FEDERAL DEPOSIT INSURANCE CORPORATION

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ADVISORY COMMITTEE ON COMMUNITY BANKING

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MEETING

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WEDNESDAY
JULY 20, 2015

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The Advisory Committee met in the Board Room of the FDIC Headquarters, 550 17th Street, N.W., Washington, D.C., at 9:05 a.m., Martin J. Gruenberg, Chairman, presiding.

PRESENT

MARTIN J. GRUENBERG, Chairman, FDIC
CYNTHIA L. BLANKENSHIP, Bank of the West
PEDRO A. BRYANT, Metro Bank
LEONEL CASTILLO, American Bank of Commerce
CHRISTOPHER W. EMMONS, Gorham Savings Bank
JANE HASKIN, First Bethany & Trust
JAMES LUNDY, Western Alliance Bank
MARY ANN SCULLY, Howard Bank
DAVID SELESKI, Stonegate Bank
GWEN M. THOMPSON, Clover Community Bank
JOHN M. TOLOMER, The Westchester Bank
DEREK B. WILLIAMS, Century Bank & Trust

PANELISTS PRESENT

BARBARA RYAN, Chief of Staff, FDIC
RUTH R. AMBERG, Assistant General Counsel, Legal Division, FDIC
FRANK M. BLANCHARD, Economic Analyst, Division of Insurance and Research, FDIC
LUKE H. BROWN, Associate Director, Division of Depositor and Consumer Protection, FDIC
DOREEN R. EBERLEY, Director, Division of Risk Management Supervision, FDIC
KATIE L. KRAMER, Economic Assistant, Division of Insurance and Research, FDIC
GREG A. LYONS, Student Trainee, Division of Depositor and Consumer Protection, FDIC
ROBERTA K. McINERNEY, Deputy General Counsel, Legal Division, FDIC
JONATHAN N. MILLER, Deputy Director, Division of Depositor and Consumer Protection
RAE-ANN MILLER, Associate Director, Division of Risk Management Supervision
MICHAEL S. McCOY, Student Trainee, Division of Risk Management Supervision, FDIC
MARK S. MOYLAN, Deputy Director, Division of Risk Management Supervision, FDIC
FAYE MURPHY, Section Chief, Division of Depositor and Consumer Protection, FDIC
MARK PEARCE, Director, Division of Depositor and Consumer Protection, FDIC
STEPHEN H. SIMPSON, Senior Financial Analyst, Division of Insurance and Research, FDIC
ROBERT F. STORCH, Chief Accountant, Division of Risk Management Supervision, FDIC
JAMES C. WATKINS, Senior Deputy Director, Division of Risk Management Supervision, FDIC

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1 P-R-O-C-E-E-D-I-N-G-S

2 (9:05 a.m.)

3 CHAIRMAN GRUENBERG: Welcome,
4 everybody. I'd like to welcome you all to this
5 meeting of our advisory committee.

6 Before I walk through the agenda, I
7 wanted to start by acknowledging and thanking a
8 number of our advisory committee members who,
9 sadly, are here for their last meeting because
10 their terms on the advisory committee are coming
11 to an end.

12 We established two-year terms, but we
13 really didn't want to let people go, if we could,
14 so we actually extended them and each of the people
15 who are now leaving actually had agreed to serve
16 on extensions of their two-year terms. As a
17 general rule, we try to rotate membership to give
18 as many bankers as possible an opportunity to serve
19 on the committee.

20 If I may, I'd like to just acknowledge
21 at the outset, the following committee members for
22 whom this will be their last meeting: Cynthia

1 Blankenship, Vice Chairman and CFO of Bank of the
2 West, Grapevine, Texas; Pedro Bryant, President
3 and CEO, Metro Bank of Louisville, Kentucky; Lionel
4 Castillo, President and CEO of American Bank of
5 Commerce, Provo, Utah; Jane Haskin, President and
6 CEO, First Bethany Bank Corp, Bethany, Oklahoma;
7 Mark Hesser, President, Pinnacle Bank, Lincoln --
8 excuse me -- Lincoln, Nebraska; James Lundy, Chief
9 Executive Officer, Western Alliance Bank, Phoenix,
10 Arizona; David Seleski, President, CEO, and
11 Director of Stonegate Bank in Fort Lauderdale,
12 Florida; and Derek Williams, President and CEO of
13 First People's Bank, Pine Mountain, Georgia.
14 Let me just express my personal
15 gratitude. It's been a pleasure getting to know
16 each of you. I think each of you has really made
17 terrific contributions to this committee and
18 genuinely enhanced the FDIC's appreciation of
19 the -- I guess of the challenges and opportunities
20 facing community banks.
21 We're grateful for the
22 opportunity -- that we've had the opportunity of

1 getting to know you, and we thank you very much for
2 your service to this agency.
3 PARTICIPANT: Thank you.
4 PARTICIPANT: It's been a great
5 experience.
6 CHAIRMAN GRUENBERG: Let me, if I may,
7 give you a brief overview of the agenda for today's
8 meeting, which is pretty full, and I think will be
9 of interest.
10 The first session today will provide an
11 update on the FDIC's Community Banking Initiative
12 and a report on some follow-up items from our
13 community banking conference, which took place in
14 April of this year.
15 Second, you may recall that at our
16 community banking conference in April, and also at
17 the most recent meeting of this committee, there
18 was some interest expressed in seeing if we could
19 get a better understanding of the perspectives of
20 millennials on banking. So we've tried to round
21 up a few --
22 (Laughter.)

1 CHAIRMAN GRUENBERG: -- and asking
2 about their banking needs, communication styles,
3 and expectations, as well as how they use
4 technology to conduct banking transactions. In
5 addition, there was some interest in discussing the
6 best ways for banks to recruit and retain employees
7 from the millennial generation.
8 As I indicated, we've asked a few of our
9 millennial employees to make a presentation to the
10 committee today. That will begin at 9:30. I
11 think you'll find them interesting. I actually
12 had the chance to meet with them and some of our
13 senior executives. They have interesting and, I
14 think, somewhat insightful things to say, so I'm
15 looking forward to it.
16 Following the millennial panel, we'll
17 take a brief break. After the break, we'll provide
18 the committee with an update of the FDIC's
19 regulatory review being conducted with the other
20 federal banking agencies, in accordance with the
21 EGRPRA -- the so-called EGRPRA regulatory review.
22 This process is nearing the end, and our staff will

1 inform the committee about some of the initiatives
2 that are underway as a result of the review process.
3 Then just before lunch, we'll cover
4 some consumer compliance issues, including an
5 interagency proposal being developed under the
6 FFIEC to revise the existing Consumer Compliance
7 Rating System to better reflect the current
8 consumer compliance supervisory approaches.
9 After lunch, we're going to discuss
10 some issues relating to financial technology.
11 Senior staff will brief the committee on our
12 efforts to better understand the system monitor
13 intake activities, risks, and trends. We will
14 greatly appreciate your input to help us formulate
15 an appropriate strategy -- seems to be the current
16 phrase, to respond to the opportunities and
17 challenges presented by Fintech going forward.
18 Our last issue today, we'll cover some
19 recent supervisory developments, including recent
20 updates to our IT examination procedures to provide
21 a more efficient, risk-focused IT examination
22 approach. In addition, senior staff from our

1 Division of Risk Management Supervision will
2 provide the committee with an update in some recent
3 developments with the Financial Accounting
4 Standards Board, or FASB, primarily related to
5 FASB's model for current expected credit loss. It's
6 this thing called CECL.
7 Finally, senior staff will provide the
8 committee with some information about the
9 interagency proposal that was put out for comment
10 last month on incentivized compensation
11 arrangements and some recently issued Q&As on
12 brokered deposits.
13 I think we've tried to touch every hot
14 button that we could come up with. I think it'll
15 be an interesting day, and I look forward to the
16 presentations. I'll turn it over to Barbara Ryan.
17 MS. RYAN: Thank you, Chairman
18 Gruenberg, and good morning, everyone. As the
19 Chairman indicated, we thought we would start off
20 this morning by providing the committee with a
21 quick update on our Community Banking Initiative,
22 as well as some follow-up items from our community

1 banking conference in April.
2 To provide us with those updates, we're
3 going to now hear from Doreen Eberley, Director of
4 the Division of Risk Management Supervision, and
5 Mark Pearce, Director of our Division of Depositor
6 and Consumer Protection.
7 Doreen's going to go first, so I'll turn
8 the program over to her.
9 MS. EBERLEY: Okay, thanks, Barbara.
10 Good morning, everybody. I'm happy to give you an
11 update this morning on the Community Banking
12 Initiative and then some follow up activities that
13 are coming out of the community banking conference
14 last April and our discussion that followed that
15 the next day.
16 Starting with our ongoing initiatives,
17 Technical Assistance Videos, we issued the video
18 on corporate governance just this week. It went
19 out on Monday. We're working on taking a look at
20 the Directors' College portfolio of videos and
21 updating those and maybe adding some additional
22 videos to the Directors' College portfolio.

1 Working with each of the regions to do that, as
2 they're planning their next round of in-person
3 sessions, and making sure that we've got a good
4 capturing of the messages that are going out in each
5 of the regions in the Directors' Colleges.
6 We did update the interest rate risk
7 Directors' College video recently, but that's
8 really the only one that's been updated since the
9 original group was released a couple of years ago.
10 We do want to get those reviewed and updated and
11 added to as appropriate.
12 Following up on the conference, you all
13 received the Community Bank Resource Kit during the
14 conference and liked it very much. We finished the
15 printing of those. We had done one initial
16 printing for the conference to be able to
17 distribute copies to everybody there.
18 The copying is done. We have copies
19 for every financial institution we supervise.
20 Over the course of the next several weeks, copies
21 will be mailed to all the institutions we supervise
22 with a cover letter from me and Mark highlighting

1 the materials inside.
2 A couple of the items that we
3 highlighted were the Supervisory Insights Special
4 Edition, a Community Bank Director's Guide to
5 Corporate Governance. It's a little small version
6 of our SIJ that fits in the kit that really walks
7 through what are the expectations for a board of
8 directors in the world of corporate governance, in
9 terms of determining the institution's risk
10 profile, having that conversation with the
11 examination team, addressing strategic planning
12 based on the business and the community that the
13 institution is serving, and the risk profile and
14 risk appetite of the board of directors that's been
15 stated.
16 What's the difference between rules and
17 regulations, guidance, and best practices? How do
18 those affect how the institution operates and
19 interacts with the examiners? What to expect
20 during the examination process in terms of
21 corporate governance, and just some ongoing
22 considerations.

1 It refers back to the Pocket Guide for
2 Directors, which we did update. It's got a new
3 cover and a new look and new colors, but the content
4 is the same. One thing that we really felt
5 strongly about was that this was timeless, and that
6 the duties and responsibilities of directors
7 really have not changed since we first issued this
8 in the '80s. It's got a new look, but not new
9 content.
10 A couple of the other items that we
11 highlighted in our letter that will go out are the
12 technical assistance pamphlet for managing
13 consumer compliance responsibilities, all sorts of
14 pamphlets covering our Technical Assistance Video
15 Program, the Directors' Resource Center, and the
16 materials that are available on the Directors'
17 Resource Center to help institutions, lots of
18 material on cybersecurity, including some
19 pamphlets that you can reprint and send to your
20 customers. There's a pamphlet designed for
21 consumer customers, and one for business
22 customers, to help them increase their

1 cybersecurity savvy and help protect themselves
2 and your institution.
3 Of course, we've updated Cyber
4 Challenge. The updated version has the flash
5 cards for all seven video vignettes, plus a
6 diskette with the video vignettes on it for those
7 institutions that don't allow access to YouTube in
8 the institution. They can also be downloaded off
9 of FDICconnect.
10 Then we've got a couple of other
11 reprints of Supervisory Insights that we think are
12 important and timely ones, even though they've been
13 out for a while. One is Managing Interest Rate
14 Risk, and the other is The Risk Management
15 Examination in Your Community Bank. So what to
16 expect through the examination process, how
17 communication should work, and how we invite board
18 and management to participate with the examiners
19 through the examination and conversations.
20 Those will be -- you'll start seeing
21 them over the course of the next few weeks. It will
22 probably take three or four weeks to get all the

1 mailings out. We've got our Division of
2 Administration handling that for us. You'll start
3 to see those arriving in the mail soon.
4 We talked a lot at the community banking
5 conference about de novos and the steps that we want
6 to take to be helpful and supportive of the
7 formation of de novo institutions. One of the
8 items we talked about was hosting some roundtable
9 meetings with organizing groups that might be
10 interested, the consultants that work with those
11 groups in that area, and hosting a few of those
12 around the country.
13 We're starting this year with three
14 regions: San Francisco, New York, and Atlanta.
15 San Francisco will kick us off on September 28.
16 We're deep in the planning for that session. I did
17 want to recognize and thank John Tolomer for his
18 idea that as part of these sessions, we have a
19 panel.
20 Rather than just having regulators
21 talking about what's the process and what are the
22 best ways to approach it, let's have a panel of

1 successful de novo bankers talk about their
2 experiences; what worked, what are the lessons they
3 learned along the way that they would like to share
4 with others? John has graciously agreed to join
5 us at the first session in San Francisco, as well
6 as the session in New York.
7 We're very much looking forward to
8 that, think it's going to be a really good day. The
9 agenda's shaping up nicely, and we'll be looking
10 forward to reporting out on that at the next
11 meeting. We'll probably have two under our belt
12 by that time. We should have both San Francisco
13 and New York completed by the next meeting.
14 We're working on our handbook for
15 deposit insurance, which will be available later
16 this year. In the meantime, we may be having a
17 shorter article in our next version of Supervisory
18 Insights talking about the process and really
19 outlining it. So kind of an outline of what to
20 expect in the broader handbook.
21 Then I'd like to mention, also, as a
22 subset of community banks, mutual institutions.

1 We do maintain a special page on our webpage,
2 fdic.gov, for mutual institutions. Every other
3 year, we host a mutual bank conference jointly with
4 the OCC and the Federal Reserve. The next
5 conference is coming up week after next, August
6 4th, and we look forward to having that event.
7 The remaining items that really came
8 out of our work streams coming out of the community
9 bank conference related to looking at schools that
10 are offering banking degrees and finding a way to
11 facilitate conversation between those schools and
12 bankers and state banking associations about how
13 they could work together.
14 Just bringing together the parties, I
15 think, will be our role. We've identified a number
16 of institutions that actually do offer, at both an
17 undergraduate and a graduate level -- some not
18 both, but we've got lists of institutions that do
19 both that we've been able to identify -- that we
20 think we can bring together in a central location
21 to have a conversation about what they're doing,
22 how they interest folks in banking careers, and how

1 you may be able to partner with them to help find
2 employees and look for the next generation of bank
3 officers and employees.
4 We're continuing to do work on
5 technology service providers. We certainly heard
6 the discussion loud and clear. That's something
7 we've been working on the interagency basis. I
8 don't have anything ready for prime time just yet,
9 but do want to emphasize to you that we are actively
10 working on ways that we can ensure that
11 institutions are able to partner with their
12 technology service providers in an equal way.
13 Our guidance applies already to both
14 technology service providers and financial
15 institutions that they service, or maybe vice
16 versa, the institutions that they service and the
17 technology service providers themselves that are
18 providing the services. We are continuing to
19 explore ways that we can help with that
20 relationship and make sure that institutions are
21 well positioned to do the due diligence that they
22 need to do and to manage those relationships, and

1 particularly hearing the concerns that we heard on
2 cybersecurity and liabilities and the issues that
3 were raised during the conference. That work is
4 ongoing.
5 I would point out -- the Chairman
6 already mentioned it -- but the new IT examination
7 program, InTREx, our Information Technology Risk
8 Examination Program is what InTREx stands for. We
9 love our acronyms.
10 At any rate, that was one way that we
11 tried to make -- as we worked through this process,
12 how could we make the examination work program more
13 transparent to institutions, and how could you
14 better understand any concerns that we have
15 relative to the rating system and relative to the
16 components of that rating system.
17 The work program has been completely
18 redesigned. It aligns with the rating system.
19 We're going to start disclosing ratings -- so not
20 to steal a little bit of Mark's thunder, but
21 disclosing the component ratings for the rating
22 system, as opposed to just the composite, to help

1 with the awareness. It's very much like when we
2 first started disclosing component ratings in the
3 panels. Some of you will remember that. I do.
4 Before that, you had to kind of guess
5 where we were coming from. We want to be very
6 clear, very transparent. We think that's helpful
7 in any relationship, but certainly in
8 understanding the risks that we're trying to talk
9 about. That should be beneficial.
10 Then finally, we're conducting some
11 research -- not too terribly sure that we'll have
12 anything coming out of this, but it was a very
13 interesting conversation at the conference about
14 the pressure that institutions felt to provide
15 liquidity to shareholders and to really be able to
16 provide some liquidity in their share base and the
17 different ways that we heard institutions going
18 about that.
19 We've started some research in that
20 regard, taking a look at that. At the very least,
21 I think we'll be able to share our research. There
22 may not be any answers or aha moments coming out

1 of it, but we can at least share what we're seeing.
2 Thought that was a very interesting thread to kind
3 of keep pulling on and taking a look at that came
4 out of the conference. So that's the work from the
5 RMS side of the house.
6 MR. PEARCE: Great, so thanks. I'll
7 pick up with just a couple of things from the
8 consumer protection/DCP side. One of the things
9 you'll learn about putting up a series of Technical
10 Assistance Videos is then you have to really pay
11 attention when they need to be updated.
12 Recently, we updated our Technical
13 Assistance Video related to flood insurance. Later
14 this summer, we're going to release an updated
15 version of one of our mortgage videos, the ones
16 related to the ability to repay rule and qualified
17 mortgage. Folks may remember that in the last
18 year, there's been a legislative change that
19 affects the definition of what a rural institution
20 may be, and so we're making sure we update that and
21 any other changes that have been made since CFPB
22 issued that rule a couple years ago. Those videos

1 will be refreshed and up to date.
2 Speaking of the mortgage market,
3 another way that we think we can help support
4 community banks in the mortgage area is by
5 providing some information about how community
6 banks can access affordable mortgage programs.
7 There's programs at the state level, through state
8 housing finance agencies. Federal home loan banks
9 have a series of programs that community banks can
10 access, and there are also various federal
11 programs, like USDA or FHA, et cetera.
12 We've been working for some time now,
13 first starting out by talking with community banks
14 about how they've utilized those programs to really
15 get a sense of how these are really playing out in
16 the field and how banks are utilizing these
17 programs to serve their customers, and then trying
18 to do the research to put together a resource guide
19 for community banks on affordable mortgage
20 programs.
21 Hopefully, later this summer, we'll
22 publish part one of that that will cover a whole

1 series of federal programs and have not only what
2 are the opportunities for those programs, some
3 potential risks or concerns for those programs, but
4 also some stories from community bankers about how
5 they've actually utilized these programs.
6 We really do think that will be helpful
7 because a lot of community bankers, in particular,
8 may just not understand the different programs out
9 there. They all have their unique differences, so
10 this provides sort of a basic, hopefully
11 easy-to-understand guide to be a gateway into some
12 of the program opportunities to serve customers.
13 Then the last thing I wanted to mention
14 is over the last couple years on the supervisory
15 side, we have been looking at our examination
16 process to try to improve the risk focusing. What
17 that really has meant is looking, in particular,
18 at the pre-exam planning process.
19 Over the last couple years, in
20 particular, we have spent more time to make sure
21 that by the time our examiners get on site at the
22 bank, we have a good understanding of the bank, its

1 risk profile, complexity, its business model.
2 That has made the on-site portion much more
3 efficient. We've got a lot of positive feedback
4 so far on that program. We decided this year to
5 take another look at how well that's been working
6 and ways that we can refine that. We've got a team
7 of people internally that are taking a look at it.
8 One of the areas that has come up from
9 some community banks is the number of questions
10 that we ask in the pre-exam planning process. That
11 has been an issue of concern for some banks, just
12 the amount of information and questions on the
13 front end. It's really helpful when we get all
14 that information on the front end because it makes
15 the on-site exam go smoothly -- or more smoothly,
16 but we want to take a look at the numbers of
17 questions and are we asking for the information we
18 really need to be effective in the examination
19 program? Those are two or three things on the DCP
20 side.
21 MS. RYAN: Thanks, Mark and Doreen.
22 Any comments or questions?

1 MEMBER TOLOMER: Yes, I had a chance to
2 review or watch the video this morning on
3 governance. I thought it was excellent. I think
4 it would be helpful for de novos, but also, I think
5 it would be a great reminder for current boards to
6 look at goals and responsibilities. It was very
7 well done.
8 MS. EBERLEY: Thank you.
9 MEMBER LUNDY: Just for a technical
10 comment on the information updated on the flood
11 insurance, and it might intersect with your key
12 vendor relationships.
13 We've had some issues with flood
14 insurance violations, unintentionally most of them
15 are, related to contents not being covered.
16 Sometimes the contents -- we can all think of a
17 situation where the contents of a building that you
18 take a deed of trust on are perhaps critical to the
19 underwriting. Many times they aren't. Almost
20 all deeds of trust have boilerplate contents
21 included. LaserPro, which I know does the long
22 docs for many, many community banks, it would be

1 helpful if they had a module that you could click:
2 we want contents, or we don't want contents.
3 Typically, contents are always
4 included in the deed of trust. Often, they're
5 totally unrelated to the safety and soundness of
6 the loan. Often, flood insurance is taken on the
7 building, but it's missed being taken on the
8 contents. That's creating a situation of
9 unintentional technical violations of the flood
10 insurance policy. Sometimes you do need to cover
11 the contents, and you ought to get flood insurance
12 on it. But I think there's a little bit of a
13 mismatch between practical reality with the
14 complications of the flood maps, which change, and
15 the documentation that many banks use.
16 For larger transactions, where outside
17 counsel prepare docs, very few transactional
18 attorneys are aware of this kind of esoterica. The
19 contents are always included in their documents.
20 That, again, can give rise unintentionally. I
21 don't know if you're aware of that, if it's come
22 up through the process.

1 MR. PEARCE: Certainly, contents
2 coverage, I know, has been a pain point for a lot
3 of bankers. The deeds of trust generally do
4 include that. I think the suggestion you made is
5 the first I've heard of a specific suggestion that
6 might be helpful for bankers to navigate some of
7 the challenges there. As Doreen mentioned in her
8 comments, we are spending some time looking at
9 technology service providers.
10 On the consumer compliance side, one of
11 the recent rules that have come out related to the
12 mortgage disclosure updates -- I know that a number
13 of community banks have challenges with their
14 vendors and being able to provide software to
15 enable them to be effectively compliant with the
16 law. That's an issue that we're working together
17 on to try to make sure that technology service
18 providers that are providing software or
19 disclosure forms are doing so in a way that helps
20 support community bank compliance, not just the
21 technical compliance. Your point is really
22 enabling a solution that would help them be able

1 to do that more effectively.
2 MEMBER BLANKENSHIP: I'd just like to
3 say following our last meeting, I called and
4 requested several of the Community Bank Resource
5 Kits, which we received, and passed that out to our
6 board of directors and told them that we would cover
7 it probably in 60 days.
8 I had one of our directors call back and
9 say this is great. This is really, really good
10 because it was a summary, and they can understand
11 it. So I applaud your idea. Honestly, I plan to
12 pass more of the kits out to our branch presidents
13 because it is just a good refresher. It puts in
14 front of mind that risk factor. Every time they
15 make a decision throughout the day, then it kind
16 of brings it full circle, so thank you for that.
17 MEMBER BRYANT: I'd also like to
18 comment. I'm on the Consumer Advisory Board. The
19 topic of this came up at the last advisory board
20 session as well.
21 MEMBER TOLOMER: Can I comment on the
22 questionnaire? While it looks

1 intimidating -- because we're preparing for an
2 audit exam in September -- we provided the
3 information to the FDIC. We requested a phone
4 conversation just to make sure there was clarity
5 on all the points.
6 It's comprehensive, but it's not
7 anything that I shouldn't know. I think I wouldn't
8 change very much of it. As long as you have the
9 ability to talk to somebody to make sure there's
10 clarity, I think it should be helpful.
11 MR. PEARCE: Thanks for the feedback on
12 that. I do think the principle of trying to do the
13 off-site work so that examiners are prepared when
14 they get on site, I think, is something that we are
15 committed to continuing.
16 Looking at things like if you've been
17 through one exam, is there a way on the second exam,
18 so you don't have to ask them the same set of
19 questions? There may be things that haven't
20 changed and looking for opportunities to refine
21 that process.
22 MS. RYAN: Thanks very much Mark and

1 Doreen. We're going to move now into our next
2 panel discussion, which is on millennials'
3 perspectives on banking.
4 As Chairman Gruenberg mentioned, we've
5 invited a group of millennials to spend some time
6 with us, to talk about their attitudes toward
7 banking, how they generally access and use
8 financial services, and other interesting
9 information.
10 To address these, our group is led by
11 Stephen Simpson. Stephen, to my right, is from our
12 New York region, where he's a senior financial
13 analyst in our Division of Insurance and Research.
14 He's joined on the panel by Frank Blanchard, who's
15 an economic assistant in our Division of Insurance
16 and Research; Greg Lyons, a student trainee in our
17 Division of Depositor and Consumer Protection; and
18 Michael McCoy, a student trainee in our Division
19 of Risk Management Supervision. I'm going to just
20 turn the program over to Stephen now.
21 MR. SIMPSON: Thank you very much,
22 Barbara. I don't know if everybody has a chance

1 to see it, but in your packets, there should be a
2 handout that we've provided. The title slide
3 says: Millennials Shaping the Future of Community
4 Banks. We'll kind of follow along through that,
5 so if you'd like to, you can start with that.
6 First, I want to say thank you so much
7 for having us here today. As Barbara noted, my
8 name's Stephen Simpson. I'm a senior financial
9 analyst in the New York Regional Office for the
10 Division of Insurance and Research here at the
11 FDIC. That means that under normal circumstances,
12 I'm digging into the data and looking for financial
13 trends and potential risks to the financial
14 industry.
15 But today, I have a special task to come
16 here, and I'm very excited to have some of my
17 colleagues up here today, some of the bright young
18 people from the FDIC, to talk about their attitudes
19 toward banking and their thoughts and perceptions
20 on the banking industry.
21 The idea behind this discussion came
22 about from the April 2016 community banking

1 conference. There was quite a bit of interest at
2 least discussed about how millennials think about
3 banking and what kind of differences there are from
4 prior generations. On the second page of the
5 handout that you have, we put together the four
6 major themes that came from that community banking
7 conference.
8 The first of which was the shift in
9 focus on the generations and the differing banking
10 needs, primarily the discussion was between baby
11 boomers to millennials. The second theme was the
12 differing styles of communication and related
13 expectations of this particular age group. Third
14 was the dynamic landscape of technology and its
15 role in banking. Finally, we discussed
16 millennials in the workforce, and there's a real
17 focus on attracting and retaining that talent.
18 I've prepared a set of questions to lead
19 us through this discussion, but I've also made sure
20 to leave time at various points in the discussion
21 for the advisory council to provide any input or
22 questions or just general comments that you'd like

1 to add. I think I'll start out by introducing our
2 panelists. Then, what we'll do is we'll give a
3 little bit of background into the millennial
4 generation, who that refers to, and what makes this
5 group so different from our prior generations.
6 If we could start, maybe we'll just go
7 down the line. Frank, do you want to give us a
8 little bit of background about you?
9 MR. BLANCHARD: Sure, thank you,
10 Stephen. It's a pleasure to be here. My name is
11 Frank Blanchard. I'm an economic analyst in the
12 Division of Insurance and Research. I've been
13 with the FDIC for approximately four years now.
14 I'm originally from Virginia Beach, Virginia, and
15 I went to school at James Madison University.
16 MS. KRAMER: Hi, my name is Katie
17 Kramer. I'm originally from Naples, Florida, and
18 then went to Marshall University and got my
19 undergraduate degree in economics, and then an MBA.
20 I am also in DIR working as an economic assistant.
21 I've been here for about one year.
22 MR. LYONS: My name's Greg Lyons. I'm

1 a graduate research assistant within the Division
2 of Consumer Protection. I've been here only about
3 six months now. I got my undergraduate degree in
4 policy analysis from Cornell University and am
5 earning my master's in public policy from
6 Georgetown. Student loans will obviously be a big
7 part of the discussion for me. Happy to be here,
8 thank you so much.
9 MR. MCCOY: Good morning. I'm Mike
10 McCoy. I'm an intern with the Division of Risk
11 Management Supervision. I'm a 28-year-old
12 retired Army veteran, who's originally from
13 Pittsburgh and is currently attending Robert
14 Morris University for accounting.
15 MR. SIMPSON: Thank you. Before we
16 shine the spotlight on my colleagues' opinions up
17 here, I thought it would really be helpful to take
18 a step back and look at the larger population of
19 millennials and just sort of frame our thinking.
20 If you would, you could take a look at the pie chart
21 on the next page, on page 3, there, of the handout
22 in front of you. We'll start by identifying who

1 the tagline millennials really refers to and what
2 makes them such an omnipresent part of our
3 conversation.
4 Putting an exact born on and expiration
5 date on generations is a bit of a nebulous task
6 because usually, when we talk about generations,
7 we're talking about aggregated social trends and
8 behavioral patterns. But as a fairly loose
9 definition, when you hear the term millennial, it
10 generally refers to the population born between
11 1980 and 2000.
12 I'm going to take a little bit more of
13 a refined look by including only the group of young
14 adults that had reached the age of 18 to 34 as of
15 the end of 2015. That's a very specific subset.
16 It makes the oldest millennials born in 1982, and
17 it makes the youngest millennials born in 1998.
18 I'm going to do that for two reasons.
19 First, it gives credence to me as an
20 impartial moderator because I am well outside,
21 unfortunately, of that demographic. Second, and
22 probably more importantly, is that there's several

1 mainstream and comprehensive studies that have
2 been provided, one of which I'll refer to a lot is
3 from the Pew Research Institute, and another one's
4 from Nielsen. It gives us a bit of a consensus to
5 rely on, and I can steal some of those statistics.
6 Using the definition born in 1982 to
7 1998, the most recent full estimate available from
8 the U.S. Census Bureau identifies the millennial
9 population at a little over 74 million as of July
10 2015. That's a full year ago, but that's the most
11 recent data. If you look at the pie chart, you can
12 see that's about 23 percent of the U.S. population,
13 which puts them right in the same category as baby
14 boomers, in terms of the overall size.
15 Now, there's more recent estimates that
16 will come out, obviously, in July 2016. Some of
17 those estimates have already trickled out.
18 They're as high as about 84 million, which puts the
19 millennial population at about 25 percent of our
20 population, which makes the largest cohort of
21 generations in the U.S.
22 Now, not only is the sheer size

1 important, but also, this demographic is rapidly
2 approaching its sort of critical stage in their
3 lives. The youngest millennials are approaching
4 their financial independence, and the older
5 millennials are rapidly approaching their prime
6 earning years. As a result of that, they quite
7 literally become everybody's target market.
8 They're getting a lot of discussion out there.
9 In the next few slides, I'm going to
10 refer to some of the other generations. Just for
11 clarity, Generation Z generally refers to the
12 youngest generation alive right now. That's from
13 1999 through present. Millennials, of course,
14 1982 to 1998. Then we'll talk about Gen X precedes
15 them, so they were born 1966 to 1981, baby boomers,
16 post-World War II to mid-1960s, and then silent
17 generation. The greatest generation's still out
18 there, but they represent a very small piece of the
19 demographics, so we won't really refer to them
20 much.
21 If you follow me over to the next page
22 in your handout, page 4, I'd like to talk about what

1 makes millennials so different from the prior
2 generations. There's no shortage, unfortunately,
3 of statistics out there on millennials. Believe
4 me, I had to sift through quite a few.
5 But one that I found particularly
6 profound was that U.S. Census data shows that in
7 1975, three out of every four 30 year olds held a
8 job, owned a home, and had started a family. By
9 2015, the share of 30 year olds that had tackled
10 those same life events fell to just one in three.
11 It's been a huge change. These life cycle changes
12 can be further broken down by looking at several
13 milestones.
14 First, it's taking millennials a little
15 bit longer to figure out a defined career path.
16 The 2015 Pew Research study that I was referring
17 to earlier noted that 30 percent of males age 18
18 to 33 are either unemployed or not in the labor
19 force. That's compared to about 20 percent for the
20 prior generation, for Generation X, and 37 percent
21 of females are either unemployed or not in the labor
22 force, and that's compared to 31 percent. So quite

1 a bit higher unemployed or not in the labor force
2 rates.
3 Second, marriage is becoming more of a
4 capstone type of event. It used to be that you
5 would graduate college, partner up, and then sort
6 of tackle life's challenges together. But today,
7 that's becoming more of obtain financial
8 independence, and then go down the marriage route.
9 According to that Pew Research study, 28 percent
10 of millennials are married, and that's compared to
11 38 percent of Gen X, 49 percent baby boomers, and
12 64 percent of silent at the same age. That's sort
13 of a prolonged trend that's really getting a lot
14 of play time.
15 Millennials also have a tendency to
16 choose to live in city centers. Similar to the
17 trend before, it's a long-term trend, but 86
18 percent of millennials live in a metropolitan area.
19 That's compared to 83 percent of Generation X, just
20 68 percent of baby boomers, and 64 percent of
21 silents at that same age.
22 Millennials also have a tendency to be

1 more educated, or at least attain higher levels of
2 education. Fifty-five percent of males age 18 to
3 33, and 64 percent of females, have at least some
4 college education. That's the highest among all
5 those generational cohorts.
6 They're also savers. They grew up with
7 the great recession. It impacted their formative
8 years, which affects how they think about money and
9 personal finance. On average, millennials start
10 saving at age 22. That's five years before Gen X
11 and 13 years before baby boomers. They also
12 proportionately save more. Millennials are
13 saving around 8 percent. The long-term average
14 for their predecessors was around 7 percent of
15 their income.
16 Millennials have a tendency to be
17 socially connected. This is the one that we always
18 hear about in the mainstream media, but it's true.
19 They grew up with social networks, and they care
20 about social issues. I read that 84 percent had
21 made a charitable donation in 2014, and 70 percent
22 had volunteered at least one hour of their time,

1 which I think is very high.
2 As a corollary, they grew up in a golden
3 age of information technology. That's kind of
4 what we hear about so much is that they're very
5 comfortable with trying out new technologies.
6 They're early adopters of those technologies, and
7 they're very comfortable with making decisions
8 based solely off of online or web experiences.
9 What do these demographic and social
10 differences really imply? There's a few key
11 trends that are noteworthy. First, housing
12 formation had been affected due to the delay in
13 marriage, which affects the timing of your initial
14 home purchase. It also affects the timing of
15 subsequent home purchases because you don't
16 outgrow your first home and have the need to get
17 a second home.
18 That second theme, in terms of
19 urbanization, housing affordability and
20 preference have pushed millennials into city
21 centers. That's not only affecting the purchase
22 of houses, as well, but it's also affecting auto

1 lending. If you live in the center of the city,
2 you're less likely to need to buy a car, and even
3 more or less likely to buy multiple cars.
4 The more college education that we
5 talked about, that's led to student loans. Greg
6 already mentioned that a little bit, but two thirds
7 of bachelor degree recipients have outstanding
8 student loans with an average debt of about
9 $27,000. It's a big number. Two decades ago,
10 only half of recent graduates had college debt, and
11 the average was down around $15,000. So that's
12 quite a bit of growth, not only in the amount, but
13 also the percentage of. That also affects
14 affordability because that's part of their
15 household debt. Being able to afford a home is
16 impacted by that, as well.
17 Lastly, they're more apt to research,
18 identify, establish, and maintain relationships
19 with businesses based solely off of their web or
20 online experiences. That impacts the way that we
21 do business with millennials.
22 All these trends add up to one thing

1 that we're getting at here. That is they have a
2 very different banking relationship and a very
3 different outlook on banking.
4 Now that we've established a little bit
5 of background about millennials, at least from a
6 very high level, now we can focus in and shine the
7 spotlight on our panelists here. I want to point
8 out, though, that the views expressed today are
9 their opinions. They don't necessarily represent
10 the FDIC's opinions.
11 With that, we'll talk a little bit about
12 how millennials use financial services. I think
13 we'd like to hear a little bit about how you came
14 about to choose your bank, and maybe elaborate on
15 the biggest factors that played a role in your
16 choice of banks. Maybe we'll start the opposite.
17 You want to start, Michael?
18 MR. MCCOY: Sure. I grew up in a very
19 small town, about 3,200 people. Despite living in
20 more than a dozen locations worldwide in the last
21 decade, I've maintained my relationship with the
22 local community bank, predominantly because the

1 branch manager was a baseball coach of mine for
2 about a decade. The loan officer at that branch
3 was in high school with me. Essentially, everyone
4 in that building knows my name. I know their
5 names. The reason that I've stayed with them,
6 despite not having great access over the years, is
7 because I know and trust the people at the
8 institution.
9 MR. LYONS: Similarly, I grew up in a
10 small town. When I was 10, I opened up an account
11 with our local community bank. I really did enjoy
12 the service there, but when I went off to college,
13 there was no way I was going to be able to continue
14 banking with them. They didn't have online or
15 mobile services, and there were no locations near
16 my college.
17 I switched to another institution just
18 simply because of the name. I just picked a big
19 bank. I wasn't very savvy about it. I stayed with
20 them up until in my final year at college -- it comes
21 down to cost and convenience, at this point.
22 At one point, I bought a $4 snack in the

1 middle of finals week. Unknown to me, I got
2 charged with a $35 overdraft fee. As I was leaving
3 from that purchase, I decided to get a drink, as
4 well, got hit with another $35 overdraft fee. I
5 left the bank a week after that.
6 After that, it really was just about
7 finding a bank that could offer me a convenience.
8 That was exclusively online access. It was mobile
9 access. I knew I was going to be traveling a lot
10 for work. I've lived in five states over the last
11 three years. Things like being able to deposit
12 checks online were important, but it really just
13 came down to that convenience factor.
14 MS. KRAMER: I also have a community
15 bank located only in Florida. I first opened a,
16 I think, joint checking account there when I was
17 in high school and haven't really found a reason
18 to leave because I pretty much bank just based off
19 of the web and a mobile app on my phone. One thing
20 that was also very helpful is refunded ATM fees,
21 studying abroad, as well, those were all refunded,
22 so I could get cash there. So yes, the president

1 is a family friend, so I haven't really found a
2 reason to leave yet.
3 MR. BLANCHARD: My initial selection
4 for my financial institution was done by my
5 parents. They set up a savings account for me
6 there at an early age. And I just maintained that
7 relationship with them because they had a large
8 footprint on the East Coast, and they do offer a
9 lot of the online technologies that Greg was
10 mentioning. They had mobile banking, good web
11 applications, and also, they are part of a large
12 ATM network, so whenever I do need to get cash, I
13 can get that without the fees.
14 MR. SIMPSON: Clearly, the earlier you
15 get reached, the better. I also hear a lot of the
16 sort of like, the technology issue, in terms of
17 convenience, the refunding of ATM fees. That
18 helps you, obviously, if you're not able to reach
19 a branch or able to reach an ATM. The web apps,
20 certainly hear a lot of that, but really, the main
21 theme is trust and establishing a relationship,
22 right? Trust and establishing a relationship. I

1 know we're all very interested to hear about the
2 technology aspect. Maybe we could start by
3 talking about what products and services you
4 currently use, and what touchpoints or technology
5 you rely on to access your account. Greg, do you
6 want to start?
7 MR. LYONS: Yes. My primary
8 touchpoint with my bank is through the mobile
9 applications they have. I don't do any
10 transactions there, but I just review my finances,
11 just to know what's going on. In order to shift
12 funds, things of that nature, I do most of that
13 through their online application.
14 I'm a little different than the
15 panelists here. I have not been in a
16 brick-and-mortar location for my bank since 2013,
17 even though they have a location that's within two
18 miles of my house. I do use third-party apps, in
19 some instances, to also track. Being able to sync
20 up with those is useful. Like I said before, being
21 able to deposit checks through a mobile app is also
22 helpful.

1 MR. SIMPSON: How about you, Katie?
2 MS. KRAMER: I pretty much just use
3 check cashing. That's a separate app for my bank.
4 I can take a picture of it, and it's deposited.
5 Then I do also transfer funds via an app and get
6 a text message and an email sent when that happens,
7 kind of a fraud alert message, and then bill pay
8 services. I also do that online.
9 MR. SIMPSON: Frank?
10 MR. BLANCHARD: Additionally, I use
11 the web and mobile applications. I use the mobile
12 check deposits and the online balance transfers.
13 Additionally, I use some third-party applications,
14 such as Samsung Pay, which my financial institution
15 has teamed up with. That helps add a layer of
16 security.
17 MR. SIMPSON: Michael, how about you?
18 MR. MCCOY: My primary touchpoint is an
19 actual brick-and-mortar location. I use online
20 strictly to check and make sure that people have
21 cashed checks that I've written. I don't use
22 mobile. I'm way off from the rest of the panel on

1 that. In my town, banking is still a social
2 experience. You go in, have a cup of coffee, sit
3 down. You don't run in for five minutes. It's a
4 good half an hour catching up with people and
5 chatting.
6 MR. SIMPSON: So Greg, we heard from you
7 it sounds like it's not important at all to have
8 physical access to a branch, and then Michael, it
9 sounds like it is very important to have physical
10 access to a branch. How about for you, Katie, and
11 for you, Frank? How likely are you to go into a
12 branch? How important is it to you to be able to
13 go into a branch?
14 MS. KRAMER: If I were to get a big
15 loan, I would want to, I think, do that face to face.
16 But with my bank being in another state, as long
17 as I can pick up the phone and call someone that
18 I know and my bank's helpful with that, I really
19 don't need to physically go in.
20 MR. SIMPSON: All right. And Frank?
21 MR. BLANCHARD: It's not really that
22 important, but I like to know that if I really need

1 to go in to the institution, I can go in to a branch
2 that's nearby. Because I have branches, again,
3 like I said, they're all over the East Coast, so
4 I can access them whenever.
5 MR. SIMPSON: I know we talk about life
6 events. You said if I needed to get a big loan.
7 Does anyone on the panel see their banking service
8 needs changing rapidly or in a major way? Greg,
9 do you?
10 MR. LYONS: Absolutely. As I
11 mentioned, student loans are definitely going to
12 be part of my life for a long time. I already
13 started getting mail from people about
14 consolidation or other sorts of services they have.
15 I haven't taken up anyone on that yet. I will have
16 to consider that as those become more pressing. I
17 will likely have to look to different institutions
18 as I consider a mortgage or other things. I'm not
19 necessarily tied to my primary institution. It's
20 just where I am at this point.
21 MR. SIMPSON: Okay. Michael, how about
22 you?

1 MR. MCCOY: I've got pretty deep ties
2 to my bank already. They hold one of my mortgages.
3 They hold one of my car loans, my boat loan. I
4 don't really see myself moving from them anytime.
5 MR. SIMPSON: Bucking the trend with
6 the house and the boat. Greg, you kind of gave me
7 a good segue into the communication styles, in
8 terms of you've already been receiving information
9 about your student loans. There's a lot of talk
10 about how the style of communication is important
11 in being able to reach millennials. What's the
12 best or most memorable way that a financial
13 institution has reached out to you, and what made
14 that approach so effective for you guys? Katie,
15 can we start with you?
16 MS. KRAMER: I do get lots of emails and
17 mail from different financial institutions and,
18 honestly, delete the emails or rarely open the
19 mail. But the most memorable touchpoint, I think,
20 from my own bank, has been that they send me
21 hand-signed Christmas cards and birthday cards, I
22 think. That is just kind of a nice way to, again,

1 to not see the people who work there, but to know
2 that we have that relationship.
3 MR. SIMPSON: Right, to get touched by
4 them twice a year. There's nothing wrong with
5 that. How about for you, Frank?
6 MR. BLANCHARD: Same. Whenever I get
7 an email, I'm pretty much deleting it or throwing
8 the mail away. Basically, it's actually more me
9 reaching out to them. I know that whenever I call
10 my financial institution, I'm talking to someone,
11 not a machine or anything like that. I'm talking
12 to someone within under a minute, and it's good to
13 know that someone's always there, ready to pick up
14 the phone for me.
15 MR. SIMPSON: Greg?
16 MR. LYONS: This is the fact that most
17 of us did start these relationships during the
18 financial crisis. For me, the most effective
19 marketing was always trust based. As I mentioned,
20 that middle institution I had that charged me $70
21 in overdraft fees made me feel kind of like I was
22 a product, a line item. And so marketing that I

1 see that focuses on consumers, rather than
2 services, tends to influence me more.
3 MR. SIMPSON: Michael?
4 MR. MCCOY: I tend to get a lot of paper
5 mail, especially refinance your mortgage,
6 refinance your car. I don't open it anymore. I
7 just throw it away. What's important to me is the
8 fact that I can pick up the phone any time that I
9 need to and call and get somebody at my bank. They
10 can explain whatever it is that I need explained.
11 It's all about that personal contact for me.
12 MR. SIMPSON: Pretty easy to summarize
13 that, right? It's maybe not as important the
14 bank's reaching out to them, but important to be
15 able to get a hold of somebody, and them being able
16 to reach out to you. How about researching online?
17 If you're looking for things, is that sort of your
18 primary method? That would be where you would
19 start, or would you have a different method? You
20 would reach out, call them, go to a branch,
21 something like that? Greg?
22 MR. LYONS: I've actually expanded

1 services through my banks a couple times after
2 calling them. I will either have a question about
3 something I saw on their site online, but I've
4 opened two or three different products with them
5 just based on being able to reach somebody
6 immediately and have somebody come up with ideas
7 for how we can rectify that.
8 MR. SIMPSON: Katie?
9 MS. KRAMER: I usually would go to the
10 website.
11 MR. SIMPSON: You guys all indicated
12 that you have fairly established banking
13 relationships. I guess, Greg, yours maybe isn't
14 quite as relational. Is there anything that a bank
15 might offer you that could make you switch banks?
16 Michael?
17 MR. MCCOY: I've got pretty deep ties.
18 I feel like it would be very difficult to get me
19 to move from my current institution. You would
20 have to be offering something extremely
21 comprehensive. The start of that is it better be
22 somebody I know that's contacting me.

1 MR. SIMPSON: Okay, and Greg, how about
2 you?
3 MR. LYONS: I'll admit that yes, I'm
4 relatively transactional. As I mentioned
5 earlier, with student loans or mortgage products,
6 there are absolutely things that could be pitched
7 to me to get me to switch.
8 MR. SIMPSON: Katie?
9 MS. KRAMER: I think a similar answer
10 to Greg. If I'm looking for a mortgage or looking
11 at different rates or whatever, I would definitely,
12 probably compare between banks, but at this point
13 ---
14 MR. SIMPSON: Okay.
15 MS. KRAMER: I don't ---
16 MR. SIMPSON: A painful phone call to
17 your family president. How about you, Frank?
18 MR. BLANCHARD: Similar. If I'm
19 shopping for rates, like getting an auto loan or
20 a mortgage, I would definitely check other
21 financial institutions.
22 MR. SIMPSON: In shopping for that,

1 would you start at your bank? If, for example,
2 you're going for a home loan, you would just start
3 at your bank immediately?
4 MR. BLANCHARD: Sure. I would look at
5 the rates in my bank, and then start to branch out
6 from there and compare.
7 MR. SIMPSON: I think, again, I hear a
8 lot of the relationship issue, but certainly
9 there's the convenience factor plays a big role
10 with at least this panel. Before I switch gears
11 a little bit and really delve into millennials in
12 the labor force, when you talk about some of that,
13 I want to make sure I give you guys an opportunity
14 to -- if there's anything that comes up that you'd
15 like to talk about. Yes, ma'am?
16 MEMBER BLANKENSHIP: I'd just like to
17 ask Frank, so you said you would shop rates if you
18 were looking for auto or mortgage. If you found
19 a lower rate, would you go back to your bank and
20 ask them to match it?
21 MR. BLANCHARD: Absolutely.
22 MEMBER WILLIAMS: One of the things I

1 think I keep coming back to -- and I have three
2 millennial daughters. We were at my middle
3 daughter's house and my wife was looking for an
4 envelope. She said, Betsy, do you have an
5 envelope? She said, no. She said, how do you mail
6 your bills? She said, I don't mail bills. What
7 are you talking about? But the thing I keep
8 hearing, and the thing I think is community banks'
9 ace in the hole, I hear you guys talking about
10 relationships and being able to talk with someone
11 that you know or being able to talk to a human
12 being -- Greg, even in your situation, a little more
13 transactional. I keep looking at the fact that it
14 appears to me that millennials are -- given the
15 choice between a Home Depot or a Lowe's and a
16 neighborhood hardware store, where you know
17 people, the tendency is to go to that neighborhood
18 hardware store.
19 I get that impression. Given the
20 choice between a local coffee shop and a Starbucks,
21 you might tend to go to that local coffee shop. Am
22 I missing that, or are we on track? Because I think

1 that's our ace, as far as I'm concerned.
2 We're not going to be able to offer,
3 probably, the entire plethora of products that are
4 out there from some of the bigger banks, but we can
5 offer that service and having a human being answer
6 the phone, somebody that you know. That's got to
7 be the ace for us is having, really, as I refer to
8 it, the best of both worlds, the technology to get
9 it done, but the back door of always knowing you
10 can pick up that phone and call somebody. I keep
11 hearing that theme. That's not just you four,
12 right? That's the rest of --
13 (Laughter.)
14 MEMBER WILLIAMS: Am I missing the
15 boat on that, or are we pretty much -- that's going
16 to be key for us isn't it, is community banks?
17 MR. LYONS: I think you're absolutely
18 right. There's a huge opportunity here because
19 large institutions, for a while, were needed for
20 transient millennials because that was just the
21 only way to get money. Now, if you have good enough
22 services online, you don't need somebody with 1,000

1 locations. You could use somebody with five.
2 MS. KRAMER: If information is readily
3 available in the same way as a large bank, I think
4 that would be the preference.
5 PARTICIPANT: You'll take that every
6 time. Good.
7 MEMBER HASKIN: Let me ask you this
8 question. If you can't contact someone on the
9 weekend, does that pose a problem? Is having
10 immediate access to a real live person a necessity?
11 MR. MCCOY: I don't know about anybody
12 else, but my branch manager was a baseball coach
13 of mine. I'll pick up the phone and call him on
14 Sunday if I have to. When you've got their cell
15 phone number, you're good forever.
16 MEMBER BRYANT: Michael and Katie, you
17 appear to be very loyal and relations --- have
18 strong relationships with the institutions. The
19 one thing that I picked up from all four of you is
20 that peddling products to you, whether it's online
21 or through the mail, is not something that gets your
22 attention.

1 MR. MCCOY: No, even if it's something
2 that I need, I don't like it when people ---
3 especially when we come to the idea of everything
4 that you do online is tracked, and everything feels
5 a little bit analyzed. I really don't like things
6 that are specifically tailored to me popping up.
7 I just feel like there's a degree of intrusion there
8 that's a bit uncomfortable.
9 MEMBER THOMPSON: Even if it comes from
10 your bank, that still is not interesting to you?
11 MR. MCCOY: Luckily, I don't have that
12 experience with my bank. They don't send me
13 advertisements. We're a generation of people who,
14 the second we have a question, we're on our phones,
15 and we're looking up the answer in 15 seconds.
16 That means that products are -- it's almost better
17 just to be known as a presence, to have a bank -- I
18 don't mind banks reaching out at all just to
19 effectively say we're here, just in case you have
20 these issues, as I said, conveying that sort of
21 trust message. I do feel that people my age, if
22 we have a question about something, we'll do that.

1 We'll take out our phones, and we'll look it up.
2 MEMBER BRYANT: Here's a follow up
3 experience my wife and I have had. We had a car
4 salesman who's 18 years old. When you drive to the
5 lot, he might come out to see you. And if you come
6 in, he'll give you his card. He says, I'm not going
7 to try to sell you something you don't want.
8 You've done your research. You know what you want.
9 Once you've decided, come see me and we'll make it
10 happen. Is that the type of person that gets your
11 attention?
12 MS. KRAMER: For me, absolutely.
13 MEMBER BRYANT: This guy is the No. 1
14 salesman at his dealership in Louisville.
15 MR. MCCOY: I'm actually going to
16 relate directly to that. My most recent vehicle
17 purchase, I walked in, walked to the first
18 salesman, told him, this is what I'm looking for.
19 This is what I want. These are the options I want.
20 I know what dealership invoice is. Set me up. He
21 sold a car in 15 minutes, without having to do
22 anything. I feel like that's big for our

1 generation because we have access to this volume
2 of information. If it's something that we want,
3 especially on these larger ticket items, we're
4 really going to dig in ourselves. Because
5 honestly, there's a bit of institutional mistrust
6 after 2008.
7 MEMBER CASTILLO: Let me ask two or
8 three questions. You talked a little bit about
9 using a website to collect the information. How
10 much information are you looking for? For
11 example, if you're looking for a loan, are you
12 looking for pricing, fees, all-in costs,
13 application, being able to do that online, or are
14 you looking for -- you've got a general idea of
15 what's available, and then picking up the phone and
16 talking to somebody?
17 That's one question. The second
18 question is as you consider a financial
19 institution, does the fact that we're FDIC insured,
20 does that cross your minds at all? Is that
21 something that you assume is there, or do you even
22 care about whether that insurance is available?

1 MR. MCCOY: I find seeing that little
2 placard in the bank nice and comforting.
3 MS. KRAMER: We're FDIC employees, so
4 yes.
5 (Laughter.)
6 MS. KRAMER: But having said that, I
7 would say that most millennials probably don't look
8 for that plaque, if I'm being honest. I think it's
9 honestly assumed.
10 MEMBER LUNDY: Did any of you ever look
11 for that before you came to work for the FDIC, if
12 you can recall? Would that have been important to
13 you before you ever had this job, or did you even
14 think about it?
15 MR. LYONS: IndyMac wasn't that long
16 ago, so I think the knowledge that there is a safety
17 net is very important. I would be very -- I don't
18 think I'm alone in my fears that I'd be very worried
19 if I saw that an institution didn't have that.
20 MR. BLANCHARD: There is some lack of
21 information out there. I have friends that when
22 I've talked to them about institutions not being

1 FDIC insured, they go, what? That's possible to
2 do that? And so I inform them now, that they become
3 more aware of that. I would say the majority of
4 people I know, they don't look for the plaque.
5 They just assume that it's FDIC insured.
6 MEMBER BRYANT: Even with apps like
7 online to non-traditional lending they're
8 comfortable with it?
9 MR. BLANCHARD: I'm not too familiar
10 with that. I don't know of a lot of people who have
11 done that.
12 MR. SIMPSON: I have to say that the
13 less known we are, the better off everybody is.
14 It's not a bad thing when somebody has to ask you
15 what the FDIC is because that means we're not in
16 the news about something about banks needing to
17 access our funds. I just want to redirect into
18 that sort of labor force issue. And that way,
19 hopefully, we'll leave a little bit of time because
20 I think we're having a very good discussion, but
21 I want to make sure we cover everything. Switching
22 gears a little bit, in terms of the labor force,

1 what are the most important factors that you guys
2 considered in choosing your career path? Maybe
3 Katie, we'll start with you.
4 MS. KRAMER: In my graduating MBA
5 class, I think a lot of people went to go work for
6 big companies. Not that there's anything wrong
7 with that, but I knew that I did want to have
8 meaningful work, and not necessarily purely work
9 for the bottom line, kind of, with the main goal
10 being profit. Not that there really is anything
11 wrong with that, but the mission of the corporation
12 here is very well known.
13 It's a very integral part of our work.
14 Personally, I think that is a big reason why I do
15 enjoy my job, because you can see the effects of
16 what the FDIC does play out throughout the economy
17 and financial system. That was important for me,
18 as well as location and some work/life balance,
19 just being able to maintain personal priorities,
20 while still working hard.
21 MR. SIMPSON: Frank, how about you?
22 MR. BLANCHARD: The largest factor I

1 was looking for was where I was located. Growing
2 up in Virginia Beach, it is a metropolitan area,
3 but it's not a traditional one. It's based on the
4 tourist industry. I was looking for something
5 more city-like, so New York, Washington D.C., and
6 also somewhere on the East Coast. D.C. definitely
7 checked that box. Additionally, I was looking for
8 a job that, because I'm going to be living in a
9 metropolitan area, a job with a decent salary, so
10 that I could actually live there, because that can
11 be challenging now.
12 MR. SIMPSON: How about you, Greg?
13 MR. LYONS: So I might not be the target
14 market because with a degree in political science,
15 and then a Master's in political science, I have
16 fairly limited options.
17 (Simultaneous speaking.)
18 MR. LYONS: For me, the place that I
19 work, there's two things that really drive me to
20 look for someplace. One is a sort of mission
21 focus, but the other is that I really look for
22 places that I believe are meritocratic, where if

1 I come in and I work very hard, I have the
2 possibility of moving up the rank there.
3 Immediate benefits, to me, are less important than
4 the opportunities for mentorship and my overall
5 trajectory within a company.
6 MR. SIMPSON: Thank you. Michael.
7 MR. MCCOY: Having completed one
8 career already, I'm used to work that was extremely
9 physically challenging. When I started looking
10 around after that, I was looking for something that
11 was equally challenging in the intellectual field.
12 Doing something that's going to keep my mind
13 stimulated was important to me. At the same time,
14 I wanted to have a good degree of work/life
15 flexibility. I feel like I've worked my share of
16 14-16-hour days. Comp was slightly less
17 important, and maybe a little bit more time off,
18 a little bit more balance.
19 Unlike a lot of the other panelists, a
20 metropolitan area was not important to me. I like
21 to be convenient to the fishing and the boating and
22 the camping. D.C.'s not exactly my ideal

1 location, but the work here is worth the trade-off.
2 MR. SIMPSON: Again, to relate back to
3 the themes, I hear meaningful work and
4 community-type involvement. That certainly
5 relates to the theme. Then the obvious is the
6 urbanization sort of deal. But again, these are
7 not randomly selected.
8 These are all FDIC employees from here
9 and Washington, D.C., so it makes sense that they
10 have a stronger feeling about that. What do you
11 perceive as the benefits of working in a smaller
12 company versus working in a larger company, or if
13 you have experience in each, then maybe talk about
14 that. Frank, do you want to start?
15 MR. BLANCHARD: There's pluses and
16 minuses to both. In a smaller company, it's more
17 intimate setting. You can be closer to your
18 co-workers and really operate more efficiently in
19 a team environment. But also, there's those
20 pressures to maintain contracts and other outside
21 pressures such as that. In a larger company,
22 there's a perception that you could just be another

1 cog in the system. I know especially millennials
2 nowadays, they like to be more individualistic.
3 That can be a big turnoff for working in a large
4 company.
5 MR. SIMPSON: Katie, how about you,
6 small versus big?
7 MS. KRAMER: Same kind of themes.
8 There's definitely the perception that you can have
9 a closer relationship, I think, in a smaller
10 organization, maybe some more mobility upwards in
11 a larger organization. But I think, at the same
12 time, it depends. At a larger organization, you
13 can be in a smaller group of people working day to
14 day and form those relationships.
15 MR. SIMPSON: Greg?
16 MR. LYONS: I think one of the
17 stereotypes of millennials is that we tend to be
18 very impatient, that we expect things immediately.
19 For many of us, I think that there's a preference
20 to work in smaller institutions because, as I got
21 back to that point about meritocracy, you feel that
22 if you work very hard within a small institution,

1 that will be recognized.

2 You'll have more of an impact on the

3 organization, and you will hopefully rise up

4 faster. There are more mentorship opportunities

5 within large institutions, in my experience, but

6 I think that there's a preference for small.

7 MR. SIMPSON: Michael?

8 MR. MCCOY: I feel like I've run the

9 gamut a little bit on this. I've worked for a

10 company that was a grand total of eight people in

11 my hometown when I was a teenager to the 415,000

12 people that the Army employees. I've seen both

13 sides of the coin.

14 I kind of have issues with both. With

15 smaller institutions, it kind of feels like

16 sometimes, regardless of how well you do,

17 somebody's got to retire for you to move up. With

18 a larger institution, sometimes it feels like you

19 are a cog. To me, there's an important balance

20 there. It needs to be easy to move forward in your

21 career, but at the same time, you want to be doing

22 work that makes you feel like you're accomplishing

1 something and contributing.

2 MR. SIMPSON: I want to make sure that
3 I leave time. We have about 15 minutes, it looks
4 like. I want to make sure I leave time because I
5 know as presidents of banks, this is a very
6 important topic to you, as well, staffing the
7 appropriate levels at all levels of an institution.
8 Then, of course, we hear from examiners about
9 succession planning and things like that. If
10 there's some more questions about that, then we can
11 always go back, as well, to prior topics. Yes,
12 ma'am?

13 MEMBER BLANKENSHIP: I'd like to just
14 ask the question -- I think each and every one of
15 you said something about work/life balance and how
16 important that is. We're currently reviewing our
17 employee handbook, which probably has -- most of
18 the bankers here, we haven't really changed our PTO
19 policy, the two-week vacation. We do now allow
20 that to be split, but believe it or not, that went
21 decades and decades. Was that a big factor, and
22 do you look at flexible PTO? Is that pretty

1 important to you?

2 MR. MCCOY: For me, absolutely.

3 MR. LYONS: Flexible PTO is almost less

4 important to me than telework opportunities,

5 especially depending on where I live.

6 MS. KRAMER: It's important to me. I

7 have friends where I went to school in different

8 states and family at home. So to be able to take

9 a Friday or a Monday off and have a long weekend

10 is very nice for me.

11 MEMBER BLANKENSHIP: How about you,

12 Frank?

13 MR. BLANCHARD: I would say it's very

14 important to me. Initially, it wasn't so much

15 because leaving college, I was finishing up summer

16 break, and I still assumed that the rest of the

17 world had summer breaks, but ---

18 (Laughter.)

19 MR. BLANCHARD: Learned that lesson

20 really quick. Understanding that the company I

21 work for or will work for has a good PTO system,

22 I think that's very important.

1 MEMBER BLANKENSHIP: I think as
2 community banks, particularly, we're kind of
3 behind the eight ball. And the reason --- I have
4 millennial daughters, as well. My middle daughter
5 just went to work for an accounting firm. She got
6 more vacation than I have. But that is a huge
7 benefit and, I think, something that will snag
8 millennials and keep them as part of your labor
9 force. It's something that I think we're
10 challenged with, taking a step back and seeing how
11 we could be more flexible in that regard.
12 MEMBER WILLIAMS: I also heard a
13 recurring theme of mission focus, that there's
14 some -- you see the results of your work versus the
15 factory mentality, put the bolt here and put the
16 bolt here. That's something I keep hearing. I
17 think that's probably something we need to do a
18 better job of as leaders in community banks is
19 making sure that we're spending time sharing the
20 overall focus of what we're trying to accomplish
21 in our communities and making sure people
22 understand that they have a hand in making that

1 happen, so that's good to hear because that's
2 another ace, I think --
3 (Simultaneous speaking.)
4 MEMBER BRYANT: When Stephen
5 introduced each of you or you introduced
6 yourselves, I don't think I -- normally you guys
7 don't move into urban areas, but we have so much
8 technology and you can communicate with people all
9 over the world. From your conversations with
10 friends and peers, what's driving the modulation
11 from rural, small communities to larger urban
12 areas?
13 MR. MCCOY: I think opportunity has a
14 lot to do with it. Pittsburgh has kind of gone
15 through a renaissance over the last few years and
16 has recently been ranked as the No. 1 place for
17 recent college graduates to move. I think a lot
18 of that has to do with the vast array of
19 opportunities that Pittsburgh offers, not just in
20 financial services, but in tech and industry, as
21 well.
22 MR. LYONS: For me, my hometown, over

1 the last, actually, two years, has lost about 1,000
2 jobs, in a city of 17,000 people. Most people just
3 recognize that they can't stay somewhere that's in
4 decline. The feeling is that even they try to
5 start their careers there, they would have to move
6 at some point anyway. There's a feeling that
7 there's more opportunity, especially at the start
8 of your career, in a larger city.
9 MS. KRAMER: I think I agree. There
10 are probably different events held in big cities.
11 In D.C., for example, there's festivals on
12 weekends. Of course, you have the political arena
13 here, and things like concerts and that kind of
14 thing, where it is an exciting place to be for young
15 people. There's definitely a large proportion of
16 young people here. But at the same time, I also
17 like to go hike at the national park nearby and that
18 kind of thing. I think people are interested,
19 especially with technology, in different areas and
20 different --- there are rural areas with other
21 things that interest young people. But again, we
22 are four people who live here, so a little partial.

1 MR. BLANCHARD: Not just job
2 opportunities, but overall convenience. I live
3 within a 15-minute walk to work, so I can minimize
4 my commute by living in the city. Kind of what
5 Katie was saying, there's a lot going on here. I
6 can walk out of my apartment door and be anywhere
7 within 20 minutes, just walking, so I also get my
8 exercise, as well. I have a car, but I might drive
9 it once every two weeks. That's just to make sure
10 she still starts. It's a she.
11 MEMBER TOLOMER: First of all,
12 Michael, thank you for your service, appreciate it.
13 What would keep -- I don't want to make this an FDIC
14 thing, make it uncomfortable, but what will keep
15 a millennial in the job that they pick? Assuming
16 all the things that we've talked about, and now
17 you're working at an organization -- let's not make
18 this an FDIC issue, but what will keep a millennial
19 in the job?
20 MR. SIMPSON: That's an important
21 question. Frank, do you want to start?
22 MR. BLANCHARD: Sure. I think we were

1 talking about earlier, being able to see that our
2 work we're putting into it is showing results. Not
3 that you need recognition, but you know that
4 whatever you are doing, you're not just running a
5 report just to run the report, for the sake of
6 running a report. You know that it's going
7 somewhere; it's actually being utilized. Also,
8 just promotion potential, knowing that you know
9 that you're not going to be pigeonholed in this
10 position. You have that option -- not necessarily
11 promotion, but there are training-based programs
12 out there to help you learn more.
13 MS. KRAMER: Right. I would say,
14 again, not necessarily a promotion by a new title
15 or anything, but just the ability to not do the same
16 thing every day, to grow in your job and have some
17 new tasks, maybe feel -- for a small company, in
18 my opinion, it would be to feel like you have some
19 say in the long-term strategy of the corporation,
20 or at least to just be informed and forward looking,
21 and then, right, just receiving new challenges.
22 MR. LYONS: I don't think that if you

1 have any millennial employees that they're going
2 to want to be the president of the bank in a year.
3 There is the knowledge that you have to put in the
4 hard work. Things that will keep them there, in
5 my mind, are not even necessarily mentorship, but
6 feeling that they have some knowledge of where the
7 company's going, the feeling of they're learning
8 about the industry, itself, the feeling that
9 they're learning things that will help them if and
10 when they're ready for a promotion down the line.
11 I think that millennials are very quick to jump off
12 of a job that they don't feel is going to help
13 elevate their career.
14 MR. MCCOY: I tend to agree with a lot
15 of what was already said, but I think one thing that
16 we kind of missed focusing on is when I come to work,
17 I like to come to work. It's important for me to
18 come to work and know that I enjoy the people that
19 I work with, and I enjoy the work that I do. Work
20 dissatisfaction tends to bleed into personal
21 dissatisfaction for millennials, so part of it is
22 also the culture of the corporation. It should

1 feel like home.
2 MS. KRAMER: I think no matter what
3 you're doing, if you're with people who are excited
4 about it and passionate about it, it's definitely
5 a place you want to be.
6 MR. MCCOY: Even if you get to the point
7 where the work kind of gets tough or frustrating,
8 you're not really sure why you're doing it, if
9 you're doing it with people that you enjoy doing
10 it with, a lot of millennials will ride that feeling
11 out.
12 MEMBER LUNDY: You are obviously a
13 small subset. You're all well-educated. You all
14 work at the same place. Are the trends that were
15 talked about here, in terms of saving loans or
16 perhaps lower credit card debt -- you mentioned
17 student loan debt. As you look at your peers, do
18 you think that they are more debt averse than maybe
19 Gen Xers? What's your attitude towards that
20 issue?
21 MR. BLANCHARD: I would say they're
22 probably more debt averse. That's why you do see

1 a lot of people waiting to get a mortgage. You just
2 continually rent for a while. They don't want to
3 have that big burden on the books.
4 MR. LYONS: I'd have to disagree. The
5 millennials that I know, the reason they're not
6 buying a home is because they can't put 20 percent
7 down on a home in D.C. I'm not sure how many other
8 people can, either.
9 PARTICIPANT: I'm not sure how many of
10 us can.
11 MS. KRAMER: It's a little hard to
12 compare because we run around and -- we didn't know
13 the generation ahead of us at this age. I do know
14 many people who are saving.
15 PARTICIPANT: Who are saving?
16 MS. KRAMER: Mm-hm.
17 MR. SIMPSON: If you don't mind me
18 asking, do you guys all pay your credit card
19 balances the second you get your bill, or do you
20 keep a running --- yes.
21 MR. LYONS: The one thing I'll point
22 out, though, is that I think people in our age

1 bracket are sensitized to debt early on because
2 they are taking out a massive amount for student
3 loans. They're not necessarily shy of tacking on
4 debt. I think a lot of us have the feeling that
5 because we're savers, we want to have homes,
6 because then we feel like we're building equity,
7 rather than just throwing away money at the end of
8 every month. There is a desire to save, and debt
9 is sometimes seen as an avenue to help us build
10 assets.
11 MEMBER CASTILLO: Let me ask a
12 question. You mentioned that you're not familiar
13 with the prior generation, what that experience
14 was. Do you experience, or do you sense
15 inter-generational challenges as it comes to
16 certain things? For example, you all grew up in
17 the digital era. That's when you went to school,
18 you were starting in your professions.
19 There's folks like me that sometimes we
20 struggle with the technology that's available and
21 getting used to texting your child because they're
22 never going to answer your phone call, but they'll

1 respond immediately to the text. That's one
2 question, if there are any challenges there. The
3 other is I think some people of my generation
4 believe you're not doing your job unless you're
5 working 50-60 hours a week to get ahead. The
6 work/life balance is something that, for some older
7 folks, is a little bit foreign, if you will. I
8 guess the question, in a long-winded sort of way,
9 do you run into generational type of challenges,
10 and how do you address those, and in what areas?
11 MR. LYONS: Getting to your last point
12 about balance, I attend school in the evenings.
13 I'm a part-time student there. Everyone in my
14 program is working full time. They're attending
15 classes at night. I felt that I had too much time,
16 so I'm also assisting a professor for 10-15 hours
17 a week on another research project. I think that's
18 not uncommon. There's the feeling that we need to
19 put in a lot of work to get where we want to be.
20 I think that the assumption that millennials might
21 be lazy or feel that they're entitled to a promotion
22 just because they show up 9:00 to 5:00 every day

1 might be misguided.
2 MR. MCCOY: I agree with the assessment
3 there. There tends to be this belief that
4 millennials are sort of lazy, but as far as I'm
5 concerned, the truth is when I leave here in August
6 and go back to school, I go back to taking 18 credits
7 while working 50 hours a week at a local accounting
8 firm.
9 MEMBER WILLIAMS: To be clear, I wasn't
10 suggesting that anybody ---
11 (Laughter.)
12 MEMBER WILLIAMS: --- especially you
13 folks, were lazy. I think, really, the point is
14 there's 40 hours set aside for work. I've got to
15 do my best there, give it my all, and then I'm going
16 to move on to other parts of my life.
17 MS. KRAMER: I do think that work/life
18 balance does not necessarily just mean 40 hours a
19 week, and then I'm not at work. For example, here,
20 there's a fitness center. We can go during our
21 lunch break and run on the treadmill for 20 minutes
22 and come right back up and go back to work, that

1 kind of thing, just to where it's almost like you
2 can still maintain other priorities and not -- I
3 love the idea of working hard. I want to work. I
4 think it's almost more of a flexibility kind of
5 deal, even if you are working more hours than 40,
6 instead of just a certain number.
7 MR. SIMPSON: I'm going to try to keep
8 us on task because I know you guys have a lot of
9 important issues that are going to get put in front
10 of you today. I think we're kind of running up
11 against the end of our time. In an attempt to sort
12 of summarize and relate back to those themes we
13 talked about, in terms of choosing a bank, we heard
14 a lot of trust and establishing relationships. If
15 they can get you in there at three years old, then
16 apparently that's the easiest way to ---
17 (Laughter.)
18 MR. SIMPSON: In terms of keeping that
19 relationship, we've heard a lot about convenience.
20 Cost is certainly a factor, sort of the traditional
21 things that we'd hear from any generation.
22 Technology's obviously very

1 emphasized. Technology's very important,
2 particularly since the mobility of where you are
3 in your careers and moving around quite a bit, it's
4 important to be able to reach your bank without
5 having to change.
6 Communication, I heard a lot -- maybe
7 we didn't actually say it, but it sounds like the
8 social impact, your bank might be able to play a
9 role in terms of how active they are in the
10 community. That might be a better way to advertise
11 to you than actually sending something directly to
12 you. But in any event, everybody definitely said
13 that they like being able to reach their bank. You
14 like to be able to reach out to your bank and contact
15 them when they need to. Then in terms of the labor
16 themes, what I got out of it a lot was there's a
17 lot of upward mobility. A lot of is there
18 opportunity to grow in this career? You think
19 that's important. Then, of course, those same
20 themes, in terms of social impact. Everybody
21 seems to like what they see in terms of that, not
22 that it's completely altruistic, but certainly,

1 you have mission behind us, as well.
2 I think, again, that's all the time we
3 really have, so I don't want to take up too much
4 of you all's time, but I really appreciate you
5 having us here and allowing us to be involved in
6 this discussion, so thank you.
7 PARTICIPANT: Thank you guys very
8 much.
9 CHAIRMAN GRUENBERG: I'd just like to
10 say I have one observation that I found
11 enlightening, which is that you all seem to value
12 technology, the ability to engage with your
13 institution on a remote basis, but at the same time,
14 for most of you, it's also a value that you should
15 have a scale that you can reach and relate to, you
16 have people that you can actually necessarily call
17 on. So to me, actually, I found that interesting
18 and sort of encouraging. I sort of had an assumption
19 that if you're focused on doing your banking
20 online, I sort of had an assumption that the larger
21 institutions could offer a wider array of things,
22 it's almost the smaller institution offers the

1 basic services online that you need to do your
2 business, they're adding value of also having
3 somebody that you can contact, access, engage with,
4 and that you know is a real value for you. It
5 strikes me that's a combination where the smaller
6 institution can use technology functions to
7 advance its business and the two seem consistent.
8 MEMBER WILLIAMS: It's great news for
9 us.
10 MR. SIMPSON: All right, thank you,
11 guys.
12 (Simultaneous speaking.)
13 MS. RYAN: We're going to take a
14 15-minute break now, and we'll regroup at 10:45.
15 (Whereupon, the above-entitled matter
16 went off the record at 10:31 a.m. and resumed at
17 10:49 a.m.)
18 MS. RYAN: Welcome back, everybody.
19 We're now going to have senior staff provide the
20 committee with a brief update on the FDIC's ongoing
21 regulatory review being conducted with the other
22 federal banking agencies, in accordance with the

1 Economic Growth and Regulatory Paperwork Reduction
2 Act, or EGRPRA. To tell you about the latest
3 developments in the EGRPRA review process, Roberta
4 McInerney, deputy general counsel in our Legal
5 Division, and Ruth Amberg, assistant general
6 counsel in the Legal Division.
7 They will be joined by Jim Watkins,
8 senior deputy director in the Division of Risk
9 Management Supervision, and Bob Storch, who is our
10 chief accountant. After Roberta and Ruth provide
11 the committee with a general update on the EGRPRA,
12 Jim and Bob are going to tell the committee about
13 a number of related initiatives that are currently
14 underway. So I'll turn it over to Roberta now.
15 MS. MCINERNEY: Thank you, Barbara.
16 Good morning, everybody. It's great to see all of
17 you here. It's always a really interesting event,
18 and I always learn a lot, so thank you. As Barbara
19 mentioned, I'm delighted to be here. I'm here
20 along with my colleagues, Ruth Amberg, Bob Storch,
21 and Jim Watkins, to provide you with a brief update
22 on where we are in the EGRPRA process. As a very

1 quick reminder, the EGRPRA statute requires the
2 FDIC, OCC, and Federal Reserve to review our
3 regulations at least once every ten years.
4 The purpose of the review is to identify
5 any outdated regulations or those that are
6 unnecessary that affect insured depository
7 institutions. We conducted our last EGRPRA review
8 in 2006 and are on target to complete our current
9 review by the end of this year. The agencies began
10 the EGRPRA review in 2014, by publishing the first
11 in a series of four Federal Register notices that
12 requested comments from bankers and other
13 interested parties on our regulations.
14 The comment period for the fourth and
15 final notice ended this past March. The four
16 notices covered all regulations issued by the
17 agencies through December 31, 2015, so it did allow
18 comment on a number of the Dodd-Frank regulations,
19 as requested by bankers and others. As you know,
20 we organized each regulation according to 12
21 substantive categories, applications and
22 reporting, powers and activities, international

1 operations, banking operations, capital,
2 Community Reinvestment Act, consumer protection,
3 directors, officers, and employees, money
4 laundering, rules of procedure, safety and
5 soundness, and securities.
6 In addition to the Federal Register
7 notices, the agencies held six outreach sessions
8 --- excuse me, six outreach events across the
9 country in the West, the East, in the middle of the
10 country, and with over 1,000 participants
11 attending in person, by telephone, or via live
12 stream. The Kansas City outreach meeting
13 specifically focused on rural and community bank
14 issues.
15 We heard directly from many individual
16 bankers, as well as from consumer and community
17 groups, regarding their concerns with our
18 regulations. Agencies also received over 250
19 written comment letters in response to the four
20 federal register notices, and many of them are very
21 detailed, and they're very thoughtful comments, I
22 must say. We are now in the process of really

1 analyzing those comments, each one of the comments,
2 to prioritize them, to make sure we address all the
3 comment areas and consider all of them and
4 prioritize recommendations and consider
5 appropriate changes that we could make in our
6 regulations. Agencies plan to complete our final
7 EGRPRA report by the end of this year, and then
8 submit it to Congress, as required under the
9 statute. As you know, we haven't waited for the
10 issuance of the final report to take action.
11 We certainly began to take action in
12 response to some of the comments we received,
13 including some of the discussions we've heard at
14 this committee. For more information about the
15 actions the FDIC has taken so far and is still in
16 the process of taking, and also some of the things
17 we've heard from commenters, I'll turn the session
18 over to Jim Watkins. Jim.
19 MR. WATKINS: Thank you, Roberta, and
20 good morning. Please allow me to take a moment and
21 touch on a few of the regulatory burden reducing
22 initiatives and actions taken or in the process of

1 being taken. The FDIC is acting on regulatory
2 relief suggestions throughout the EGRPRA process,
3 and we appreciate the comments that we have
4 received at the outreach sessions and by this
5 group, as well. As a reminder of some of the
6 actions taken so far, we've issued several
7 financial institution letters, for example,
8 relating to the application process. In November
9 of 2014, we released an initial set of questions
10 and answers about the deposit insurance
11 application process to aid applicants in
12 developing proposals for federal deposit
13 insurance, and to enhance transparency of the
14 application process.
15 In April of this year, we issued an
16 update to these frequently asked questions. The
17 supplemental questions and answers addressed
18 business plan content with respect to initial
19 submissions, kind of addressing some weaknesses
20 that we've identified in other plans, and addresses
21 changes in business plans.
22 We also previously released a financial

1 institution letter relating to applications which
2 have significantly streamlined the requirements
3 for applications to conduct permissible activities
4 for certain bank subsidiaries organized as limited
5 liability companies or LLCs. These new procedures
6 are streamlining the process for institutions by
7 requiring far fewer applications, and in the cases
8 where it's necessary to file an application, most
9 of those decisions now are being made at our
10 regional offices. In April of this year, the FDIC
11 announced the rescission of a prior financial
12 institution letter titled, "Enhanced Supervisory
13 Procedures for Newly Insured FDIC Supervised
14 Depository Institutions," which basically
15 eliminated the enhanced supervision and reporting
16 requirements for institutions in the years four
17 through seven that were viewed as de novo
18 institutions.
19 The de novo period, now, for
20 institutions, is reverted back to the original and
21 customary three-year term. In addition, the FDIC
22 announced subject-matter experts that we have

1 placed and designated in each of our regional
2 offices to serve as points of contact for deposit
3 insurance application.
4 The FDIC remains committed to working
5 with groups interested in organizing community
6 banks. To that end, we are developing additional
7 resource materials, as suggested by Director
8 Doreen Eberley this morning, to guide applicants
9 through the application process. We're also
10 planning outreach meetings with the banking
11 industry and participants, organizing groups and
12 such, to ensure that industry participants are very
13 well informed about the FDIC's application
14 approval process, as well as available tools and
15 resources that we have issued in this regard.
16 For example, such tools include a
17 series of educational videos categorized often as
18 technical assistance, new directors' education,
19 and virtual directors' colleges produced by the
20 FDIC and available on our website under the
21 directors' resource center page.
22 These series are designed to provide

1 useful information to bank directors, officers,
2 employees on regulatory issues and proposed
3 regulatory changes and include over 25 available
4 videos, with topics ranging from operational areas
5 to cybersecurity and our examination process.
6 If you have previously reviewed the
7 community bank corporate governance video, you may
8 want to re-review it again because we've just come
9 out with an update, as you suggested earlier this
10 morning. One last change I wish to mention has to
11 do with the examination cycle. Upon authorization
12 provided under the FAST Act, the banking agencies
13 moved quickly to make an 18-month examination cycle
14 available to more community financial institutions
15 by increasing the eligibility threshold for
16 qualifying institutions from $500 million in total
17 assets to $1 billion in total assets.
18 That's very positive news for many of
19 you. Now, to continue our discussion on FDIC
20 initiatives and the work that's being performed in
21 that regard, let me turn the mic over to our chief
22 accountant, Bob Storch, who will talk about call

1 report changes.

2 MR. STORCH: Thank you, Jim. Good

3 morning. The FDIC and the other banking agencies

4 are continuing to move forward with the FFIEC's

5 Community Bank Call Report Burden Reduction

6 Initiative. I spoke to this committee in July of

7 last year about the five action areas that comprise

8 this inter-agency initiative.

9 The areas that may be of most interest

10 to you this morning are those where you can, or will

11 soon, see some concrete steps being taken to reduce

12 call report burden. One action area where the

13 agencies are in the final stage is the

14 implementation of an initial small number of

15 burden-reducing changes to the call report. These

16 burden-reducing changes were issued as part of a

17 proposal in September of 2015 that also included

18 some other revisions to the call report that

19 generally should have a limited impact on community

20 banks. After considering the comments and the

21 proposal, the FFIEC and the banking agencies

22 recently finalized these provisions.

1 On July 1st, the FFIEC sent a financial
2 institution letter to all institutions outlining
3 these final call report changes and when they would
4 take effect. Most of the burden-reducing changes
5 and some other revisions take effect September 30th
6 of this year, with the remaining changes taking
7 effect in March of 2017.
8 Drafts of the revised reporting forms
9 and instructions for these changes were posted on
10 the FFIEC's website in early July. The July 1st
11 financial institution letter also addressed
12 another action item under the Burden Reduction
13 Initiative, which is the agencies' consideration
14 of the feasibility of introducing a streamlined
15 call report for small institutions. At last
16 December's examination council meeting, the
17 FFIEC's task force on reports discussed several
18 options for the possible design of a
19 less-burdensome call report for small institutions
20 and other call report streamlining methods.
21 The agencies gained insight on the
22 burdensome aspects of the call report preparation

1 process from on-site visits to nine community
2 institutions during the third quarter of 2015, and
3 through a number of conference call meetings with
4 small groups of community bankers earlier this year
5 that were organized by the Independent Community
6 Bankers of America and the American Bankers
7 Association.
8 During the visits to banks and during
9 these conference call meetings, community bankers
10 explained how they prepared their call reports,
11 identified which schedules or data items take a
12 significant amount of time or manual processes to
13 complete, and described the reasons for these
14 challenges in call report preparation.
15 The bankers also offered suggestions
16 for streamlining the call report. The
17 constructive banker feedback about call report
18 burden and these options from the task force's
19 community banker outreach activities have helped
20 the agencies develop a specific call report
21 streamlining proposal for small institutions.
22 The proposal is now being reviewed by senior

1 leadership of the FFIEC's member entities. The
2 FFIEC and the agencies anticipate publishing this
3 proposal within the coming months. We believe it
4 should meaningfully expand the burden-reducing
5 changes to the call report well beyond those
6 included in the September 2015 proposal.
7 Once that proposal is published, we
8 certainly encourage you and invite you to share
9 your comments on the proposal and the industry's
10 comments, as a whole. We'll look forward to
11 receiving to try to move forward to implement a
12 streamlined call report for smaller banks. Thank
13 you. Roberta or Barbara, we can turn it back to
14 you for questions and discussion.
15 MS. RYAN: Okay, any comments or
16 questions from the committee, reactions?
17 MEMBER BLANKENSHIP: I just want to say
18 thank you because for our shop, there is quite a
19 bit of manual effort that goes into that. That
20 would free up -- unfortunately, it's the key people
21 in accounting and in the loan department that seem
22 to be particularly burdened. It's always at

1 quarter end and a busy time for banks, so thank you
2 for any relief that you could give us in that area.
3 MEMBER WILLIAMS: Overall, I think the
4 effort in this process was very evident to the
5 bankers, that you guys were very serious about
6 actually taking a look at this and doing what you
7 could to help streamline the process and help us
8 in any way you can. That's appreciated.
9 MS. RYAN: Okay, great. Thank you,
10 Roberta, Ruth, Jim, and Bob. Now, we're going to
11 turn to our next panel. We thought we would
12 provide the committee with an update on some
13 consumer compliance issues, particularly recent
14 proposed changes to the Consumer Compliance Rating
15 System for banks.
16 To lead us in this discussion, we're
17 going to have Jonathan Miller, deputy director in
18 our Division of Depositor and Consumer Protection,
19 and Luke Brown, associate director in our Division
20 of Depositor and Consumer Protection, as well as
21 Faye Murphy, who is a colleague of Jonathan and
22 Luke's. At this point, I guess I'll turn it over

1 to Jonathan.
2 MR. MILLER: Thanks, Barbara. Good
3 morning, everybody, although I'm mindful of the
4 fact that we're the last panel before lunch. It's
5 always a dangerous position to be in. I've asked
6 Luke and Faye to prepare a presentation on the new
7 compliance ratings proposal.
8 If we have some time after that, I may
9 talk briefly, also, about the new CRA guidance that
10 was just put out recently, and maybe a couple of
11 other things, but this will probably be the focus
12 most of the panel, so Luke, go ahead.
13 MR. BROWN: Good afternoon, everybody.
14 Happy to be here. On May 3, 2016, the member
15 agencies of the FFIEC released a proposal for
16 updating the inter-agency Consumer Compliance
17 Rating System. Just as a reminder, the FFIEC is
18 made up of the Federal Reserve Board, the FDIC,
19 CFPB, OCC, NCUA, as well as representatives from
20 the state banking agencies. I just want to
21 highlight that because this is something that we
22 all collectively worked on, in terms of consistent

1 guidance across the agencies, which I think will
2 be helpful to the institutions going forward. The
3 rating system is used by examiners to evaluate
4 financial institutions' adherence to consumer
5 compliance laws and regulations. Based on the
6 ratings framework, examiners assign a consumer
7 compliance rating to each institution, as you're
8 well aware. The main purpose of the rating system
9 is to ensure that supervisory institutions are
10 evaluated by the FFIEC agencies in a comprehensive
11 and consistent manner.
12 The goal is also to ensure that
13 supervisory resources are appropriately focused on
14 areas exhibiting risk and on institutions that
15 warrant elevated supervisory attention. The
16 public comment period ended not too long ago in
17 July, July 5th. We received 17 public comments,
18 which we're looking at very closely. We look to
19 hopefully receive some comments that will improve
20 the guidance.
21 Today, Faye and I are going to briefly
22 describe the proposal, as well as related

1 background information. But I do note that
2 because this is a proposal, and the agencies are
3 going through the public comments and looking for
4 input through those comments, I think it's
5 premature to have a conversation about what the
6 final guidance might look like as we work through
7 this. However, during this discussion, we welcome
8 any feedback you might have, and we will certainly
9 include that feedback in our process, going
10 forward, as we work with the other agencies. In
11 your packet, you might have a copy -- I shouldn't
12 say might.
13 I'm sure you have a copy of the
14 proposal, if you want to look at it. I think
15 particularly during Faye's portion of the
16 conversation, there's a table in the back that is
17 essentially is the framework and the meat of the
18 proposal. The existing rating system that's in
19 place now has been in place for some years.
20 It was adopted by the FFIEC when
21 examinations focused more on transactional
22 testing, sort of the more rule-based approach for

1 regulatory compliance, rather than evaluating the
2 sufficiency of an institution's management of
3 risks generally to ensure compliance. In May,
4 when the proposal was released, the proposal was
5 released in recognition of all the significant
6 changes that have taken place over the years. As
7 you are well aware, regulatory changes,
8 supervisory changes, market changes, there was no
9 CFPB when these were issued. We thought it was
10 important to revisit the guidance and take a look
11 at it very closely. We also, over the years, have
12 received requests from the industry to update the
13 compliance rating, so that was also front of mind
14 for us. The revisions are designed to more fully
15 align the rating system with the FFIEC agencies'
16 current risk-based approaches and our tailored
17 examination approaches.
18 The proposed revisions were not
19 developed to set new or higher supervisory
20 expectations. Essentially, they're consistent
21 with the way we've been examining for some time,
22 so they should represent no additional regulatory

1 burden. Since the existing ratings were issued,
2 each of the agencies has adopted a risk-based
3 consumer compliance examination approach.
4 As you know, risk-based consumer
5 compliance supervision evaluates whether an
6 institution's compliance management system
7 effectively manages the compliance risk at an
8 institution. Under this supervisory approach,
9 examiners tailor supervisory activities to each
10 institution and adjust these activities over time.
11 The revisions proposed in May would more fully
12 align the ratings system with the FFIEC agencies'
13 current examination approaches in a number of ways.
14 For example, the proposed revisions emphasize the
15 importance of institutions' compliance management
16 systems, in particular, risk-controlled processes
17 designed to manage risks in the products and
18 services offered to bank customers.
19 Another objective is to develop a
20 rating system appropriate for evaluating
21 institutions of all size. This is a really
22 important tenet for us, as we examine community

1 banks. Consequently, each oversight factor in the
2 proposal places an emphasis on examiners
3 evaluating the institution commensurate with its
4 size, complexity, and risk profile. That's very
5 important, and it's noted throughout, as you'll see
6 when we look at the proposal.
7 Also, a new rating system would
8 establish incentives for institutions to promote
9 consumer compliance by creating a framework for
10 recognizing when a bank is preventing or
11 self-identifying or addressing compliance issues
12 in a very proactive manner. We thought that was
13 also an important priority. In addition, the
14 proposal would promote coordination among the
15 agencies. Each of the agencies would import and
16 use the same rating system to apply to their
17 institution, so it would be a consistent standard
18 across all institutions, whether bank or non-bank.
19 With that, that's my overview of the proposal. I'm
20 going to ask Faye to go into a little more detail
21 and talk about the components and the structure of
22 the rating system.

1 MS. MURPHY: Thanks, Luke. The
2 proposal retains the current five-scale framework
3 for the proposed Consumer Compliance Rating
4 System. A one represents the highest rating and,
5 consequently, the lowest degree of supervisory
6 concern, while five represents the lowest rating
7 and the most critically deficient level of
8 performance and, therefore, the highest degree of
9 supervisory concern.
10 As Luke mentioned, the proposed rating
11 system reflects risk-based expectations
12 commensurate with the size, complexity and risk
13 profile of institutions and incents institutions
14 to prevent, self-identify, and address compliance
15 issues. Each institution would be assigned a
16 consumer compliance rating based primarily on the
17 adequacy of its CMS, which is designed to ensure
18 compliance on a continuing basis. The agencies
19 are proposing a rating system that includes three
20 categories of assessment factors, board and
21 management oversight, compliance program, and
22 violations of laws and consumer harm.

1 When assigning a rating under the
2 proposed rating system, the examiners will
3 consider each of the assessment factors in each
4 category. There are a total of 12. The three
5 categories allow examiners to distinguish between
6 varying levels of supervisory concern when rating
7 institutions for compliance with federal consumer
8 protection laws. The consumer compliance rating
9 should reflect a comprehensive evaluation of the
10 institution's performance.
11 It is not based on a numeric average or
12 any other quantitative calculation. Specific
13 numeric ratings will not be assigned to any of the
14 12 assessment factors. It is important to stress
15 that all institutions, regardless of size, should
16 maintain an effective CMS. The sophistication and
17 formality of the CMS typically will increase,
18 commensurate with the size, complexity, and risk
19 profile of the institution. It is also important
20 to note that the articulation of CMS assessment
21 factors is not intended to create new expectations
22 for lower-risk institutions. Now, I'll briefly

1 describe the rating system category and the
2 assessment factors.
3 The first category of the proposed
4 rating system, board and management oversight,
5 will be used to analyze the institution's CMS and
6 the role of its board and management officials.
7 The four assessment factors in this category would
8 be oversight and commitment, which would measure
9 the overall institution's compliance risk
10 management program.
11 There's change management. This is
12 where we measure the effectiveness of the
13 institution's change management processes,
14 including responding timely and satisfactorily to
15 any variety of change, internal or external, to the
16 institution.
17 There's comprehension identification
18 and management of risk, which would arise from the
19 institution's product services or activities, and
20 then also under this category, there's corrective
21 action and self-identification, where you're
22 looking at corrective action undertaken as

1 consumer compliance issues are identified.
2 Compliance expectations contained within this
3 category extends to third-party relationships,
4 into which the financial institution has entered.
5 Examiners should evaluate activities conducted
6 through the third-party relationships as though
7 the activities were performed by the institution,
8 itself.
9 The agencies believe the above factors
10 will provide examiners with an effective and
11 consistent framework for evaluating whether or not
12 board and management are engaged to a satisfactory
13 degree at a particular institution. All
14 institutions, regardless of size, should maintain
15 an effective CMS.
16 However, each institution should be
17 evaluated based on its size, complexity, and risk
18 profile. You'll notice that we're going to keep
19 mentioning that. The second category, compliance
20 program, would be used to analyze other elements
21 of an effective CMS. The assessment factors for
22 a compliance program are policies and

1 procedures -- here's where we look at whether the
2 institution's policies and procedures are
3 appropriate to the risk in the products, services,
4 and activities of the institution. The next
5 assessment factor is training. Here's where we
6 look at the degree to which compliance training is
7 current and tailored to risk and staff
8 responsibilities. Also, we'd look at monitoring
9 and/or audit.
10 Here's where we look at the sufficiency
11 of the monitoring and, if applicable, audit to
12 encompass compliance risks throughout the
13 institution. Finally, in this category, there's
14 the consumer complaint response. Here's where we
15 look at the responsiveness and effectiveness of the
16 consumer complaint resolution process. Examiners
17 should also review a financial institution's
18 management of third-party relationships and
19 services as part of its overall compliance program.
20 The agencies believe these factors,
21 along with board and management oversight, will
22 provide an effective and consistent framework to

1 evaluate an institution's CMS. Each of these
2 assessment factors will be considered in
3 evaluating risk and assigning a consumer
4 compliance rating. As previously mentioned, each
5 institution would be evaluated based on its size,
6 complexity, or risk profile. Next time, I'll have
7 you all say it with me. The third category,
8 violations and consumer harm, will provide
9 examiners with a framework for considering the
10 broad range of violations of consumer protection
11 laws and evidence of consumer harm. Consumer harm
12 may occur as a result of a violation of law.
13 While many instances of consumer harm
14 can be quantified as a dollar amount associated
15 with financial loss, such as charging higher fees
16 for a product than was initially disclosed,
17 consumer harm may also result from a denial of an
18 opportunity. In conjunction with assessing an
19 institution's CMS, based on the first two
20 categories, examiners will evaluate the consumer
21 protection violations, if any, and related
22 consumer harm, based on the following four

1 assessment factors.
2 The root cause assessment factor
3 analyzes the degree to which weaknesses in the CMS
4 gave rise to the violations. The severity
5 assessment factor weighs the type of consumer harm,
6 if any, that resulted from violations of law. The
7 duration assessment factor describes the length of
8 time over which violations occurred, and the
9 pervasiveness assessment factor evaluates the
10 extent of the violations and resulting consumer
11 harm, if any. Examiners are directed to consider
12 all violations of consumer law, based on the root
13 cause severity, duration and pervasiveness of the
14 violation.
15 This approach emphasizes the
16 importance of a range of consumer protection laws
17 and is intended to reflect a broad array of risks
18 in the market and the potential harm caused by
19 consumer protection-related violations. In
20 conclusion, we want to emphasize that the agencies
21 believe that self-identification and prompt
22 correction of violation of law reflect strength in

1 an institution's CMS.

2 We want to emphasize that a robust CMS,
3 appropriate for the size, complexity, and risk
4 profile of an institution's business often will
5 prevent violations or will facilitate early
6 detection of potential violations. This early
7 detection can limit the size and scope of consumer
8 harm. We also want to emphasize that prompt
9 self-reporting of serious violations represent
10 concrete evidence of an institution's commitment
11 to responsibly address underlying risks. In
12 addition, appropriate corrective action,
13 including both corrections of programmatic
14 weaknesses and full redress for injured parties
15 limits consumer harm and prevents violations from
16 occurring in the future.

17 Finally, we want to emphasize that the
18 intent of the proposed Consumer Compliance Rating
19 System is to recognize institutions that
20 consistently adopt the strategies that I just
21 previously discussed. With that, I'm going to
22 turn it over to Jonathan.

1 MR. MILLER: I think maybe we can have
2 a little bit of a discussion on this proposal since
3 there's a lot to digest here. You may have a lot
4 of questions. I do want to underscore, I think,
5 the message that we're trying to give both
6 externally, to the bankers -- and this is, again,
7 on an inter-agency basis -- and internally, to our
8 examiners is we believe that these changes make the
9 ratings -- catch the rating system up with the
10 process we actually use. We're not really
11 expecting changes in our ratings, but the old
12 ratings which, again, as Luke mentioned, were last
13 done in 1980, just didn't really -- just were not
14 really matching with the process we were using.
15 That's our fundamental message point, but it's a
16 significantly new system, so I know there may be
17 a lot of questions. Let me open it up.
18 MEMBER BRYANT: I thought I needed to
19 get this in. I think this is a great improvement.
20 One of the items that I got a chance to read, looking
21 at Pages 20-23, mentioned something about a
22 violation of law or having major problems, not

1 necessarily keeping the institution from receiving
2 a 1 or a 2 compliance. The area that I think is
3 extremely helpful for institutions is the area of
4 corrective action and self-identification.
5 Without having a chance to read through
6 all of it, corrective action, self-identification,
7 I would assume would also include having compliance
8 committees comment on this include information
9 that's shared with board members, so that when
10 there's a Safety & Soundness examination, the
11 examiners will be able to go and look at minutes
12 to see that the board has seen that there have been
13 compliance issues or it's a violation of law, and
14 that it was properly identified and pointed to the
15 board and corrective action taken, correct?
16 MR. BROWN: Obviously, there's a
17 number of ways, whether it's through the monitoring
18 or audit or reports. If an issue is identified and
19 you resolve that issue, that's something that we
20 like to see when we come in for a formal
21 examination. There's no express mention of that
22 in the current, existing rating system, so we

1 wanted to make sure we outlined that very
2 specifically in the proposal, so that people could
3 get credit when they self-identify appropriately.
4 MR. MILLER: There's a helpful -- I saw
5 it on Page 24. There's a helpful chart. I think
6 right in the very first box there, under the board
7 and management oversight assessment factor, for a
8 one rating, examiners will evaluate if board and
9 management demonstrate strong commitment and
10 oversight of the financial institution's
11 compliance system, so exactly what you said,
12 evidence of that active participation by the board
13 is important.
14 MEMBER WILLIAMS: I know we talked
15 about not getting into the details about what the
16 final will look like, but as it's proposed, I'm
17 assuming there's effectively three component
18 ratings and an overall composite rating?
19 MR. BROWN: That is not correct.
20 Every institution's business, essentially, is
21 different, obviously. You could have a focus on
22 mortgages or credit cards. Every time you go to

1 an examination, you're looking at it from a
2 risk-based perspective.
3 As opposed to a component rating that
4 would be stagnant and applied consistently every
5 time, we think it's important for an examiner to
6 use their judgment. So to the extent that board
7 and management involvement, in terms of good things
8 or negative things, is considered consistent with
9 what's going on at that institution.
10 If you had a component rating and it
11 equally was weighted across this whole area, that
12 would not work for all institutions. We want to
13 be able to give people credit for where they're
14 doing well and emphasize that when we're doing an
15 assessment.
16 MEMBER WILLIAMS: So no --
17 (Simultaneous speaking.)
18 MR. BROWN: It's just an overall.
19 MEMBER WILLIAMS: Just an overall,
20 okay. I was under the impression there would not
21 be individual ratings for -- I'm sure appreciative
22 of that fact, that for rate 12 categories, so it

1 would just be the overall composite?
2 MR. BROWN: That's right, but all
3 examiners will consistently think through those 12
4 components. That's what's important.
5 MR. MILLER: Any other comments?
6 MEMBER HASKIN: I would just say that
7 we have just had waves and waves of new consumer
8 regulations put upon us, and some of those have not
9 had very large windows to train and educate, and
10 even to acquire software to be prepared. And so
11 I would just say that we find ourselves constantly
12 reviewing to make sure we're doing things right
13 these days, and even though we think we're
14 prepared, sometimes we don't know what we don't
15 know until we actually do a loan.
16 So I would hope that in this time of new
17 regulations that the examiners would be mindful of
18 that. That banks are really trying to do the right
19 thing, but it's sometimes difficult to comply to
20 the letter. Especially the mortgage rules.
21 We're struggling. We keep sending people to
22 schools and quite honestly, a lot of the training

1 we receive we're getting different messages,
2 conflicting messages, as this process of actually
3 preparing loans and using these new regulations as
4 they're implemented, finding out those differences
5 and what applies. So I would just pray that you
6 be mindful of that.
7 I know that we spend a tremendous amount
8 of time in our bank trying to be correct on
9 compliance issues, but we have just really been
10 struggling to make sure that we're doing everything
11 correctly.
12 MEMBER WILLIAMS: I would just add,
13 too, especially in light of -- when you start
14 talking about time frames, that's probably been the
15 biggest issue for us, as far as some of the mortgage
16 regulations. While I understand that the FDIC is
17 not writing this, you're regulating it.
18 There's that fine balance for us
19 between taking care of our customers and doing it
20 the right way. I'm sure some of the other bankers
21 have seen this, but we've seen a great deal of
22 customer response saying we trust you. We don't

1 need four days to look over this document.
2 Our response is don't care, you've got
3 to take it. You can't have your money until
4 this -- those are the kind of things -- the hoops
5 that have been hardest for us to jump through.
6 Again, I would just echo Jane's comments. Be
7 patient with us as we try to get through this
8 process.
9 MR. BROWN: I just want to mention
10 we've been in touch with our examiners, and we stay
11 in touch on what's happening on the ground, in terms
12 of issues that you're seeing and challenges
13 you're having. We did issue a financial
14 institutions letter last fall, which says we're
15 mindful of all the changes, and we're keeping that
16 in mind as we examine.
17 MEMBER WILLIAMS: We saw that in the
18 process of our exam. I agree. It's a slower
19 process than we had hoped it would be trying to get
20 on top of all this, and it keeps changing. That's
21 the problem.
22 MEMBER BLANKENSHIP: Just to kind of

1 touch on that, as well, just with the new TRID
2 disclosures and the title companies and everyone's
3 interpretation being just a little bit different,
4 we're seeing more than ever that the consumers are
5 actually being harmed by this.
6 Because you have a closing set on
7 Friday, movers lined up. They've brought the dog,
8 the cat, kids, and then they can't close because
9 it's one little line, and everyone is so paranoid
10 about changing anything before they get 14 stamps
11 of approval that it really is creating a lot of
12 delays, at least in our experience, for that
13 consumer.
14 MR. MILLER: When the first set of
15 mortgage rules went into place in the run up to that
16 in 2013, they went into place in 2014, we took the
17 position that what we were -- we would not expect
18 for our banks to have everything absolutely
19 perfect. We were going to look for efforts by the
20 bank to get in compliance, actively to get into
21 compliance, an understanding of the requirements
22 and so forth.

1 That's the position we took with the
2 first set of rules. We took exactly the same
3 position with TRID, what the CFPB calls know before
4 you owe, the combined TILA-RESPA disclosures, as
5 Luke just outlined. We've actually pulled our
6 examiners and have found that for the most part,
7 the banks are doing that.
8 We're finding some violations, where
9 we're noting the violations where we find them,
10 just to have a record, but without really any
11 consequence, as long as, again, the bank is
12 pursuing the effort to get into compliance. Even
13 the violations we saw were not particularly
14 significant. From our experience, I think we're
15 seeing a nice path towards compliance among our
16 institutions.
17 MEMBER HASKIN: One other thing I'll
18 mention is the reference material for lenders to
19 use is very complicated. It refers to sections of
20 the code. It's not user friendly. And a lot of
21 our people have tried to research that to
22 understand exactly how we need to disclose, and

1 it's very difficult to use the information that's
2 out there as a user to know how to do the documents,
3 because it refers a lot to the code. I believe
4 that's the CFPB's code.
5 MR. MILLER: Right, they have --
6 MEMBER HASKIN: So I don't know if
7 that's something that all the agencies can work on,
8 but our people do try to research those things, and
9 that's one of the things that my documentation
10 preparers have told me, is that it's very, very hard
11 to get any guidance from that documentation.
12 MR. MILLER: The CFPB has put out a lot
13 of educational material
14 (Simultaneous speaking.)
15 MEMBER HASKIN: There is material out
16 there, pieces out there, but they all reference
17 codes. It's so cryptic that we can't discern how
18 we're supposed to use it. It's very cryptic
19 referring to the code.
20 MR. MILLER: That's a helpful comment,
21 and we can pass that along. Any other --
22 MEMBER LUNDY: Since this is my last

1 meeting on the committee, I'll throw something out
2 that I threw out probably at my first meeting. I
3 throw this out for a suggestion for the kind of
4 research that I know you all committed to do. I'm
5 from a western state -- there are nine community
6 property states. Each one of them has a slightly
7 different variance on it. Sometimes, those
8 community property laws, which were forward
9 looking at the time, in terms of equal ownership
10 of property, and are generally forward looking, and
11 in some ways, equal opportunity credit laws passed
12 two generations later caught up with the same
13 thing.
14 But for our frequent instances where
15 the specifics of those community property laws were
16 in variance with technical interpretations of
17 equal opportunity, and there's some confusion
18 about that. The thing that comes up most often is
19 called the spousal joinder issue. It's whether
20 and when a spouse, who may have separate property
21 and may not be directly involved in a business, it's
22 appropriate to either have that spouse join in the

1 guaranty, or whether and how the financial
2 institution analyzes property.
3 This is not the appropriate time to get
4 into all the nuances, but it is a nuance they
5 complicated -- and different because California
6 and Arizona and Nevada and Washington all have
7 slightly different variations on the theme. So I
8 would just suggest, as a future item, that jointly,
9 you all could get on that and work on it and try
10 to come up with a common roadmap, where there are
11 differences in state law that has to -- that's, I
12 think, probably the reason that it's been difficult
13 to try to get a common roadmap because those
14 differences make it difficult.
15 At any rate, I think that's an area that
16 can cause some confusion. Ironically, the one
17 area where all the potential violations of
18 requiring a guaranty when you shouldn't have go out
19 the window for SBA on this one. Small Business
20 Administration absolutely requires both spouses to
21 sign, no matter the source of their personal
22 property, the ownership source.

1 At any rate, I don't have a specific
2 suggestion, other than it can be an ongoing
3 irritant, and sometimes a major issue in a
4 compliance exam. I just throw that out as a
5 suggestion for future work.
6 MEMBER WILLIAMS: I'll make one last
7 comment. It's one I probably made before. I
8 think having just gone through a compliance exam,
9 this rating system matches up much better to what
10 the examiners did and how they looked at the bank.
11 While somebody made reference earlier today to the
12 fact that the pre-exam questionnaire is much
13 lengthier than it was, in fact, I think our folks
14 said, "I think we got more than one copy." I said,
15 "No, I think this is it." It took quite a bit of
16 time to get that information in, but it was
17 done -- that information was used well up front.
18 The amount of time in the bank was
19 limited. The results were great. It's the right
20 path, at least all the folks that I've talked to
21 that have been through exams, my counterparts,
22 recently, that experience has been very positive.

1 That's very much a step in the right direction.
2 Thank you.
3 MEMBER SCULLY: I just have a
4 clarifying question, which is that presumably all
5 harm is deemed a subset of a violation, just a claim
6 of harm, but without it being a violation --
7 MR. MILLER: Right. You wouldn't just
8 have a claim -- a claim of harm is not sufficient --
9 MEMBER SCULLY: We all know we get
10 claims of harm --
11 (Simultaneous speaking.)
12 MR. MILLER: Right, and that may
13 not -- we have a complaint line, a consumer response
14 center. We get a lot of calls there. We track
15 down those. If there is a problem -- it's actually
16 a good source of intelligence for us. If there is
17 a problem it's very helpful, but it often turns out
18 not to be a problem at all.
19 MEMBER SCULLY: And specifically not
20 to be a violation.
21 MR. MILLER: Well right. If it's not
22 a violation then yes. Anything else?

1 MEMBER BRYANT: You will be around for
2 a few minutes, right?
3 MR. MILLER: We will.
4 MR. BROWN: Longer than that if you
5 need it.
6 MR. MILLER: I'll just quickly
7 cover -- just recently, we released a second set
8 of Community Reinvestment Act questions and
9 answers. These have been outstanding for quite a
10 while. We've been working with the OCC and the fed
11 to finalize them, to update some of the guides for
12 the CRA. They were finalized just last week, as
13 a matter of fact. Basically, they're additional
14 guidance in a number of areas. Availability and
15 effectiveness of retail banking services is one of
16 the areas we put out some additional guidance,
17 innovative and flexible lending practices.
18 Just as an aside, because of a meeting
19 I had yesterday with Jim and a colleague that he
20 brought in, one of the things that we look for in
21 CRA as sort of a plus is if a bank does something
22 innovative to serve the low and moderate income

1 community in its assessment area.
2 Jim brought in a person that's doing an
3 IDA account. It's an individual development
4 account to help low and moderate income people for
5 college education. It's quite an intensive
6 account management process. Even if other
7 institutions in an area provide a service, if it's
8 new to that institution, we will consider it
9 innovative.
10 In fact, in that case, I don't think
11 there are many other institutions -- of kinds we
12 look for. It includes some community development
13 related issues, including economic development,
14 community development loans and activities, and
15 revitalize or stabilize underserved non-metro
16 middle income geographies and community
17 development services. It's a nice set of helpful
18 guidance that will help your institutions figure
19 out better ways to serve your communities.
20 MEMBER SCULLY: It's a lengthy
21 document, but I commend you for at least trying on
22 the community development I think it's always

1 difficult to determine is this really needed
2 development or not.
3 MR. MILLER: Two areas that might just
4 be worth calling out is investment in broadband
5 infrastructure, which is going to be increasingly
6 important for community, as a whole, as long as it
7 includes low and moderate income segments.
8 That's, I think, going to be particularly important
9 as we talk to the millennials and the importance
10 of technology to them, so having community banks
11 have access to high-speed Internet. Then energy
12 efficiency, as well, is another area that we've
13 sort of elevated for community development.
14 MEMBER SCULLY: But they both have to
15 be directed at --
16 MR. MILLER: Include, yes, correct.
17 If it's a small community and you're providing
18 access to the whole community, you'd get credit for
19 that. You couldn't cut out the low and moderate
20 income. Thank you.
21 MS. RYAN: Okay, thanks, Jonathan,
22 Luke, and Faye. Right now, we're going to take a

1 break for lunch. We'll reconvene at 1:00. So all
2 of the committee members and senior FDIC staff are
3 welcome to join us upstairs. Thanks.
4 (Whereupon, the above-entitled matter
5 went off the record at 11:40 a.m. and resumed at
6 1:09 p.m.)
7 MS. RYAN: Welcome back, everybody.
8 We're now going to focus on financial technology,
9 or what is called fintech issues. We have senior
10 staff from our Division of Risk Management
11 Supervision and Division of Depositor and Consumer
12 Protection, I think most of whom you've already
13 heard from today, except, I believe, Rae-Ann Miller
14 is new with us today. She's associate director
15 with the Division of Risk Management Supervision.
16 With that, I'll turn it over to Doreen.
17 MS. EBERLEY: I'm going to quickly turn
18 it over to Jim. Mark and I have strategically
19 placed ourselves on the other end of the speakers.
20 Jim, if you can kick us off.
21 MR. WATKINS: Thank you, Doreen, thank
22 you, Mark, and good afternoon. The FDIC

1 continually monitors emerging issues, emerging
2 trends for financial institutions and really, the
3 financial industry as a whole. Financial
4 technology or fintech is one of those emerging
5 issues that we are exploring and looking at.
6 It is becoming a rather significant and
7 important topic for the banking industry. It is
8 also important for the FDIC and for community
9 bankers. We'd like to spend some time with you
10 this afternoon discussing this matter and solicit
11 your feedback, your insights, your comments. We
12 have a brief slide deck. We have eight slides that
13 we'd like to walk through, and then kind of open
14 it up for a broader discussion.
15 If I could turn your attention to the
16 second slide, which is FDIC's fintech steering
17 committee and the objectives of our steering
18 committee. Let me begin by noting that the FDIC
19 has formed a fintech steering committee, which is
20 comprised of FDIC executives from supervision,
21 from compliance and consumer protection, from our
22 insurance and research areas. It also includes

1 representation from our Office of the Chief Risk
2 Officer, and also our Legal Division, as well. The
3 objectives of the steering committee are outlined
4 here.
5 Basically, it's to gain an
6 understanding and assess, monitor, if you will,
7 fintech activities, developments, and trends,
8 understand in greater detail what is occurring in
9 the market and what may be occurring in the market,
10 evaluate the impacts to our organization and our
11 stakeholders, banking, especially community
12 banking, the deposit insurance structure.
13 Supervision and oversight would be included in
14 that, as well as economic inclusion, and consumer
15 protection.
16 Also, the steering committee objective
17 would be to oversee our internal working groups
18 that the FDIC has formed relating to fintech. We
19 will talk a little bit more on that topic in the
20 next couple of slides that follow. But
21 essentially, we have a staff that is actively
22 researching and gaining an understanding and

1 insights into the fintech area and its multiple
2 aspects relating to banking. Then the steering
3 committee may end up making recommendations for
4 follow-up action and monitor any implementation of
5 those recommendations.
6 Then finally, it is to help formulate
7 potential strategies to respond to opportunities
8 and challenges presented by fintech to ensure
9 developments align with our regulatory objectives
10 and goals. The idea here is that as this area
11 evolves, we want to make sure that we understand
12 it and are prepared for it and how it would affect
13 our jobs. Now, I will turn the next slide over to
14 Rae-Ann Miller.
15 MS. MILLER: Thanks, Jim. As we talk
16 through fintech just amongst ourselves, with our
17 colleagues at the other agencies and other
18 stakeholders that come in and visit with us, we
19 start with what is it. I think there's some debate
20 there. This definition here -- I'm not going to
21 read it; you can read it yourself -- it's from the
22 Financial Stability Board. Broadly here, when we

1 talk about it, we look at fintech as the use of
2 technology in an attempt to make financial services
3 more efficient. In this regard, it's nothing new.
4 You folks look for ways to improve efficiencies,
5 I would assume, in your jobs. Under this
6 definition, ATMs probably would have been fintech
7 at one point, but I can't remember a time when we
8 didn't have them.
9 In some respects, fintech is viewed as
10 a potential to existing financial services, that's
11 the whole disruption theory. That part is more of
12 a customer service dimension, but there's a whole
13 other area of fintech that has to do with trying
14 to improve efficiencies in the back office space.
15 Slide 4, I wanted to just expand a little bit more
16 about what we look at, in terms of the dimensions
17 of fintech.
18 Obviously, there are fintech companies
19 and processes that develop credit products. We
20 talked to this committee a few meetings ago about
21 marketplace lending. It's probably the most
22 visible example in the credit space, but we also

1 look at crowd funding in this group. There are
2 other credit products in this segment that are
3 emerging, as well. There's also companies that
4 specialize in offering deposit accounts without
5 brick and mortar. We heard the folks today. One
6 guy didn't go into a bank for two years. There are
7 companies, mostly partnering with banks, at this
8 point, that just offer deposit-gathering services.
9 Then within the payment sphere, there's a number
10 of person-to-person payment systems,
11 international payment transfer and currency
12 exchanges. Some of our millennials that work
13 here, not the ones that were up, but other ones,
14 will Venmo you.
15 I'll Venmo you later, if you go out to
16 lunch. That's paying each other. I had to be told
17 what that was, but that's what that is. In terms
18 of investment management and personal finance,
19 there's companies and applications that aggregate
20 accounts. People know those. I think, again, one
21 of the millennials actually talked about using one
22 of those.

1 There's investment allocation
2 packages, and even high-frequency trading we view
3 as coming in this area. Then the back office
4 processing covers things like distributed ledger
5 technology that you may have heard about and smart
6 contracts. Then under the capital markets, when
7 we're talking about that, we look at companies and
8 services that facilitate, basically, trading,
9 settlement and even security valuation services.
10 Moving to Slide 5, this is sort of a list of our
11 views of benefits to fintech. Again, I'm not going
12 to read them all. You can see them here. But at
13 its core, the technological innovation tends to
14 promise speed, cost reduction and a better customer
15 experience.
16 With fintech, and especially with some
17 of the companies that deal with deposit and credit
18 products, they talk about increasing access to the
19 banking system, as well. It may be in a different
20 way, but a lot of the things that you folks do, as
21 well.
22 From our perspective -- this might be

1 one you haven't thought about, but from our
2 perspective, in supervising, insuring and
3 resolving institutions, there might be certain
4 fintech advancements that could allow quicker
5 access to information we need to do our jobs. In
6 that way, maybe we could do our jobs in a less
7 intrusive way, as well. I'll turn it over to Jon.
8 MR. MILLER: If you look at Slide 6, of
9 course, like anything new, there are also
10 challenges and risks. For our banks, when they
11 enter into any new product, service or third-party
12 relationship, whether that's fintech or any other,
13 they need to identify and understand the associated
14 risks and then manage and mitigate those risks.
15 Depending on the activities and business model of
16 the fintech company, risks presented by fintech are
17 similar to those faced by your banks and others,
18 but there may be heightened risks.
19 For example, if it's a
20 technology-focused service, then obviously cyber
21 issues, IT area, because of the reliance on the
22 technology may be a particular risk to be aware of.

1 Also, some of these firms rely very heavily on
2 sophisticated models, underwriting models, and
3 they so far have been untested under stress
4 conditions, or may, if not properly monitored, pose
5 fair lending risk.
6 Other challenges include
7 disintermediation, or the so-called disruption of
8 traditional banks Rae-Ann mentioned, and perhaps
9 even disruption of their service providers. We
10 added to the list, as a challenge, changes in
11 capital markets processing, given the breadth of
12 those markets and the size and number of the
13 participants that could be affected by wholesale
14 changes there. If you turn to Slide 7, I want to
15 talk a little bit about our ongoing efforts. Jim
16 mentioned that we've recently created a steering
17 committee. This is how we're really addressing
18 following the fintech trends here at the FDIC.
19 We've put together two inter-divisional working
20 groups, split between the wholesale and the retail
21 aspects of fintech.
22 The wholesale focuses on repos,

1 derivatives, clearing, central counterparties and
2 credit. The retail focuses on consumer and small
3 business aspects of fintech. The retail group
4 follows trends in marketplace lending -- Rae-Ann
5 mentioned, we've talked about that -- alternative
6 scoring systems which we are starting to hear more
7 about, mobile and virtual deposit services,
8 account aggregators and person-to-person
9 payments.
10 The wholesale group monitors
11 distributed ledger technology, smart contracts, as
12 well as the development of virtual and alternative
13 currencies. We also have frequent interactions
14 with interested stakeholders. For example, we'll
15 meet with companies that offer fintech products and
16 services, and attend and participate in
17 conferences. Those kinds of meetings are really
18 an important source of information for us, and we
19 learn a lot by those.
20 Our final slide, Slide 8. On an
21 ongoing basis, we have a number of ways we monitor
22 and respond to innovation, starting with the

1 committee here, the community bank advisory
2 committee. We also do a lot of work around
3 increasing access to mainstream financial
4 services.
5 A lot of that has to do with innovation,
6 and particularly technological innovation. For
7 example, we have another advisory committee called
8 the Advisory Committee on Economic Inclusion or
9 ComE-IN, as we call it. We're spending a lot of
10 time exploring the use of technological
11 innovations to bring the un-banked and
12 under-banked into the financial mainstream.
13 This work, right now, is focused on the
14 use of mobile financial technology to achieve this
15 goal. In fact, we had some of our research staff
16 make a presentation to this committee at the last
17 meeting on that work. There's also the Alliance
18 for Economic Inclusion and Bank-On Movement, which
19 are coalitions of financial institutions,
20 community-based organizations, local governments
21 and other partners that are really focusing on,
22 really, a large number of communities around the

1 country. Again, their focus is to get people into
2 mainstream financial services, again, thinking
3 about the use of technology to achieve that goal.
4 Just this May, we issued a request for comment.
5 That's our Financial Institution Letter 32-2016,
6 for those of you keeping score at home.
7 That request is on mobile financial
8 service strategies and how they can be leveraged
9 to improve economic inclusion. In fact, we're
10 looking for bank partners who may want to work with
11 us to demonstrate the effectiveness of mobile
12 financial services in bringing and keeping the
13 underserved in the banking system.
14 Every other year, we do a survey
15 conducted with the U.S. Census to collect data on
16 the number of U.S. households that are un-banked
17 and under-banked, their demographic
18 characteristics, and the reasons that they are
19 un-banked and under-banked. We've learned an
20 awful lot from that study. Each year, we get to
21 change the questions a little bit and get a deeper
22 and more nuanced understanding. That study will

1 be presented to ComeE-IN, the Advisory Committee
2 on Economic Inclusion in October.
3 Finally, we monitor and address issues
4 related to fintech through our regular examination
5 process. That concludes our formal presentation,
6 but we would really be interested in your views on
7 the developments we're seeing in the marketplace
8 and how the FDIC should be focusing its resources
9 as we continue our efforts to monitor and stay on
10 top of this issue.
11 MEMBER SELESKI: Have we thought about
12 looking -- some of these things are very additive
13 to what we do, in terms of banks and services we
14 offer our clients, but there's also a threat from
15 non-banks eating into our traditional profit
16 areas. I'll give you a few examples. Obviously,
17 consumer lending, now, that seems to -- community
18 banks really aren't involved with that anymore.
19 It's pretty much of an online, shop for
20 the best rate, whether it's Quicken Loans -- I
21 heard, for instance, that Quicken Loans, I think,
22 does one out of every four home mortgages online

1 now. Then on top of that, when you look at such
2 things as -- you've got these same-day ACH for a
3 dime. You can do it for ten cents versus sending
4 a wire for $15. Our bank has grown a lot. Our wire
5 volume has stayed consistent. I think it might be
6 useful to see, also, how these non-bank -- or how
7 some of these applications are actually going to
8 hurt the earnings of banks, to some degree. I do
9 think it's going to -- I believe it's probably the
10 biggest threat.
11 We can talk about regulatory and all
12 these other things. I think these non-banks,
13 these fintech-type opportunities are going to be
14 the biggest threat to especially community banks
15 going forward. I think you mentioned it. I'm
16 stealing your thunder. Three years ago, if you
17 said that. I was half asleep up here. I thought,
18 you're crazy, when you were talking about it, but
19 now I agree 100 percent with you.
20 MR. PEARCE: Just one of the things
21 that we have been monitoring and seeing is some of
22 the non-bank fintech companies are really looking

1 for that opportunity where they see there's a
2 particular aspect of a banking process that they
3 can try to disrupt, like remittance or wire
4 transfers is an area where I think some of the
5 non-bank technology companies have really said
6 there's a different way to do that, which really,
7 I think, does pose a risk of putting pressure on
8 revenue at some institutions that are relying on
9 those services.
10 MEMBER BLANKENSHIP: The other thing
11 that we were discussing -- maybe I'll just steal
12 some of your thunder, but we have to really be
13 concerned about where the end liability lies.
14 When you start looking at some of these ways to make
15 these payments -- and I do think that is going
16 forward because just the way you move money around
17 is becoming such a hot technology commodity, but
18 where is the end liability -- you still have to
19 get -- that money has to end up at a bank somewhere.
20 I think we really need to look at are
21 we going to be left holding the bag if there's an
22 issue? You see all this, and my millennials use

1 these payments that I've never heard of. They
2 don't really think about where that track goes, but
3 what if it ends up at our bank and we never even
4 knew -- it's so far removed, we never even knew it,
5 but the end liability comes back to us. That's
6 something that I think we really need to look at,
7 as well. Maybe you need some regulation from CFPB
8 or something. There's got to be a standard.
9 MEMBER SCULLY: I think Rae-Ann did a
10 great job of explaining why this isn't going to go
11 away: because it's relevant. It's relevant to
12 consumers and small businesses. Probably like
13 everybody else at this table, what I worry about
14 is how do we participate in that.
15 I, personally, think we're, in the long
16 run, less threatened by the lending models because
17 I think ultimately, they're all funded by equity
18 right now. You can't run a lending business
19 without leverage. They're going to end up coming
20 back to us, and some of them already are, either
21 by trying to sell us what they've originated, or
22 by borrowing directly from us.

1 But it's the payment systems that I
2 think are the scariest. The consumers are all
3 obsessed with the front-end applications, and why
4 wouldn't they be? They're neat front-end
5 applications. But community banks aren't playing
6 in that space at all. To the extent they have to
7 use the payment system, they're doing it through
8 money center banks. We're getting marginalized on
9 the payment systems. If we get marginalized on the
10 payment systems, then we've been cut out as an
11 intermediary. Again, it's not going to go away.
12 How do we deal with it? One of the things that I
13 would say -- and this is a theme, I think, that we
14 talk about a lot -- one of the reasons why it's
15 difficult for us to participate on the payment
16 system side with the companies that are developing
17 these apps is because our core processors won't
18 give us a window into it.
19 MEMBER HASKIN: One of the areas that
20 we struggle with is online accounting. That's the
21 struggle for banks that are regulated. If there
22 could be some clear definitions on how you can go

1 about those processes within the regulations -- I
2 know there are banks that do that.
3 We've looked at it, and we've looked at
4 it. It's hard for us to make that final decision
5 to do that because we just -- it's hard to analyze
6 the risk in that. I have read that that's one of
7 the ingredients that is holding back the
8 under-served from banking and banks is because
9 they're asked to go in and provide all this
10 documentation to a physical location and sign up
11 for an account. If they were able to do that online
12 and take that friction. You know, it's all about
13 friction in your account. If I have to make
14 someone come into my bank, that's additional
15 friction. If they can go elsewhere, that is where
16 they're going to go. That's one of the great
17 concerns that I have.
18 I think we can all work together and
19 figure out some type of method that's clear
20 because, thumbprints, our customers can sign on
21 online with their thumbprint, so they're online
22 banking at our bank and that's a secure type of

1 innovation. That would be an issue I would ask you
2 to explore because we still feel uncomfortable
3 making that final commitment as a community
4 institution.
5 MEMBER CASTILLO: A couple of
6 observations that I've noted the last couple of
7 months. I think it really has to do more on the
8 lending side. Our little bank has explored how we
9 might be able to take advantage of some of the
10 efficiencies that technology provides.
11 I believe it's a lot easier said than
12 done. I think a statement that Luke made earlier
13 today is something along the lines that examiners
14 are going to evaluate third-party activities as if
15 the financial institution was providing that
16 service directly. We've looked at either
17 partnering with a company or buying stock, or if
18 it allows us to more efficiently and more
19 effectively manage our smaller loan originations.
20 One of the things, in partnering with
21 someone -- there's all sorts of ways that you can
22 partner, but one of the things that really got my

1 board's attention is that, regardless of how those
2 originations happen, if those loans -- if you
3 partner with someone, whether it's On Deck or
4 whoever it is -- that ultimately, if there was a
5 problem, you're the financial institution.
6 You're where the buck stops. I think
7 that's -- trying to manage that liability is going
8 to be a huge, huge challenge. I think, as you go
9 through these steering committees, and as you go
10 through this research, there's two or three
11 questions that come to my mind.
12 At this point, I don't really know how
13 these are solved, but I do think that there's some
14 very distinct differences between having a company
15 help you with process, where you do it all
16 in-house -- and there's a lot of companies out there
17 like that -- between that type of a company and a
18 company where you are read out their model or their
19 black-box technology. You tell them what your
20 credit factors are going to be, and then they crank
21 them through their machine and tell you so-and-so
22 qualifies, so-and-so doesn't. The ones that

1 qualify, you can charge this rate and be within fair
2 lending guidelines. I think there's some huge
3 differences there.
4 The other thing that I'm curious
5 about -- and this is something that we've looked
6 at in passing -- is does it make sense for a
7 community bank like us, a small company, to buy the
8 expertise versus partnering with someone?
9 Because that way, you can control everything that
10 you're doing, but there's some trade-offs there.
11 I think that as you go through this research, those
12 are a couple of things to look at.
13 I think from a risk profile, the other
14 thing that we've determined is that we're bankers,
15 and we have a much different risk profile than
16 someone that has started an online lending
17 company -- I'm just focusing on that for right
18 now -- because they believe we're going to look at
19 these 500 different factors, including Yelp and
20 longevity and all of these different things, and
21 you end up with, potentially, some compliance
22 issues, but you have a risk appetite from a

1 potential partner that potentially is much, much
2 greater than what you, as a financial institution,
3 are willing to take on. Those are all things that
4 need to be evaluated within the decision-making
5 process.
6 MR. PEARCE: Just to follow up on that
7 a little bit, as we've looked at this space, one
8 of the things that strikes me is we've had guidance
9 outstanding on third-party relationship and the
10 management factors there, since 2008. Although
11 the technology is changing and there's lots of
12 things that have been evolving, the principles in
13 this guidance hold up well from, at least, my point
14 of view.
15 Just as you were describing, that
16 culture and the risk-appetite difference in having
17 institutions consider their own risk appetite as
18 they're thinking about what their strategy is going
19 to be to deal with new technologies. Are they
20 going to take a path where you hire internal
21 expertise because you'll have more control and be
22 able to monitor the implementation of that, and

1 then degrees to which you, then, are relying on
2 outside firms. As you said, various and sundry
3 partnership, there's lots of different ways to do
4 that, but just being really intentional about what
5 is your risk appetite, and then doing the due
6 diligence of the firm and the monitoring of the firm
7 and how you structure your contracts to be
8 effective in managing that risk, it's really very
9 consistent with our long-standing approaches.
10 MEMBER CASTILLO: Regarding the
11 third-party risk guidance, we've used that -- we
12 looked at a potential partnership. Our board read
13 that, became familiar with it. We told this
14 potential partner, here is this guidance. If you
15 want to put a proposal together, address these
16 issues here. The guidance really is excellent.
17 This is where my culture comment comes from because
18 when we got a proposal back, it was completely out
19 of touch with what the guidance was suggesting.
20 That's a culture type of thing.
21 CHAIRMAN GRUENBERG: Let me take the
22 opportunity here, if you all don't mind, just to

1 go around the table and ask, I'd be interested if
2 each of you could comment on acknowledging that
3 you've actually committed your institution, and
4 what is the spectrum, what worries you most about
5 risk and issues both the positive and the negative.
6 MEMBER TOLOMER: We have a full array
7 of electronic services, so online banking,
8 business online banking, consumer online banking,
9 mobile. The key for us is we're offering pretty
10 much what all the banks are offering, large and
11 small, to small and medium-sized businesses and the
12 consumer.
13 We think we have a good product, and
14 we're not concerned about that aspect. We also do
15 the deposit and the like. I'm not at all concerned
16 about the third-party lending. We talked about
17 that, I think, two or three meetings ago. Some
18 people were a little concerned about it.
19 You can see what's happened to Lending
20 Club and management changes. I'll venture a guess
21 that everybody here has been offered a portfolio
22 to purchase or the loans that they've generated.

1 I'm sure we've all said no. So I'm not too worried
2 about them. In terms of the payment systems, I
3 think it's something you're going to have to look
4 at. My sense is you'll get the more that happens,
5 there'll be more regulatory oversight because it
6 does affect -- I think Cynthia's right. It affects
7 the banking system. I think from that standpoint,
8 you've got to stick to your bank model and continue
9 doing what you're doing and recognize that there's
10 plenty of competition every which way, whether it's
11 a traditional bank or it's one of these fintechs.
12 We'll have to see how it plays out, but
13 I'm not too -- we watch it. We'll obviously have
14 some level of concern, but I think we spend more
15 time executing what we're supposed to be doing.
16 MEMBER SCULLY: I said just a few
17 minutes ago, it's the payment system front end that
18 worries me the most from a competitive standpoint.
19 In terms of what we're doing now, we're
20 participating on two fronts, one through our core
21 processor, which is the consumer-to-consumer
22 payments that can be made directly, so the standard

1 application, you can pick up with some of the core
2 processors, but it lets them directly pay a
3 consumer with an online application, and we're
4 buying leads for one of our consumer businesses,
5 but there's no requirement that we do anything with
6 the leads. It's more of a marketing lead, so we're
7 not obligated. We've rejected anybody that's
8 offered to actually sell us portfolio loans to put
9 in block portfolios. If we can't originate them,
10 we won’t do that. The two things that we're
11 investigating are online accounting. I think,
12 like Jane, we feel like we should be able to do this,
13 but every time we look at the rules, we say that
14 we can't do this.
15 Those of us that have legalized
16 marijuana in our states, it's exactly the same
17 argument. You look at it and you inevitably
18 conclude, I can't do this, but others are doing it.
19 Then we're looking at some of the fintech
20 applications to help us originate, on the small
21 business side, and to link things to sales
22 management systems.

1 I think from an internal processing
2 standpoint, we're very excited, see it as a
3 win-win. In other areas, we're feeling
4 threatened, in terms of can we compete with those
5 who are starting to do this? But we actually have
6 a permanent task force, obviously part time, of
7 four officers in our company, all millennials from
8 different disciplines, who are supposed to look at
9 all of this and try to raise the flag for us.
10 MEMBER LUNDY: I don't have a lot to add
11 to that. Probably the most effective tool that we
12 use in our model is we brought deposit capture when
13 we changed vendors about two years ago to upgrade
14 that. We are going through a core process of
15 conversion now. That process, which we decided on
16 about a year ago, has delayed -- we're one of,
17 probably, the largest banks -- and we also offer
18 mobile applications.
19 With our business orientation, it just
20 hasn't been -- it's a nice to have. We feel like
21 we kind of need it just to say that we're a real
22 bank, but the reality is most of our customers are

1 business people who don't really need to do
2 business on their phone, but we will have that. To
3 the risk point that we worry about, we have
4 strategically gone after a number of large deposit
5 pools of various kinds.
6 We call them channels. Some we've
7 researched and successfully implemented, some
8 we've gotten into the business and then abandoned
9 it. But we're constantly looking at niches that
10 we can basically attract deposit pools.
11 Particularly in the current rate environment,
12 large money center banks are awash in deposits and
13 may not want them, so depositors can look for a
14 regional bank like ours. It's big enough to
15 provide the services, and yet, we're a rapidly
16 growing loan portfolio, so we need the deposits.
17 We spend an awful lot of time trying to
18 evaluate the BSA and the compliance risks and make
19 sure that we don't get into some kind of inadvertent
20 trouble for ourselves, for our depositors, from the
21 regulators. I would say, in our particular
22 institution, that's where we spend a lot of time.

1 We identify these large deposit pools, and we
2 figure out is it really too good to be true, or can
3 we bring these in and handle the risk elements of
4 them?
5 MEMBER CASTILLO: I think that as far
6 as technology, even for a small company, we have
7 most, if not all of these services available.
8 That's one thing that's been a huge benefit over
9 the last ten years is that, regardless if you're
10 a core processor, if the cost equation has changed
11 so significantly that all of these things are
12 available to us fairly quickly. On the concern
13 side -- and listening to these young folks speak
14 earlier today -- by the way, that was fascinating,
15 some of their comments that they made -- I think
16 the biggest challenge for us on the technology
17 side, whether it's on the loan side or the deposit
18 side, is trying to eliminate some of the friction
19 points that Jane spoke about.
20 Because I think for us, it's still a
21 very clunky experience for somebody that loves our
22 bank, they have my cell phone, they can call me

1 Sunday anytime. But still, I can make them feel
2 better, but my website or my application doesn't
3 necessarily have all of those things available to
4 them. One of them may be as simple as -- we have
5 a PDF application for a loan on our website.
6 It's not interactive. They can't
7 automatically send it to us. So the biggest
8 challenge that we have is really making that
9 experience online close to as good as it is when
10 they talk to the person. Because there is that
11 expectation that I can get on there 11:00 Friday
12 night, and I can do all of this.
13 MEMBER WILLIAMS: Again, same
14 situation with us. You pretty much have to have
15 everything on the depository side, unless you're
16 in the most remote of areas. We have had
17 situations -- we only recently did, for example,
18 instant issue debit cards. We've had customers
19 walk out of the bank because they couldn't walk out
20 with a debit card prior. You've got to have those
21 things. P2P is going to get bigger. Venmo, I hear
22 about it all the time.

1 My daughters Venmo back and forth. We
2 have systems in place, but you've got to get bank
3 information, and you've got to send an email. This
4 is immediate. Now, Venmo requires that they both
5 be signed up with Venmo. How can my customer get
6 money that quickly to someone who's not a customer
7 of the bank? Those are the hurdles that we're
8 trying to get by on that.
9 On the deposit side, we've got the
10 technology. It's there. We can be competitive.
11 I don't think that's going to be an issue. I do
12 fear a little bit, though, on the online lending
13 side, for some of the reasons that Leo was just
14 talking about here. It's just these little
15 breaches of the front gate, these little pecks.
16 Because so much of what we do relies on the
17 relationships that we've established with our
18 customers. When we initially had conversations at
19 the national association/state association
20 levels, FDIC level about these lenders, the
21 old-line banker response was these guys are going
22 after loans we don't want. They're making $50,000

1 unsecured loans with very little information.
2 They're charging really, really high rates, big
3 default rates.
4 Those are not the loans we want anyway.
5 I fear that these guys are going to get better and
6 better at it. There's issues with the model.
7 Obviously, we've seen it. But I think they'll
8 continue to. At the point, for my good customer,
9 that a $10,000 unsecured loan gets to 21/2 percent
10 online, and he says, Derek, I can't pay you 5; I'm
11 sorry. I'm just not going be able to. I love you
12 to death, but -- that's when they begin to breach
13 the gate a little bit. That concerns me, that
14 they're going to get better at what they do. The
15 models are going to improve, and we're going to lose
16 some business on that end. That's the concern.
17 (Off microphone comment.)
18 MEMBER WILLIAMS: Well, I suppose we
19 could. The problem is overall, and they're using
20 equity. It's the age-old problem of our situation
21 versus some of the big banks. It's a cost of funds
22 issue in the long run, the ability to have the

1 access -- when we're using local deposits, we've
2 got a pretty fixed cost of funds. We don't have
3 the access to some of the markets that the big guys
4 have.
5 That's what concerns me is they're
6 going find pools of money that are willing to take
7 much less return on their money, pools of equity
8 money, and cause us some problems. I think we may
9 have that ability, but I'm worried about, from a
10 technology standpoint, whether we'll take
11 advantage of it or not.
12 MEMBER HASKIN: Several years ago, we
13 made a decision that there were too many things that
14 we wanted to keep in mind when we did our technology
15 framework. One is mobile, and the other is
16 real-time payments. Every decision that we make,
17 we try to keep those two in the forefront of our
18 decision-making process. We have a wide array now
19 looking at the P2P. We've got all these new
20 deposit transfer options. Many of the things that
21 we're finding is that these are basically
22 commodities. They're very difficult to charge

1 for, so you have to save your money on the back side,
2 and then personnel expenses and things off to
3 really see the benefits of this. Our bank, when
4 it was half the size it is now, had over 100
5 employees. Twice the size, and we have 37
6 full-time employees. That just shows the impact
7 of technology in banking.
8 We're struggling with some of these
9 friction points, but we're only as good as our core
10 processor and their technology. Because what's
11 happening, especially in the real-time space, is
12 these -- when we had ATMs, we'd go out and find the
13 best vendor to deliver the ATM service. Now, to
14 get that real-time, that immediate transaction,
15 you basically have to rely on your core processor
16 and follow all of their products.
17 That's a process because you have these
18 four and five-year contracts that you've signed up
19 for. You have to really plan ahead four and five
20 years into the future to know exactly how we're
21 going to get to the end goal. That's been a
22 challenge for us, but we've done a pretty good job

1 focusing on that and getting to those products. I
2 still don't feel my experiences has a lot of the
3 online competitors, the depository banks, but
4 we're working on that. I think real time is going
5 to be important to millennials. I think that
6 everything is real time for them, and I think
7 they're going to expect a lot of their banking.
8 Right now, our P2P is the next day. It's not same
9 day.
10 We have a lot of community banks that
11 don't want to settle more than one time a day, so
12 you're going to have to figure out some way to push
13 those credit transactions through, so that they can
14 do one-time settle. It's an interesting
15 environment. We feel good about where we are.
16 We'd like to do the online deposit opening, but we
17 have to figure out how to get there.
18 MEMBER WILLIAMS: I agree with pretty
19 much everything you were saying. I think one of
20 our bigger concerns was just a general lessening
21 of the amount of non-interest income you could get.
22 We were secondary market in mortgage loans, for

1 instance. People are going online to get those.
2 Cash management, you mentioned wires earlier.
3 About a year ago, senior management and our board
4 sat down. We took a different tack. We all follow
5 the same products, and we all have the same major
6 core processors and everything. We actually got
7 into a new line of business, figuring that we needed
8 that line of business to offset the revenue loss
9 that we're going to have in the future. We got into
10 credit cards. Nine months, we decided to become
11 a credit card issuer.
12 Benefits of that, obviously, with
13 Dodd-Frank, is we get the full interchange, versus
14 the larger banks. On top of that, you have a
15 MasterCard or a Visa that is basically updating
16 their technology and carrying you along with them,
17 so you're not actually having to go out
18 there -- it's a canned product. You don't have to
19 go out there and do it.
20 It fit very well with our commercial
21 strategy, in terms of cash management for our
22 corporate customers. So we kind of took a little

1 bit different tack, in terms of not trying to fight
2 the battle of staying ahead of it, but just trying
3 to find another source of revenue, and that was the
4 credit card side.
5 MEMBER BRYANT: Our situation is
6 completely different, in that we don't offer
7 transaction accounts. We have, in the last couple
8 years, started offering online banking. We have
9 also looked at acquiring institutions that will
10 give us access to transaction accounts. But one
11 of the things this meeting has confirmed for me is
12 that I'll probably attend a technology conference
13 to explore ways that we can grow our institution,
14 by looking at non-traditional sources for
15 financial institutions.
16 MEMBER BLANKENSHIP: Well, in our
17 bank, we offer just most of the services that are
18 readily available, but we're in a metropolitan
19 area. To stay competitive, we're more or less
20 forced to do that. We have found that there's not
21 any one sector that's more accepting of new
22 technology. Where you would think maybe the Baby

1 Boomers or some of the older generation would be
2 more hesitant to use those products, we really
3 found that they embrace that.
4 The P2P, I think, is still based largely
5 on a next-day ACH transaction, but there, again,
6 it goes between two banks, so if something goes
7 wrong, what's going to happen there, when you have
8 no control over who's initiating that? That
9 remains a concern. I think generally, with
10 technology, the biggest question is just risk
11 versus reward. Where is our risk tolerance, and
12 how much of that are we going to be forced into
13 taking to stay relevant in the market? Then you
14 have to decide if you want to stay relevant,
15 particularly in the payments area.
16 I do think relief for online opening of
17 accounts -- and I understand that there's just
18 inherent risk in not seeing that customer face to
19 face, but maybe there could be other criteria that
20 you could get around that.
21 Because my millennials, my daughters,
22 I think that's what that generation and, I think,

1 honestly, our generation will come to expect
2 because it's all about accessibility and
3 convenience.
4 If you can't deliver that, whether it's
5 in person, because you're always available and you
6 always answer the phone, or if someone can't open
7 an account, or at least apply for a loan over the
8 weekend, when they found a new travel trailer or
9 something, people, they expect it now. They
10 expect an answer now. They think that we have the
11 technology to look at them and say, yes, you've got
12 a great credit score. There are technologies out
13 there for community banks. Sometimes the cost is
14 the inhibitor. That would be an issue. One of the
15 other things that I think, as we talk about
16 technology, is we're really looking hard at social
17 media and the roles on social media and what impact
18 that will have on payment systems and deliveries.
19 How is that promoting customers away from us, or
20 can we use that to our benefit?
21 That's something that's going to fall
22 largely under consumer compliance. Look at what

1 a gigantic role Facebook and Twitter -- somebody
2 tweets out, there's a better way to make your
3 payment. We're at a competitive disadvantage.
4 That's real, at least in my mind.
5 MEMBER SCULLY: Or if we do try to put
6 it out there, it can't be done in a tweet because
7 we have to do so much disclosure around the product
8 every time we talk about it.
9 MEMBER BLANKENSHIP: Yes. Other than
10 that we offer --
11 MEMBER SCULLY: It's true. We tried
12 to do it, and you have a heart attack. We can't
13 do that.
14 MEMBER BLANKENSHIP: That is true.
15 We're a major sponsor of two festivals in our
16 community. I meet with the CVB board. Every time
17 they put our logo up -- now they tease me. I mean,
18 that's an educational process for that.
19 MEMBER THOMPSON: The thing about
20 being the last is it's hard to sound a whole lot
21 different. At our size bank, we offer -- at 125
22 million, we pretty much offer all the same products

1 as everybody else does, just like everybody said.
2 You have to, if you want to keep the doors open.
3 The big challenge for us is are we -- we
4 put in a lot of new technology in the last year,
5 year and a half. Part of the thing for us, are we
6 monitoring enough? Are we monitoring all the
7 right things? You want to continue to add the
8 technology, but then you have to do all those things
9 behind the scenes.
10 Jane, you can cut down on those
11 employees, but you've still got to monitor and
12 measure whatever it is that you're putting out
13 there, not just for regulatory purpose, for our own
14 purpose. Did you spend the money on the right
15 things? Are you getting any return? The board
16 wants to know every time you put in a new product
17 what's it doing for you? I think for us, at our
18 size and number of employees, it's trying to keep
19 up, but also trying to be sure that you're
20 monitoring everything that you've got out there in
21 the right way.
22 MEMBER EMMONS: Could you repeat the

1 question, please? I would echo a lot of what has
2 been said. I don't know that there's any
3 technology that we've actually developed, you
4 know, it's -- we are so dependent on our core
5 provider and vendors.
6 To me, we've spent a lot of time talking
7 about the person to person, kind of that retail side
8 of the business, which -- we've been listening to
9 the folks earlier, the young folks earlier today
10 -- really kind of starts with the definition of
11 commoditization that's taking place.
12 I think to our world, commoditization
13 is not a pleasant thought. I think what's
14 particularly concerning about it for us is the pace
15 of change and the fact that it's coming so quickly
16 that it constantly feels like we're addressing
17 another payment system, another model that's in the
18 market that our customers, our consumers are
19 interested in, and that obligation of feeling like
20 you have to get it. You've got to provide it. And
21 so there are all of these options. We're early
22 adopters, but at some point, there's just going to

1 be a plethora of payments that are in that P2P
2 space, and that concerns me a lot.
3 The kind of a holdout, I think, in this
4 conversation, is really the business to business
5 or the commercial side of our business, where our
6 deposits have not -- we're not seeing the kind of
7 changes that we're seeing on the retail side.
8 Cash management systems and the way
9 that we deliver services and the treasury functions
10 with the businesses still can be customized, still
11 can be priced, and still makes a difference. You
12 can build relationships on that side of the
13 business.
14 I think our sitting here today and
15 saying what would be the greatest risk is that a
16 similar kind of wave of technology passes through
17 the business to business side of payments, and it
18 becomes very similar to what we're experiencing on
19 the retail side. All of those deposits, all of
20 those transactions bypass the banking system, and
21 we're left with a real strategic challenge. I
22 think in the current environment, I think our job

1 is to make sure that we're on top of all of the
2 changes that are coming and prepare ourselves to
3 be able to afford that technology and work.
4 MEMBER WILLIAMS: Chris, you make a
5 valid point. That whole idea of there's so much
6 stuff coming, and you don't want to miss the one
7 that is going to be the death knell to the banking
8 industry. You're afraid that that one will slip
9 by, so you're looking at so many of which will be
10 gone in six months as a fad. It's hard to keep up
11 with it all.
12 CHAIRMAN GRUENBERG: Thank you. I
13 noticed our staff feverishly taking notes through
14 all of this process. I think this has been -- Ms.
15 Eberley.
16 MS. EBERLEY: It's very helpful, thank
17 you. I think you've given us some things to work
18 on and some things to think about and see if we can't
19 maybe deliver on some of the things you've asked
20 for.
21 MS. RYAN: Okay, well thanks, Doreen,
22 Jim, Rae-Ann, Jonathan, and Mark. We're going to

1 move into our last panel right now. Doreen and
2 Rae-Ann are going to stay with us, and we're going
3 to be joined by Mark Moylan, Deputy Director of our
4 Division of Risk Management Supervision, and Bob
5 Storch, who you saw earlier, as well. The focus
6 is going to be on recent supervisory developments,
7 including a new work program for examiners called
8 InTREx, and FASB's new CECL accounting standard.
9 I'll let the group here explain those acronyms.
10 I'll turn it over now, again, to Doreen.
11 MS. EBERLEY: Okay. I think, again,
12 we'll just kind of go down the line. We're going
13 to talk about the new IT examination program,
14 broker deposit FAQs, and our -- an incentive comp,
15 and our guidance on the private sector loss model.
16 MR. MOYLAN: Good afternoon. I'd like
17 to speak to you today about InTREx. I've kind of
18 hinted around of what we've been doing with InTREx
19 and really, the revisions to our prior examination
20 program. Really, InTREx -- or the Information
21 Technology Risk Examination Program -- is really
22 an enhancement of our IT examination work program

1 that we've historically worked through. The
2 regulatory requirements surrounding a bank
3 establishing an appropriate information security
4 program is really nothing new. However, the
5 parameters set forth really have lacked the
6 recognition of cybersecurity, cyber risk.
7 Certainly, our enhancement was in recognition of
8 that new risk component.
9 InTREx now specifically recognizes the
10 emergence of the cyber risk element and better
11 aligns and defines regulatory expectations in the
12 assessment of a bank's information security
13 program and the identification and mitigation of
14 this new risk.
15 Really, InTREx introduces three areas
16 of change, pre-examination procedures, changes to
17 the format and structure of the examination work
18 program, and new examination findings procedures.
19 All of these changes are made to affect better risk
20 scoping, enhance the examination process, and
21 increase transparency, as well as board awareness.
22 Let's talk a little bit about the

1 pre-exam procedural changes. If you remember, we
2 had the IT questionnaire. It's been replaced by
3 what we call the IT profile document. The IT
4 profile document has 65 percent fewer questions for
5 bank officials to answer -- so I'm sure you applaud
6 that -- is better focused, in my opinion, and bank
7 officials will now receive the document and have
8 approximately two weeks to complete and submit to
9 the FDIC. It's going to allow you time to talk to
10 your staff and not have to do it so quickly. I
11 think the thoughtful preparation is a benefit to
12 us all.
13 The two-week preparation time, along
14 with more effective questions, will provide the
15 examiners with better information to risk focus the
16 examination and appropriately staff the
17 examination commensurate with the risk profile of
18 the institution. I want to talk a little bit about
19 the actual work program, itself. In your package,
20 you're going to have one of our modules, which is
21 the audit module.
22 This is the actual work program that we

1 have developed, and it is really the framework
2 which the examiners will go through. The work
3 program modules now directly correspond to each of
4 the uniform rating systems for information
5 technology, or as we call it, URSIT ratings. If
6 you look at the audit modules, the work program
7 provides examination staff with specific decision
8 factors and analysis procedures, including basic
9 and expanded procedures. It also creates an
10 opportunity for those that may have a more complex
11 environment to incorporate the FFIEC handbook work
12 programs. Our examiners now, for our smaller
13 institutions, will use this program, and this will
14 be the framework for all of it, but if we do have
15 some areas that are more complex, then they will
16 scope in and use the entire FFIEC handbook work
17 programs, take those findings, and then flow them
18 up consistently with the URSIT ratings.
19 As you will note in the program, it also
20 highlights the various components and direct
21 relationships within a bank's information security
22 program that relate to cybersecurity, as well as

1 the information security standard, pursuant to the
2 Gramm-Leach-Bliley Act. If you turn to page 5 of
3 the audit program, you will see a private approach.
4 As you can see there on the left, you
5 will see, in this case, a cyber flag. That element
6 relates to cyber. Again, understanding that
7 cyber's really through all of these components,
8 this highlights for our exam staff that this is one
9 of the main elements associated with cyber. I
10 didn't give you a module that had
11 Gramm-Leach-Bliley, but you will see a similar flag
12 for Gramm-Leach-Bliley. Those specific elements
13 and decision factors that they're looking at as it
14 corresponds -- even though we're looking at your
15 entire information security program, these are
16 elements that are particularly specific to cyber
17 in the Gramm-Leach-Bliley Act.
18 We believe this new program will
19 provide better examiner guidance, a more
20 consistent examination approach, and better
21 support of the conclusions drawn. If you also
22 notice, on the first page of the audit -- and this

1 is something that has been something we've been
2 really working on, and we will continue to work on
3 as we move forward -- on the decision factors, you
4 will see, at the bottom, a category from strong to
5 critically deficient.
6 As the examiners draw their conclusions
7 in those areas, in the work programs, what this is
8 going to allow us to do is to perform horizontal
9 analysis. We will be able to take all of these work
10 papers of all the examinations that are conducted
11 around the country and then be able to sort and pull
12 together maybe areas that we're seeing a higher
13 level of less than satisfactory, satisfactory, see
14 the specific comments, and then draw some
15 conclusions on areas that will give us an
16 opportunity for better training, maybe more
17 guidance, and have that horizontal capacity.
18 Every one of these that's performed at all of your
19 institutions, they will be checking these boxes.
20 At some point in time, we will start
21 drawing that information out, so again, more of a
22 horizontal perspective and analysis on that. One

1 of the things I do want to mention, I think, again,
2 with support from Doreen, is that if you go to the
3 financial institution that was issued, these
4 components and these modules for audit management,
5 all of the URSIT ratings, as well as the IT profile
6 program, are now available to the banks.
7 They are available by clicking the link
8 in the financial institution, so your staff and
9 yourselves have these modules available. You'll
10 be able to preview them, understand some of the
11 elements we're looking at, again, the cyber flags,
12 the Gramm-Leach-Bliley flags. These are all
13 available to all of you through our fdic.gov
14 website. That's, I think, something, again, on
15 the form of transparency. This is what the
16 examination staff is looking for, and this is
17 available to you folks. Lastly, which certainly
18 we've been a strong advocate for, we worked with
19 the Federal Reserve, and also CSBS, on this
20 program.
21 They were partnering in this program.
22 One of the things was we wanted to move, also, in

1 the transparency, to now disclosing the entire
2 URSIT rating. Historically, we've only been
3 disclosing IT composite rating. We will now be
4 disclosing all of the components. I know all of
5 the bankers I have ever -- they know what No. 1
6 means; they know what No. 5, they know what No. 3
7 means.
8 Certainly, I think it will create much
9 better of a discussion. You may have been a
10 composite 2 in the past. In fact, you may have had
11 recommendations regarding audits. But now, if you
12 know we have rated the audit a 3, that will probably
13 perk up everybody's ears. I think that will allow
14 the board to understand, ask more questions, be
15 attuned to those recommendations, so all of the
16 composite and component ratings will now be
17 disclosed in the examination reports. The ECC
18 page will still give a summary comment regarding
19 the IT overall examination findings. It will
20 disclose the comment pages. But there will now
21 be -- what used to be an optional page, called our
22 information technology assessment page, is now

1 mandatory.
2 On that page will be a discussion of
3 each of those components and the rating. Also on
4 that page will be a summary comment on your
5 cybersecurity preparedness. It's basically
6 taking those components, with those flags, and
7 bringing them into a context specifically rated to
8 cybersecurity, very similar to what we've done
9 historically in the reports regarding
10 Gramm-Leach-Bliley.
11 Now, you will have the transparency of
12 not only seeing the components, you will have an
13 examiner opinion of your cyber preparedness.
14 Obviously, if there's elements in recommendations,
15 you will see that in the context of your cyber
16 preparedness, just as you've seen on your
17 Gramm-Leach-Bliley. Really, our goal is, again,
18 to not only give our staff a better program
19 recognition of the emerging risk of cybersecurity,
20 increased transparency through the component
21 ratings, hold better discussions with management
22 and the board regarding all of these areas, and

1 certainly, last, but not least, I think this is a
2 major benefit that these work programs are now
3 available to you folks on our webpage, to where you
4 can understand the thought process, the areas that
5 are available, and what the examiners will be
6 looking at through this process. Any questions?
7 A memo went out June 30th. There'll be
8 some pre-exam time, so no later than -- you should
9 start seeing the use of the new program no later
10 than October. If you have an examination
11 scheduled, 1st of October. There may be some
12 that'll be done a little bit earlier if the bank
13 is open to it and we're able to pre-plan.
14 You may or may not be getting the full
15 package, but I certainly would be very interested
16 in how you feel that exam goes.
17 MS. MILLER: Also on June 30th, my
18 group issued an FIL on an updated set of broker
19 deposit frequently asked questions. We call them
20 FAQs. We originally issued the broker deposit
21 FAQs in January of 2015. We did that basically to
22 provide plain language information about

1 categorizing broker deposits all in one place.
2 We talked in that FIL back in January
3 of 2015 that we would update it periodically.
4 Section 29 of the FDI Act and Part 337 of our rules
5 and regulations define the term deposit broker.
6 It restricts the acceptance of broker deposits by
7 insured institutions that are not well
8 capitalized.
9 The FAQs are based on the statute and
10 on a regulation, but also on explanations of the
11 requirements that we have provided to the industry
12 through what we call our advisory opinions from
13 time to time. We also published a study on core
14 deposits and broker deposits back in 2011, as part
15 of the Dodd-Frank Act. There's a lot of
16 information in there about categorizing deposits.
17 After that initial release in January of 2015, we
18 conducted a banker call-in. We had visits with a
19 number of trade associations and other
20 institutions. In the spirit of updating them
21 periodically, we issued a revised set of FAQs in
22 November. We addressed many of the points that

1 people came in and chatted with us about in those
2 outreach sessions.
3 We got nine comments on that November
4 release and updated the FAQs accordingly, where
5 appropriate. The updates since January, we have
6 new questions on government pre-paid cards. We've
7 got new questions on deposits gathered through dual
8 homed and call center employees, and then we
9 clarified a number of other questions. We also
10 added footnote citations to those advisory
11 opinions, where appropriate.
12 I think that was a real helpful additive
13 when we went out for comment in November. We also
14 emphasized that the FDIC takes a case-by-case
15 approach. A lot of these products are very
16 idiosyncratic. You could change one little
17 factor, and it would change the determination, so
18 we want to make that clear. In that regard, we
19 continue to get inquiries. I'm working on several
20 right now. As we get through those, we'll update
21 our advisory opinions. Then once we get enough of
22 those, our intention is to update the FAQs, as well.

1 MS. EBERLEY: Maybe just one point.
2 The footnotes that we added throughout point
3 directly to existing advisory opinions that are
4 outstanding that relate to issues, so you can see
5 how the question relates to something that's
6 already been evaluated or to the broker deposit
7 study.
8 MS. MILLER: Then with regard to
9 incentive compensation, we issued an NPR, notice
10 of proposed rulemaking, on April 26th, regarding
11 incentive compensation. This is per Section 956
12 of the Dodd-Frank Act.
13 That section requires six
14 agencies -- us, the OCC, the Fed, the NCUA, the SEC,
15 and the FHFA -- to jointly prescribe either
16 guidance or rules that prohibit any type of
17 incentive-based compensation arrangements or any
18 feature of those arrangements of the agencies
19 determined to encourage inappropriate risks by a
20 covered financial institution. 956 also requires
21 that financial institutions disclose to the
22 appropriate federal regulator the structure of

1 incentive-based compensation arrangements
2 sufficient to determine whether that structure
3 provides excessive compensation that could lead to
4 material loss to the institution.
5 956 applies to incentive-based
6 compensation arrangements offered by what's called
7 covered financial institutions, and that's insured
8 depository institutions, depository institution
9 holding companies, credit unions, broker dealers,
10 investment advisors, Fannie Mae, Freddie Mac, and
11 other institutions that the agencies jointly
12 determine should be covered by the rule.
13 Within those covered companies, those
14 over $1 billion are covered. Any of you that are
15 under that, institutions that are less than $1
16 billion, are exempt from the rule. The NPR uses
17 a tiered approach with respect to its requirements,
18 so there's a Level 1, and that goes from 1 to 50.
19 I assume you would all be in the
20 Level -- excuse me, Level 1 are $250 billion or
21 more; Level 2 is $50 to $250, and Level 3 is $1 to
22 $50 billion. That's where I assume you guys are.

1 All covered institutions would be subject to a set
2 of basically programmatic elements, policies,
3 procedures, and recordkeeping type of
4 requirements. Then as the institutions get
5 larger, it would be subject to more stringent
6 provisions.
7 Importantly, for those larger
8 institutions, the Category 1s and 2s, the proposal
9 would require minimal deferral amounts and time
10 periods for incentive-based compensation for the
11 senior executive officers and those employees that
12 could expose the institution to material levels of
13 risks.
14 In the proposal, we call them
15 significant risk takers. The proposal requires
16 those amounts to be subject to forfeiture and
17 downward adjustment in the event of certain things
18 that would happen. The proposal also has other
19 prohibitions for those larger institutions.
20 Those include prohibitions on
21 purchasing personal hedging instruments, clawback
22 provisions for already vested amounts, and there

1 are also requirements on enhanced governance, risk
2 management, and recordkeeping for those larger
3 institutions. Any questions on my two items?
4 MEMBER SCULLY: I have one question.
5 I obviously only looked at it so long. This is on
6 the incentive-based --
7 (Simultaneous speaking.)
8 MS. MILLER: You didn't read the whole
9 thing, the 600 pages?
10 MEMBER SCULLY: No; I'm sorry; I
11 didn't. Is there a way to more -- I think almost
12 everybody in this room, at best, is going to be a
13 Level 3, maybe not even a Level 3. Much of the
14 documentation seems to refer to Level 1 and Level
15 2. I understand that because of the concern. Is
16 there a way to just restructure it in a way that
17 it's easier for those of us that are Level 3 to find
18 what applies to us, as opposed to what doesn't apply
19 to us? I understand why all the emphasis on 1 and
20 2, but my first attempt to read, I could hardly find
21 references to Level 3.
22 MS. MILLER: Yes, we will certainly

1 take that into consideration. The early comments
2 are this is an extremely complicated --
3 (Simultaneous speaking.)
4 MEMBER SCULLY: -- more prescriptive
5 than it's been in the past.
6 MS. MILLER: It's open for comment.
7 We're taking all comments, that's for sure. When
8 you move to a final rule, your comments are very
9 helpful. We try, when we issue financial
10 institution letters and press releases and things,
11 to communicate what's important, especially for
12 community bankers, so certainly, we'll do,
13 hopefully, a better job of pulling that out and
14 communicating that.
15 (Simultaneous speaking.)
16 MEMBER SELESKI: I think it would be
17 difficult to -- this is like War and Peace -- to --
18 MS. MILLER: It's better, though.
19 (Laughter.)
20 MEMBER SELESKI: Everyone wants to
21 comply with the rules and regs. I think we need
22 our five millennials here to interpret this. I

1 think for the examiners coming in, I just think
2 everyone needs to be on the same page. Because we
3 all want to comply, but I almost have to hire a
4 consultant to look at all the compensation plans
5 of the people that would be involved to make sure
6 they comply because you don't want to be written
7 up. The board's going to be looking at this and
8 saying, "Why?" I agree. It needs to be
9 simplified, a chart, examples, and that type of
10 thing --
11 (Simultaneous speaking.)
12 MEMBER SCULLY: There's a reference
13 somewhere in here, I saw, to the Level 3 -- the basic
14 blah, blah, blah applies.
15 MS. MILLER: Programmatically, yes.
16 MEMBER SCULLY: I couldn't find -- I'm
17 sure it's in here, but I couldn't find what is the
18 basic?
19 MS. MILLER: That's really helpful.
20 MEMBER SCULLY: I don't think
21 anybody's trying to be lazy or critical because I
22 understand the need to focus on those 1s and 2s,

1 but it's going to be really tough to get through
2 this. As David said, your boards and your comp
3 committees are going to be all over this.
4 MS. MILLER: Yes. Certain things
5 we've done with other rules are user guides. This,
6 of course, is still in the comment phase, but videos
7 and training and things like that. We can
8 certainly consider those issues.
9 MR. STORCH: Shall we move on? Good
10 afternoon. You have to suffer through me a second
11 time today, but we'll see which topic is
12 preferable. A little more than one month ago, on
13 June 16th, the Financial Accounting Standards
14 Board -- I'm sure you know the acronym FASB.
15 Anyway, the FASB issued what's known in
16 accounting parlance as Accounting Standards
17 Update, or ASU 2016-13, on the measurement of
18 credit losses on financial instruments. The new
19 standard was the culmination of several years' work
20 by the FASB to improve the accounting for credit
21 losses.
22 The ASU formally introduces what has

1 come to become known as the current expected credit
2 losses, or CECL methodology for estimating
3 allowances for credit losses. This will replace
4 today's incurred loss methodology when the new
5 standard takes effect. The move to the CECL
6 methodology represents a significant change to
7 current allowance practices both for the agencies
8 and for your institutions and the industry, as a
9 whole. The new standard can be downloaded from the
10 FASB's website if you do want -- members of your
11 staff need to obtain a copy. On June 17th, the day
12 after the release of the new accounting standard,
13 the FDIC and the other federal financial
14 institution regulatory agencies issued a joint
15 statement on FASB's new credit losses standard to
16 provide initial information directly to all
17 institutions about the new standard, including
18 initial supervisory views regarding the
19 implementation of the CECL methodology by
20 financial institutions, and a copy of the joint
21 statement is attached to the FDIC's Financial
22 Institution Letter 39-2016 in your handout

1 materials.
2 In its simplest terms, the allowance
3 for credit losses under CECL is a valuation account
4 measured as the difference between the amortized
5 cost basis of financial assets and the net amount
6 you actually expect to collect on those assets.
7 In other words, the allowance is an
8 estimate of lifetime credit losses for however long
9 those assets will remain on your balance sheet.
10 The CECL methodology applies to all financial
11 assets carried at amortized cost, including loans
12 or investment, your traditional loan portfolio,
13 and to your held in maturity securities, as well
14 as off balance sheet exposure, such as loan
15 commitments and standby letters of credit. The
16 new standard also updates the measurement of credit
17 losses for available for sale debt securities.
18 To estimate expected credit losses
19 under the CECL methodology, institutions will use
20 a broader range of data than other existing
21 generally accepted accounting principles, or GAAP
22 accounting. These data include information about

1 past events, current conditions, and reasonable
2 and supportable forecasts relevant to assessing
3 collectability of cash flows on financial assets.
4 In contrast, under today's incurred
5 loss methodology, only past events and current
6 conditions can be considered when estimating
7 credit losses. What are differences between
8 today's incurred loss methodology and the CECL
9 methodology, the FASB strived to ensure that the
10 new accounting standard will be scalable to
11 institutions of all sizes, and the agencies expect
12 that to be the case. We also do not expect smaller
13 and less complex institutions will need to
14 implement costly and complex modeling techniques.
15 Institutions should be able to modify their
16 existing allowance methodologies to meet the newer
17 accounting standards. In so doing, institutions
18 will, however, need to change certain of the inputs
19 and assumptions they use to achieve an estimate of
20 lifetime credit losses.
21 Acceptable estimation methods under
22 the CECL methodology that are identified in the

1 standard include loss rate methods, world rate and
2 migration methods, discounting cash flows,
3 probability of default and loss given default
4 methods. The new standard explicitly states that
5 institutions are not required to use a discounted
6 cash flow methodology to estimate expected credit
7 losses.
8 Because the ASU doesn't specify a
9 single method for measuring expected credit
10 losses, the standard allows institutions to use
11 judgment to determine the relevant information and
12 estimation methods that are appropriate in their
13 individual circumstances. In addition, an
14 institution may apply different estimation methods
15 to different groups of financial assets.
16 Estimating allowance levels under the CECL
17 methodology, including assessing qualitative
18 adjustments to historical lifetime loss estimates,
19 will involve a high degree of management judgment.
20 You're already employing considerable judgment on
21 today's model, and that will be increased under the
22 new model.

1 Therefore, consistent with our
2 existing accounting and supervisory guidance,
3 allowance estimates under the CECL methodology
4 should continue to be based on the comprehensive,
5 well-documented, and consistently applied
6 analysis, as appropriate to the size of each
7 institution and the nature, scope, and risk of its
8 lending and other credit risk-taking activities.
9 The FASB has provided significant lead
10 time for institutions to prepare for their
11 implementation in the CECL methodology until the
12 new accounting standard takes effect. At the same
13 time they provided the agencies with significant
14 lead time, as well, for us to prepare.
15 In fact, since our discussion about the
16 CECL methodology at the advisory committee meeting
17 in early April, the FASB moved the effective date
18 of the standard out one more year from where it had
19 originally been set by the FASB in November of last
20 year. As a result, for those institutions that,
21 for accounting purposes, are deemed SEC filers, the
22 new standard will take effect in 2020. All other

1 institutions will begin reporting under the CECL
2 methodology either in their first quarter of 2021,
3 or as they end the fiscal '21, depending on an
4 institution's characteristics.
5 In the joint statement, the agencies
6 encouraged institutions to start their planning
7 and preparation for the new accounting standard
8 now, including becoming familiar with the new
9 standard.
10 I would include in that ensuring that
11 your directors begin to get a basic understanding
12 of the new standard, since it will change the
13 metrics that you look at, in terms of allowances
14 versus loans, identify the data needs and necessary
15 systems changes to implement the new accounting
16 standard consistent with its requirements, the
17 allowance estimation method or methods you expect
18 to be using, and our supervisory expectations.
19 Then determine how and when to begin collecting
20 additional data that you may need, and then
21 finally, assess the potential impact on the new
22 accounting standard on capital. Both during and

1 after the transition to the CECL methodology, the
2 agency's goal is to ensure consistent and timely
3 communication to institutions about the new
4 standard and to develop and issue updated
5 supervisory guidance pertaining to the standard,
6 particularly with respect to smaller and less
7 complex institutions.
8 I might just add, before we turn it over
9 to questions, tomorrow afternoon, in fact, the FASB
10 has scheduled a webcast for 1:00 to 2:00 p.m. You
11 can register at 4:00 through the FASB website, or
12 if you have staff that you would like to have hear
13 about it, you can register through the FASB's
14 website.
15 If they can't listen tomorrow, it's
16 going to be archived and available for three months
17 on the FASB's website. There's other materials
18 that FASB has issued, as well, to help support the
19 understanding of the new standard. With that, we
20 can turn it for questions.
21 MEMBER HASKIN: I commend you for
22 repeatedly, it emphasizes the complexity for small

1 banks, that it should be matched with the
2 complexity of loans. I do appreciate that. I
3 think that's something unusual. I commend you for
4 it.
5 MR. STORCH: The industry, as a whole,
6 also was very forceful, I would say, communicating
7 that need to the FASB. I think they heard that loud
8 and clear, especially over the last six to nine
9 months.
10 MEMBER WILLIAMS: I'm not sure this is
11 a proper question to ask, but I'm not back after
12 today anyway. What do you foresee as the FDIC's
13 role for the FDIC-regulated banks as we move toward
14 implementation? Do you see beginning to help us
15 start looking at our models a couple years out that
16 we're putting in place?
17 MR. STORCH: That's one subject that
18 the accounting policy staff at the agency have been
19 talking about is what sort of expectations we
20 should have for our examiners to be looking at where
21 you are in the process. Staggered effective dates
22 is not like one size fits all, so certainly,

1 institutions can't wait until the last minute.
2 Those sorts of questions are on the list of what
3 we would expect to be communicating. Thinking now
4 about what the timeline ought to be, when you may
5 want to have whatever system changes in place, so
6 you could perhaps do some dry runs in advance of
7 when it actually takes effect with major reporting,
8 involving -- it's not just an accounting exercise
9 involving whoever you're using for IT, obviously,
10 but your credit risk management staff, whoever's
11 providing support from an internal audit/internal
12 control standpoint, so making sure that those types
13 of functions throughout the bank that are impacted
14 are involved and how soon they should be involved
15 and so forth.
16 There's not a single good answer, at
17 this point, but that's one issue that the agencies
18 will continue to talk about, so that we don't have
19 examiners going to one bank, having one very
20 high-level set of expectations, which is outside
21 what would be acceptable, and other examiners
22 ignoring the issue entirely.

1 We're going to have a good level of
2 examiner preparation and some teaching for them,
3 so they understand, as well. At the same time,
4 they have to remember what the current accounting
5 standards are. I'm sure you and all the banks are
6 applying the current standards until the effective
7 date.
8 MEMBER WILLIAMS: It's probably on the
9 radar. I think that's the main concern. I
10 wouldn't expect there to be a one-day switch foot,
11 although there will be, as far as what we're
12 required to do. It's going to be a great deal of
13 preparation still. I certainly foresee periods of
14 running the systems parallel to see what we're
15 doing.
16 MR. STORCH: I think it would be fair
17 to say that none of us should expect that everyone's
18 going to get it perfect on the first day. I think
19 even in talking to the FASB, they recognize that
20 there'll be some gaps in the data on day one, which
21 you'll have to factor in qualitatively to adjust
22 for that.

1 Over time, as you build up more data,
2 you'll be in a better position to achieve what the
3 ultimate objective of the standard was. That will
4 be something -- not expecting perfecting on day
5 one, I think, is a message we really need. Our
6 management's agreement is to give out to our
7 examiners, as well.
8 MEMBER HUDSON: That's such a big source
9 for community management.
10 MR. STORCH: That's an issue we've
11 heard repeatedly. In our joint statement, we've
12 tried to signal that if you're appropriately
13 segmenting the portfolio today, under the current
14 loss model, then maybe based on the call-in work
15 categories, the standard, in and of itself, doesn't
16 require you to change that. Certainly, for
17 community banks, you want to get that message out
18 there. Because we were hearing from sources that
19 we'd have to implement dozens of new categories.
20 We didn't see the need for that.
21 MEMBER CASTILLO: I have an
22 observation. I just got an examination report,

1 and in the examination part of the discussion was,
2 have you heard of CECL? And I read the report on
3 Monday, but in the examination, itself, it says,
4 "CECL is coming, and we expect management to start
5 advocating itself."
6 I'm curious as to whether FASB or the
7 FDIC has modeled what they think an allowance might
8 look like under the CECL method? The reason that
9 I ask that -- and this is a sentence that just jumped
10 out at me, and this is on Page 6 -- it says,
11 "Institutions should not begin increasing their
12 allowance levels beyond those appropriate under
13 existing U.S. GAAP in advance of the new standard's
14 effective date." As I read that sentence, it
15 implies the reserves are going to go up. Any
16 thoughts on what's been modeled or what --
17 MR. STORCH: The FASB, in some other
18 materials, they may even be included in what they
19 do tomorrow; I don't know -- sort of tried to look
20 at different segments, particularly the loan
21 portfolio, to see what the potential impact would
22 be. For your shorter-term loans, where maybe

1 there's an average of a one-year life, that's what
2 you're pretty much doing today under incurred
3 losses.
4 What losses do you expect to realize
5 over the next year or over, let's call it a loss
6 emergency, some loans can go over. In that case,
7 there's probably not much of an impact at all. For
8 your existing loans that are impaired loans, the
9 methodology really will still be the same, even
10 though the term impaired loans isn't in the new
11 standard. When you get to more medium-term loans,
12 then there could be some modest increase because
13 you'll be looking at two to five years for the
14 longest term loans. Think of residential
15 mortgages with a seven year average life. That may
16 have the greatest impact. It's going to depend on
17 the portfolio mix as one factor, also on economic
18 conditions when we get to '20 or '21 because you
19 have to have forward looking information for this
20 reasonable and supportable forecast period.
21 In most cases, it'll be one, two, three
22 years. In the worst economic times, you may only

1 be able to get forecasts in a very short run. The
2 bank's still expected to provide, based on loss
3 experience, for the entire life of the loan and not
4 ignore credit losses that might occur beyond the
5 period for which you can forecast. So there's a
6 lot of uncertainty.
7 There's been some press coverage, over
8 time, that the OCC have done some studies in 2013,
9 which is shortly after the proposal was first
10 proposed. Of course, that was based on 2012 data.
11 Allowances and portfolios are different now than
12 they were then. They had to make a lot of
13 assumptions. At that point, they came up with sort
14 of a general range of a 30 to 50 percent increase
15 in allowance levels, with lots of caveats attached
16 to that because their range is much wider. But
17 part of the exercise of going through that was
18 because when the proposal was issued, some banks
19 and some commentators were suggesting allowance
20 levels would increase 300 and 500 percent.
21 There was a concern if that was actually
22 going to happen, would banks be prepared for it,

1 and is that improving an accounting or not, bottom
2 line? Part of the SEC's exercise was to see, on
3 a general scale level, what type of increase might
4 be expected. It's really going to vary, depending
5 on the characteristics of your portfolio, where the
6 economy is, and where your allowance level is under
7 the current standards going into the change.
8 MEMBER BRYANT: Let me ask this
9 question, and it's tied to the question he just
10 raised. I think the model would be extremely
11 valuable because my initial reaction would be to
12 shorten the loans in the portfolio. Then if you
13 are expecting rising interest rates, and then
14 certain economic future, what's that going to do
15 to the model? Because you can manage the
16 portfolio, you may have short-term, maybe 12 months
17 -- this gets larger when you go out 24, 36, 60
18 months, and 84 months. Sitting here today, still
19 here tomorrow.
20 MR. STORCH: A starting point always is
21 what your historical, now lifetime, loss
22 experience has been. To the extent you have loans

1 today for which you had similar types of loans in
2 the past, most banks typically have annualized loss
3 rates.
4 They don't normally have constructed,
5 unless they're perhaps doing the probability of
6 default loss given the default that the largest
7 banks do, they haven't constructed loss curves to
8 see how losses occur over the lives of loans. For
9 most loans, from what I've seen, the losses occur
10 out two to three years, and then they taper off.
11 That two to three-year time horizon we
12 keep talking about probably is where the peak of
13 any losses would occur. There'd be some
14 thereafter, but the performance would likely
15 revert back more to what your lifetime experience
16 is for those outer meters of the life of the loan.
17 In theory -- and I can't say whether this is a
18 working practice -- FASB's trying to say how do
19 banks manage the credit risk today? Presumably,
20 as good credit risk management, you are looking at
21 what you expect to happen in the future, both when
22 you grant the loan, and as you work with the

1 borrower to collect the loan. This proposal, and
2 the standard, now it's out, is intended to better
3 align sound credit risk management practices with
4 the accounting.
5 If your credit risk management people
6 are factoring in likely future events or expected
7 future events into their assessment of how we're
8 going to manage the portfolio, they'll now bring
9 that thought process into the estimation and
10 re-allowance going forward, at least starting in
11 2020 or '21.
12 MEMBER BRYANT: We had losses the last
13 two years, so if we can keep that to 2018-2019, I
14 think we'll be in pretty good shape.
15 MR. STORCH: You still have to look at
16 lifetime loss experience as kind of a baseline, and
17 then say given what our baseline experience is, how
18 do we expect conditions over the forecast period
19 in the life of these loans to be different than
20 those good years, where we haven't had any
21 charge-offs? It's not likely that a zero
22 allowance or some very tiny allowance would be

1 acceptable, but it's going to depend on your facts
2 and circumstances. One of the messages is should
3 it always have been under the existing rules the
4 allowance is an institution-specific number?
5 There's no one right number that's right for all
6 institutions, although sometimes you hear people
7 arguing that.
8 MEMBER LUNDY: I do think, just from an
9 observational standpoint, there's already been a
10 lot of margin pressure the last five years.
11 Bankers and our regulators, based on our historical
12 experience, have been rightly concerned about
13 interest rate risk.
14 Of course, if we could all look
15 backwards, we realize that we've left a lot of money
16 on the table, as an industry, trying to guard
17 against that interest rate risk. I don't know
18 what's going to go on in the future, but I do think
19 that Pedro's on to something. I think that this
20 will tend to compress duration, and I think that
21 will put more pressure on margin for community
22 banks who have less ability to lay off that interest

1 rate risk and are more dependent on spread income.
2 I can't quantify that, but one way to guard against
3 either an imposed or too difficult to figure out
4 expected risk loss in years three, four and five
5 is to, as a protective measure against criticism,
6 shorten that duration, which may make you less
7 competitive from a pricing standpoint. I think,
8 in particular, the smaller banks' segment, which
9 is so dependent on spread income, has to worry about
10 that and how this impacts our earnings.
11 MEMBER WILLIAMS: I just think you guys
12 just keep your eyes and ears open for it. I
13 understand the concept that every bank is
14 different, every bank has different risk profiles.
15 I understand all that, but this will come down to
16 some kind of a fairly simple model, with tweaks
17 related to the riskiness of the classification of
18 loans within the bank and that sort of thing, the
19 individual data that we have.
20 But there will be some standard for how
21 we track this information -- akin to the idea of
22 historical losses, where you say did you use a

1 rolling 24 months, did you use 36 months? There's
2 all kind of tweaks, but there's some history period
3 that you -- I think it's going to come down to some
4 model. I know you guys have to be very careful that
5 you don't manage our banks. I understand that
6 concept. But I think any help, as that model
7 begins to fall into place, to make it easier for
8 us. Does that make sense?
9 MEMBER SCULLY: I'm sure you've
10 already done this, but I think, also, staying in
11 touch with not just FASB, but individual accounting
12 firms. I know our accountants have said that
13 because of the vintage approach, no matter what
14 anybody tells us, there's no way we can keep doing
15 this on a spreadsheet, no way. That involves some
16 level of complexity.
17 (Simultaneous speaking.)
18 MR. STORCH: I think the FASB has tried
19 to dissuade people of that. There's some vintage
20 disclosures for banks that are -- for accounting
21 purposes are called public that has to be provided.
22 That's disclosure, not measurement. FASB's tried

1 to distinguish vintage measurement from vintage
2 disclosure. If you look at the standard -- or the
3 people that deal with accounting look at the
4 standard, there are examples that the FASB has
5 included of loss rate methods and so forth, to make
6 it clear that from a community institution
7 perspective particularly, those methods are
8 acceptable. There is also a vintage example, but
9 it's clearly not the only example of how to apply
10 the methodology. The agencies do have some
11 meetings with accounting policy staffs and
12 accounting firms that we are scheduling now, just
13 to find out what issues they're hearing from their
14 clients and so forth.
15 We've also indicated to the trade
16 groups that we're more than willing to work with
17 them on issues that they're hearing from their
18 members. I think we all want to get this as right
19 as we can, acknowledging that it's an evolutionary
20 process before takes effect, and even after it
21 takes effect.
22 MEMBER WILLIAMS: We can all dream that

1 you guys will come out and say just do 50 percent.
2 CHAIRMAN GRUENBERG: That sounds
3 familiar. Anything else? We focused on this and
4 be as helpful as we can. Thank you all very much.
5 To those of you who this is your last day, we'll
6 miss you, and please stay in touch. The rest of
7 you, we'll see you the next time. Thank you.
8 (Whereupon, the above-entitled matter
9 went off the record at 2:49 p.m.)
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