBs through the examination process. While technically exempt from those standards as a matter of public regulations, nothing stops an examiner from nevertheless imposing them by issuing, or threatening to issue, a supervisory directive (a Matter Requiring Attention) in a non-public examination.

More broadly, banks are subject to a "shadow enforcement regime," imposing significant penalties on banks without due process protections, any checks or balances, or any accountability. This testimony will outline proposed reforms to restore the examination framework to its intended purpose and enhance due process for banks.

As Congress holds the federal banking agencies accountable for compliance with S. 2155, it should prioritize (1) codification of automatic indexing of all regulatory tailoring thresholds, so that we are not discussing this same issue for the same reasons a few years down the road, and (2) building safeguards into the examination process to restore checks and balances on supervisory practices. The appropriate adjustment of regulatory tailoring thresholds to reflect economic reality, and a supervisory framework focused on core financial risks and subject to due process, will enable durable reforms to the bank regulatory framework and prevent needless costs to economic growth.

Ensuring Regulatory Tailoring Required by S.2155 Is Dutifully Followed

Automatically Indexing Regulatory Tailoring Thresholds

When the agencies proposed their rules implementing the Economic Growth, Regulatory Relief, and Consumer Protection Act (S.2155) in 2018, BPI emphasized repeatedly the need to automatically adjust the dollar-based thresholds used in the risk-based indicators, as well as the $700 billion asset-size threshold for Category II, on an annual basis to account for economic growth so that those indicators would retain similar relationships to risk as the U.S. banking industry as the economy expanded.

In January 2019, the U.S. regulatory agencies finalized the tailoring rule to revise the criteria for applicability of a range of prudential regulatory requirements for large banks; over a year before the significant economic growth and inflationary trends began with the onset of the COVID-19 pandemic in 2020. This rule established a framework that imposes increasingly stringent standards on banks based on their size, complexity and risk profile. The most stringent capital and liquidity requirements apply to Category I firms, identified as U.S. GSIBs. The next most stringent standards apply to Category II firms, with more than $700 billion in total consolidated assets, or cross-jurisdictional activity of $75 billion or more. Category III firms are those with more than $250 billion in total consolidated assets or $75 billion or more in either STWF, Non-Bank Assets, or Off-Balance-Sheet Exposure. Category IV standards apply to those with total consolidated assets of at least $100 billion (a statutory threshold above which the Federal Reserve *may* apply enhanced prudential standards if determined to be appropriate based on risks to financial stability of the United States or to promote safety and soundness of bank holding companies) that do not meet the thresholds for a higher category. The Federal Reserve Board determined all these indicator thresholds via rulemaking except the $250-billion Category III threshold, which was statutorily defined by S.2155.

In the final rule, the agencies did not present empirical support for their threshold calibrations. However, responding to commenter concerns, the agencies did commit to periodic threshold reviews to account for economic growth and inflation. This commitment acknowledges the need for regulatory frameworks to evolve with the economy, to maintain effectiveness and avoid unintended consequences. Even if fixed thresholds are well developed and empirically supportable at the outset, when they are not indexed or adjusted to reflect general economic growth and inflation, they can become outdated. A bank's total exposures might grow larger simply because the whole economy is growing, not because the bank's portfolio is becoming riskier or more complex. But if the thresholds do not change, this normal growth could suddenly subject the bank to much stricter rules. This would contradict the original purpose of having different requirements for banks of various sizes. If a firm's asset size and risk-based indicators increase proportionately to increases in domestic banking assets, the firm's relative significance and risk profile within the U.S. banking system—as measured by the framework set forth in the tailoring proposals—generally remains static even though the absolute value of its assets or risk-based indicators is increasing. Those increases would reflect the expansion of the banking sector and the economy more generally, not changes in the firm's risk profile.

Economic growth and inflation do not increase systemic risk in the financial system. As the economy expands, various sectors of the economy grow proportionally. First, rising household incomes improve consumer creditworthiness, enabling larger loans supported by improved ability to repay. Second, economic expansion leads to the creation of new businesses and the expansion of existing firms to meet this growing demand. These firms, ranging from small firms to large corporations, use bank loans and financial services to support their operations. In addition, the rising costs of consumer goods and housing prices due to inflation further increase borrowing levels. Adjusting the tailoring category thresholds for banks based on economic growth and inflation would prevent banks from facing more stringent regulations solely due to natural economic expansion. Since the end of 2019, nominal GDP has grown by 34 percent. If the regulatory thresholds established by the agencies' tailoring regulations were adjusted proportionally to this economic growth and inflation proxy, the Category II size threshold would increase from **$700 billion to about $950 billion**, and the Federal Reserve Board calibrated risk thresholds across categories would increase from **$75 billion to about $100 billion**.[2]

These adjustments would ensure the regulatory framework remains aligned with the current economic reality, preserving the framework's effectiveness while preventing potential distortions in the banking sector. Periodic review and adjustment of these thresholds, as initially promised by the regulatory agencies, would foster a more dynamic and responsive regulatory environment. Adjustments for economic growth and inflation should be made annually and automatically to provide predictability for firms and to be more effective.

Once properly indexed for inflation and economic growth, the agencies must also more closely align prudential standards for U.S. banking organizations with the risk profiles of these firms. Regulations designed to capture risk associated with the complex activities of internationally active banks, for example, should not be indiscriminately applied to smaller domestic banks with less complex structures and business models. As new rules are developed, care must be taken to ensure that the most stringent requirements apply to firms with the most risk based on their relative complexity, and prescribe

[2] *See* Francisco Covas and Alexander Kim, Adjusting Regulatory Thresholds for Economic Growth (September 9, 2024), available at https://bpi.com/adjusting-regulatory-thresholds-for-economic-growth/.

materially less stringent requirements for firms whose activities and structure present less risk.

Reforming Supervision to Restore Checks and Balances

Limiting Examination to Assessment of Material Financial Risks and Banks' Overall Financial Condition

No regulatory tailoring for banking organizations can be effective unless it is consistently and faithfully reflected in the examination process. However, instead of enforcing the standards in the regulations under the tailored framework, additional compliance standards are routinely imposed on banks via the examination process.

When compliance with standards that are removed from the regulations are nonetheless imposed in the examination process through matters requiring attention, horizontal reviews,[3] or rating decisions, with those requirements instead cast as "best practices" or "supervisory expectations," they are no less binding than regulations on firms in practice. Because the examination process remains confidential, it is not subject to public scrutiny, and banks effectively have no right of appeal. It is thus crucial to identify what examination reforms should be implemented to ensure that no agency guidance or ad hoc examination mandate trumps the statutory and regulatory tailoring requirements. If the agencies wish to establish new, binding standards that all or a subset of banks must follow, the law and basic due process considerations require that they do so via notice-and-comment rulemaking and not via confidential supervisory directive. When the agencies proposed their rules implementing the Economic Growth, Regulatory Relief, and Consumer Protection Act (S.2155) in 2018, BPI encouraged the agencies to ensure that final tailoring regulations not be nullified through an examination process that would reimpose the same standard.

Codifying a Standard for Safety and Soundness

To promote safe and sound banking practices, the examination framework should be refocused on risks to a bank's financial condition. Most prominent among the banking agencies' enforcement tools is the authority to issue orders to a bank to cease and desist from "unsafe or unsound" practices or conditions or violations of law. A key reform should be the adoption of regulations that define an "unsafe or unsound" practice using a financial materiality standard. Currently, the federal banking agencies often disregard judicially recognized definitions of "unsafe or unsound" practices, which emphasize financial materiality. Courts have consistently interpreted these practices as those threatening a bank's viability. The overwhelming focus of the current examination regime is on a range of acts and practices that quite clearly do not meet the legal standard established by the courts—that is, acts and practice that pose risks that are remote and contingent and, if even those risks did materialize, would result in only minor (or no) financial loss. By codifying regulations that define an "unsafe or unsound" practice using the financial materiality standard established by the courts—both for purposes of determining when an agency may issue an MRA or bring an enforcement action based on such a practice—we can ensure that

[3] See Governor Bowman, *Brief Remarks on the Economy and Accountability in Supervision, Applications, and Regulation* (February 17, 2025) ("Supervisory practices like horizontal reviews can create examiner incentives to expect uniformity and "grade on a curve," but this approach perversely punishes variation among bank practices, stifling competition and innovation."); Governor Bowman, *Brief Remarks on the Economy, and Perspective on Mutual and Community Banks* (January 31, 2025) ("I think regulatory and supervisory "trickle-down" is real and it has significantly harmed community banks. I am referring to regulators conveying expectations to community banks (for example, during the examination process) that lack a foundation in applicable rules or guidance, or that were designed for larger institutions, or based on a horizontal review of unique banks.")

MRAs and enforcement actions are used only when examiners identify practices that genuinely threaten a bank's financial integrity, rather than merely those that are inconsistent with the individual preferences or views.

Raising the Bar for MRAs

No statute specifically authorizes the agencies to issue MRAs. Instead, it is the threat of becoming subject to an enforcement action for unsafe or unsound practices (along with the related threat of ratings downgrades) that generally gives teeth to MRAs and incentivizes their remediation, unmoored from any statutory constraints. Many of these MRAs are issued for routine governance and compliance matters such as information technology and infrastructure maintenance, vendor management, etc. At the same time, the consequences associated with MRAs have increased in severity.

In addition to codifying a safety and soundness standard, further checks and balances on the issuance of MRAs are warranted to ensure that agency staff are bound by such guardrails, which would empower an institution when formally or informally challenging MRAs or notices of charges. First, an MRA must be defined *in regulation* as conduct or a problem that meets the safety and soundness standard. An MRA, as now, would then require a remediation plan, and attention from senior management and, at times in appropriate cases, the bank's board. Matters not rising to the level of an MRA would not, and MRAs would thus be appropriately limited to remediating unsafe and unsound practices or significant violations of law. This limitation would prevent MRAs from being used to enforce non-binding guidance or supervisory preferences, in violation of the agencies' rule on guidance.[4]

Second, some discipline should be imposed to ensure that MRA determinations at the examiner level are made with due discipline, particularly in the context of a large bank where an "unsafe and unsound" practice is likely to be of significant concern to agency leadership. Accordingly, establishment of a new a requirement that any MRA proposed to be issued to a U.S. bank with at least $100 billion in assets must be reported to the head or heads of the agency imposing it would help to establish necessary discipline and ensure timely escalation.

To that end, and as noted above, if the agencies wish to establish new, binding standards that all or a subset of banks must follow, the law and basic due process considerations require that they do so via notice-and-comment rulemaking and not via confidential supervisory directive. In the experience of BPI member institutions, "industry MRAs" (*i.e.*, supervisory directives that are not specific to any one bank's practices but instead are issued to multiple firms in essentially identical terms) have become increasingly common. Because MRAs generally have severe consequences and are effectively unappealable, these MRAs operate as binding rules without notice and comment, effectively bypassing statutory requirements, raising significant due process concerns for banks. To address this issue, as suggested by former Federal Reserve Vice Chair for Supervision Randal Quarles in his January 2020 speech on bank supervision, an important improvement to the process by which bank supervision is conducted would be to establish a routine practice within each agency under which significant supervisory communications, including exam letters containing MRAs, would be subject to independent review within the agency before final issuance. The purpose of such review would be to make sure that such supervisory communications, including MRAs, "focus on violations of law and material safety and

[4] Interagency Statement Clarifying the Role of Supervisory Guidance, issued by the FDIC, Board of Governors of the Federal Reserve System, OCC, National Credit Union Administration (NCUA), and Consumer Financial Protection Bureau (CFPB) (September 11, 2018) available at https://www.govinfo.gov/content/pkg/FR-2021-04-08/pdf/2021-07146.pdf.

soundness issues and that these communications don't mistakenly give the impression that supervisory guidance is binding."[5] Indeed, given that the banking agencies each subsequently issued (in response to a BPI petition for rulemaking) a final rule on guidance (referenced above), one of the functions of such internal independent review would be to confirm that the rule on guidance is being followed as a substantive matter.

Examiners have also focused on—and, in some notable instances, weaponized[6]—"reputational risk," which may arise from business activities that are safe, sound and legal, but of which the banking agencies disapprove for other reasons.[7] The reforms outlined above would refocus examiners on material financial risk and away from non-financial and subjective notions of reputational risk. For national banks and state non-member banks, the OCC[8] and FDIC[9] respectively have recently announced their intention to remove references to reputational risk in supervisory materials, and the OCC has updated its supervisory handbooks accordingly. While these are encouraging developments that may empower banks to review their own risk frameworks to eliminate any elements imposed by the prior supervisory focus on reputational risk, considerable uncertainty remains. For example, the Federal Reserve has not yet announced a similar review, and it is not clear that agency examiners have received training on what it means for reputation risk to have been removed from the OCC handbooks (i.e., on the ability to factor reputation risk into safety and soundness determinations or CAMELS ratings).

Reforming the CAMELS Rating Framework

This lack of focus on material financial risk leads to unwarranted "CAMELS" ratings downgrades as the ultimate output of the examination process. Banks are assigned CAMELS ratings composed of six components rated from 1 to 5: Capital, Asset quality, Management, Earnings, Liquidity and Sensitivity to market risk including interest rate risk. Since the Uniform Financial Institutions Rating System ("UFIRS") was adopted in 1979 as a nonbinding "internal supervisory tool for evaluating the soundness of financial institutions"[10] with no self-enforcing mechanism, the CAMELS framework has developed into a supervisory tool with significant, severe, automatic and legally binding consequences for banks and their parent holding companies. As a result of a low CAMELS rating, a bank or holding company may: (i) lose "financial holding company" status, and thus eligibility to engage in certain financial activities, (ii) face higher deposit insurance assessment pricing, (iii) lose eligibility for primary credit at the discount window, and (iv) be prohibited from acquiring another institution or expanding across state lines.

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[5] Randal K. Quarles, *Spontaneity and Order: Transparency, Accountability, and Fairness in Bank Supervision* 14 (Jan. 17, 2020), available at: https://www.federalreserve.gov/newsevents/speech/files/quarles20200117a.pdf.

[6] House Committee on Oversight and Government Reform, Report: DOJ's Operation Choke Point Secretly Pressured Banks to Cut Ties with Legal Business (May 29, 2014), available at https://oversight.house.gov/report/report-dojs-operation-choke-point-secretly-pressured-banks-cut-ties-legal-business/. *See also* Tara Payne, The Regulatory Pressures Driving Account Closures (Feb. 6, 2025), available here https://bpi.com/the-regulatory-pressures-driving-account-closures/.

[7] Reputation risk has been explained as the risk that bank stakeholders will negatively change their perception of the bank, usually an ancillary consideration to credit risk operational risk or other primary risk. *See* Julie A. Hill, *Regulating Bank Reputation Risk*, 54 Ga. L. Rev. 523 (2019). Available at: *https://scholarship.law.ua.edu/fac_articles/152*.

[8] OCC Bulletin 2025-4, Removing References to Reputation Risk (March 20, 2025), available at https://www.occ.gov/news-issuances/bulletins/2025/bulletin-2025-4.html#:~:text=The%20OCC%20has%20never%20used%20reputation%20risk%20as,condition%20and%20resilience%20arising%20from%20negative%20public%20opinion. The OCC further noted that "[f]or handbooks and guidance issuances issued jointly with other regulators, the OCC will work with those regulators to expeditiously remove references to banks' reputation risk."

[9] On March 24, acting FDIC Chairman Travis Hill informed Congress that the agency is preparing to eliminate the use of "reputation risk" as a basis for supervisory criticism. In a letter to Rep. Dan Meuser (R-Pa.), Hill explained that the FDIC has completed a review of its regulations, guidance, and examination procedures to identify and remove references to reputational concerns in its supervisory framework. Available at FDIC Letter.

[10] 61 Fed. Reg, 67024-25 (Dec. 19, 1996).

At the same time, the broader bank regulatory environment has also changed dramatically since the UFIRS' adoption, including with respect to core prudential standards integral to certain CAMELS components, including significant substantive developments in capital regulation, liquidity regulation and stress testing. Yet, the CAMELS framework has not been substantially revised to reflect such dramatic changes in the regulatory environment, and the experiences of BPI's member institutions indicate that the application of the CAMELS rating system (and the corresponding Large Financial Institutions (LFI) rating system applicable to large bank holding companies) involve a significant degree of subjectivity and inconsistency on the part of examiners.

The agencies should make clear via rulemaking with notice and comment that the explicit purpose of these ratings are to gauge the *financial condition* of the bank. This purpose is consistent with the existing components under the UFIRS, as metrics regarding capital, asset quality, earnings, liquidity and sensitivity to market risk speak principally to an institution's financial condition. To promote the clarified purpose and ensure that institutions are not penalized and subject to severe consequences unless warranted, agencies utilizing the UFIRS should limit the assignment of unsatisfactory CAMELS ratings to those institutions the financial condition of which is poor or subject to a high likelihood of degradation, focusing on the likelihood of failure at a cost to creditors or insurers (i.e., the Deposit Insurance Fund). This clarification will help examiners apply the system more objectively and allow banks to evaluate their performance against clear standards.

While this framework in theory evaluates six factors, the management rating—the "M"—dominates for purposes of determining the composite rating. The Management rating is uniquely subjective; it is not based on any empirical standard but rather serves as a vehicle by which examiners can find fault with any aspect of a bank's compliance regime and can be determined by non-financial factors and the bank's willingness to accede to examiner mandates. For example, in current practice, the Management component is often used to measure an institution's compliance with federal consumer compliance, securities, tax, anti-money laundering, sanctions and other laws or state law, or the level of "reputational risk" in the bank's lines of business. Indeed, "CAMELS ratings can be predicted by examiner identities and past experiences, holding bank fundamentals constant."[11] The Management component is also often overweighted in calculating an institution's composite rating: recent scholarship on this issue has found that "[d]isagreement in ratings across examiners can be attributed to high average weight (50%) assigned to subjective assessment of banks' management quality, as well as heterogeneity in weights attached to more objective issues such as capital adequacy."[12]

These concerns are compounded by the severe, automatic consequences of an unsatisfactory Management component rating. A Management component rating below 2 could effectively disqualify an institution from financial holding company status and eligibility even if the bank has a 2 rating for every other component. Furthermore, "examiner discretion" has been shown to have "a large and persistent causal impact on future bank capitalization and supply of credit, leading to volatility and uncertainty in bank outcomes, and a conservative anticipatory response by banks."[13] Given the severe

[11] National Bureau of Economic Research Working Paper Series, Sumit Agarwal, Bernardo C. Morais, Amit Seru, Kelly Shue, Working Paper 32344: *Noisy Experts? Discretion in Regulation* (April 2024).
[12] National Bureau of Economic Research Working Paper Series, Sumit Agarwal, Bernardo C. Morais, Amit Seru, Kelly Shue, Working Paper 32344: *Noisy Experts? Discretion in Regulation* (April 2024).
[13] National Bureau of Economic Research Working Paper Series, Sumit Agarwal, Bernardo C. Morais, Amit Seru, Kelly Shue, Working Paper 32344: *Noisy Experts? Discretion in Regulation* (April 2024).

stakes associated with a low Management component rating and the risk that such a subjective component could become increasingly politicized in its application, the Management component should be eliminated from the CAMELS framework, or alternatively, significantly reformed to focus on objective factors, to ensure that the framework preserves a fair and objective approach to supervision that is tailored to factors material to an institution's financial condition, in keeping with the proper purpose of the UFIRS.
We recognize that banks may have material risks that are not covered by the C,A,E,L or S components and yet should be relevant to its examination rating. There are material operational risks that could affect the safety and soundness of a bank: for example, persistent and critical systems failures. Rather than attempting to cover material operational risks through a wholly subjective Management component that could include any other grievance an examiner might have, we believe that the better course would be to replace the Management rating with one specifically targeted at other material risks. As with all the other components, management of such risks would be a consideration, but at the end of the day, the component would consider actual risk in a more objective manner.

Removing or replacing the Management component would (i) help limit the assignment of unsatisfactory of CAMELS ratings to institutions the financial condition of which is poor or subject to high likelihood of degradation and (ii) better reflect that a bank should be considered "well managed" if, on balance, its management team, acting under the oversight of its board of directors, is appropriately managing the bank's capital, liquidity, asset quality, earnings and sensitivity to market risk.[14]

Supervisory Appeals

While these consequences of a ratings downgrade are significant and concrete, the assignment of these ratings is effectively left entirely to the subjective judgment of the examiner: as noted above, the relevant ratings frameworks themselves provide no meaningful standard at all to govern their use (or misuse). The agencies have adopted an internal appeals process, but that process almost invariably upholds the examination finding, which is not surprising given that the appeal is to senior personnel of the agency involved in the dispute.[15] It is quite easy to uphold any examination finding on internal appeal when there is no standard against which to judge it nor any impartial decision-making body to judge it.

Bank examination ratings also constitute confidential supervisory information and it has historically been asserted by the agencies that institutions may be subject to criminal penalties for unauthorized disclosure of such confidential information. Even if there were a chance of a favorable appeal, any such victory would likely come at significant cost, as retaliation in future examinations is a real concern. Unsurprisingly, the internal appeals process is rarely pursued by banks.[16]

[14] Indeed, while this same paper acknowledges that there are some predictive benefits to the "soft information" picked up by human discretion, it finds that placing moderate limits on examiner discretion can translate into more informative and predictive ratings. See National Bureau of Economic Research Working Paper Series, Sumit Agarwal, Bernardo C. Morais, Amit Seru, Kelly Shue, Working Paper 32344: *Noisy Experts? Discretion in Regulation* (April 2024).
[15] *See* Julie Andersen Hill, When Bank Examiners Get it Wrong: Financial Institution Appeals of Material Supervisory Determinations, Washington University Law Review (2015), available at (noting that an institution must first pursue an appeal with an agency official who supervised the examination, with the decisions reached at earlier stages of the appeals processes "a near complete black box.")

[16] *See, id.* (noting that "because this level of appeal is addressed to an agency official more closely associated with the examination staff, this may be the stage at which the appeal is most likely to induce examiner retaliation.")

The pitfalls faced by institutions seeking to appeal unsatisfactory CAMELS ratings, and the severe consequences attending such ratings, conflict with fundamental regulatory principles of fairness and due process. Accordingly, agencies utilizing the UFIRS should expressly permit examination findings and ratings to be immediately appealable to a legitimately neutral fact-finder and judge, including via judicial review.

Reining in Excessive Demands for Bank Information

When focusing on areas that have minimal relationship to material financial risk, examiners routinely request volumes of information from bank management and then require meetings to have the information explained to them. We know anecdotally that regional banks have dozens of full-time examiners and are subject to constant examination; for the largest banks, that number is in the hundreds, with a dozen or more examinations ongoing at all times, and examiners are resident at all large banks.

Of particular concern in light of recent events,[17] cybersecurity is a major threat to our economy and national security, yet cyber teams are being forced to spend the bulk of their time on compliance related activities rather than implementing strategic program improvements and preparing for emerging threats. Last year, a survey of bank Chief Information Security Officers — the people responsible for guarding against cyberattacks — revealed that they spent 30-50 percent of their time on compliance and examiner management; their teams spent 70 percent of their time on those functions. They reported on average over 100 requests for information leading up to an average examination, with anywhere from 75 to 100 supplemental requests during the exam. And 25 percent of examination requests duplicate requests from other agencies. They also anecdotally report major morale problems, including burnout and attrition among their staff driven by the need to respond to these requests within days or hours.

The OCC's recent cyber breach is yet another example of how the examination regime can introduce risk to firms and the financial system. Firms must provide extraordinary amounts of sensitive information to regulators who then fail to hold themselves to the same high standards for security and incident response as they expect of the firms they regulate. We have now seen several significant cyber incidents at regulators and government agencies and it is time for a holistic review that consolidates exams, reduces the amount of sensitive information being shared and retained, and focuses on protecting against national security threats.

In conclusion, these proposed reforms aim to restore the regulatory supervisory framework to their proper purpose of monitoring unsafe and unsound banking practices while providing robust due process protections for banks. By codifying (1) automatic indexing of all regulatory tailoring thresholds, and (2) a financial materiality standard for "unsafe or unsound" practices, as well as reforming the CAMELS and LFI rating systems and enhancing due process in examinations, we can ensure that bank regulation and supervision supports financial stability without imposing undue burdens on institutions. I urge the Committee to consider these reforms to promote a tailored, fair and objective regulatory and supervisory environment.

[17] OCC News Release 2025-30, OCC Notifies Congress of Incident Involving Email System (April 8, 2025), available at https://www.occ.gov/news-issuances/news-releases/2025/nr-occ-2025-30.html; OCC News Release 2025-32, OCC Releases Letter on Information Security Incident to Supervised Institutions (April 15, 2025), available at https://www.comptrollerofthecurrency.gov/news-issuances/news-releases/2025/nr-occ-2025-32.html.

Thank you for your attention, and I look forward to your questions.