**Comment Letter on Notice of Proposed Rulemaking on Unsafe or Unsound Practices and Matters Requiring Attention**

**From:** Neal Moran

**Subject: Comment Letter on Unsafe or Unsound Practices and Matters Requiring Attention (Docket ID: OCC-2025-0174**

**Date:** December 4, 2025

I am a former federal bank examiner who spent more than 36 years in bank supervision including more than a decade in Large Bank Supervision at the OCC. I covered some of the largest and most complex banking organizations and have a deep knowledge of assessing unsafe or unsound practices, issuing MRAs, and recommending CAMELS ratings. I currently write a blog (**www.uponfurtheranalysis.com**) primarily devoted to banking and its regulation. I welcome the opportunity to comment on the Notice of Proposed Rulemaking (NPR) and believe I bring to the discussion both extensive technical knowledge of the issues and a lack of self-interest.

The proposed rule that would define "unsafe and unsound practices" and change standards for issuing matters requiring attention (MRAs) and downgrading CAMELS ratings. While supposedly designed to promote a greater focus on core financial risks, the thresholds are set so high (*likely* and *material* loss) as to undermine attempts at preventive supervision.

Effective banking regulation depends on preventive supervision. Spotting warning signs and excessive risk taking early allows supervisors to intervene when the bank is still salvageable. Waiting for weaknesses to manifest themselves in clear indicators of financial deterioration practically ensures a delayed and ineffective response.

At least the "unsafe or unsound" designation was understood to represent a high bar, reserved for the most serious deficiencies and reckless behavior. However, the NPR would compound the problem by extending the "likely financial harm" standard to intermediate supervisory steps, like MRAs and rating downgrades.

Establishing a standard of likely and material financial harm to even *criticize* a bank reflects a fundamental misunderstanding of the nature of risk. A risk can be excessive, unsafe, and unsound without a *likely* bad outcome. Consider driving while intoxicated (DWI). Drunk drivers are roughly 14 times more likely than sober drivers to get into an accident. That doesn't make getting into a crash *likely*. In fact, **only about 0.16%** of drunk drivers will get into a crash on any given trip. Does that mean that we should stop DWI enforcement since a drunk driver is more likely than not to get home safely?

*My responses to the NPR's specific questions are provided below:*

**Question 1: What effect would the proposed rule have on the agencies' ability to address misconduct by institutions under their enforcement and supervisory authority? What effect**

**would the proposed rule have on the agencies' ability to address misconduct by institution-affiliated parties under their enforcement and supervisory authority?**

The proposed rule will undermine the agencies' ability to address misconduct. Internal abuse can and has led to material financial losses both to banks and to the FDIC. The **FDIC's own study** found that insider abuse played a role in 37% of all bank failures. However, the requirement that "the conduct must be sufficiently proximate to a material harm to an institution's financial condition to meet the proposed definition" could preclude actions against a wide range of misconduct. If bank insiders steal just a little, or the extent of the damage is not yet readily apparent, that's apparently not material financial harm. The revised MRA definition can cover regulatory violations, but it precludes requiring banks to take actions to prevent violations.

In addition, the agencies expect to only take actions regarding violations of *banking* laws. Tax evasion, insider trading, and other illegal and unethical conduct would apparently be off limits. The proposal also states that the agencies *"would not downgrade an institution's composite rating to less-than-satisfactory based only on a violation of law, unless such practice, act, or failure to act that results in the violation of law also is likely to cause material harm to the financial condition of the institution, is likely to present a material risk of loss to the DIF, or has caused material harm to the institution's financial condition, as the agencies propose under the unsafe or unsound practice definition."* In other words, a bank could violate the regulations and the law with impunity and not expect any adverse consequences outside of a possible MRA.

**Question 2: Does the proposed definition of unsafe or unsound practice appropriately capture the types of objectionable practices, acts, or failures to act that should be captured? Please explain.**

No. It takes a decidedly backward-looking approach to bank supervision that would preclude a wide range of imprudent activity and abusive conduct until a loss has already occurred or is sufficiently imminent as to be deemed "likely." By that point, corrective actions are usually too late.

**Question 3: Does the proposed definition of unsafe or unsound practice provide the agencies with adequate authority to proactively address risks that could cause a precipitous decline in an institution's financial condition, such as a liquidity event or a cybersecurity incident?**

No. The requirement that a risk is *likely* to result in material financial harm would prevent supervisors from proactively addressing risks, even severe risks. Good examiners can spot emerging risks but the expectation that these risks will result in material financial harm usually occurs only after the fact. For example, Signature Bank had a high degree of liquidity risk but when did a risk become *likely*? March 2023?

**Question 4: Other than "material," are there terms that the agencies should consider to specify the magnitude of the risk required for a practice, act, or failure to act, to be considered an unsafe or unsound practice, e.g. "abnormal," "significant," or "undue"?**

"Undue" is a more appropriate term. "Material" could preclude actions against a wide range of imprudent activities. While the term "undue" remains vague, it can help identify risks that go beyond prudent banking practice.

**Question 5: Is "likely" the appropriate standard to specify the probability of risk required for a practice, act, or failure to act, to be considered an unsafe or unsound practice? Is another term more appropriate, e.g. "reasonably foreseeable," "could reasonably," "imminent," "abnormal probability?" Should the agencies specify a minimum percentage of likelihood? If so, what would be an appropriate minimum percentage of likelihood? Should the agencies consider a standard that does not imply an assessment of a forward-looking probability?**

"Reasonably foreseeable" is a better term. The "likely" threshold is much too high and would preclude most reasonable supervisory actions. The standard should not imply an assessment of a forward-looking probability. Determining probability, a priori is at best an educated guess and is nearly always wrong when looking at the tail events that lead to the most expensive and disruptive bank failures.

**Question 6: Should the agencies consider specifying one or more quantitative measurements to define or exemplify "material harm" to the financial condition of the institution?**

Yes. The current definition is extremely vague and too easy to change pre- to post-mortem. In practice, it means that front-line supervisors (usually career employees) will get little support in their assessment of "material harm" before the fact but remain open to second guessing following a costly failure. Meanwhile, policy makers, especially political appointees, can elude any accountability for their actions, by refusing to commit upfront to what they mean by material harm. We saw this scenario play out during 2023, and the newly proposed actions involve a much more active undermining of bank supervision.

**Question 8: Should the agencies define harm to the financial condition of an institution in the regulation? If so, how? Should this include specific indicators or thresholds, or adverse effects to capital, liquidity, or earnings?**

Specific indicators or thresholds can provide a useful but insufficient starting point, but just a starting point. Failures and near-failures of large and complex financial institutions usually reflect a combination of factors rather than one isolated risk or deficiency. Did a specific weakness or exposure doom Lehman? If we turn to OCC-regulated institutions, look at the massive federal assistance used to save Bank of America or Citibank (an estimated $476 billion in the case of Citibank). Would their exposure to individual asset classes or risk management weaknesses have, a priori, appeared likely to result in material financial losses, especially when hardly anything rates as material at a trillion-dollar bank?

**Question 13: Other than "could reasonably be expected," are there terms that the agencies should consider to specify the probability of risk required for a practice, act, or failure to act, to be communicated as an MRA, e.g. "could possibly," "could foreseeably," "would"? Is this standard sufficiently distinct from the likelihood requirement for unsafe or unsound practices so as to convey a lower bar?**

"Could reasonably be expected" represents too high a bar and could prevent supervisors from taking a proactive approach to emerging problems. "Could foreseeably" addresses elevated risk without requiring a material financial loss to be *likely*.

**Question 14: The proposal would allow the agencies to issue MRAs based on "reasonably foreseeable conditions." Is "reasonably foreseeable" the right standard? As an example, at what point in Silicon Valley Bank's timeline would an MRA for weaknesses in interest rate risk management have been (1) appropriate and (2) permissible under the proposal? If another standard would be more appropriate, please explain.**

Unrealized losses on securities at SVB had risen to alarmingly high levels during 2022, reaching more than 100% of Tier 1 capital. But by then it may have been too late. The optimal time for supervisory intervention would have been in 2021, when the bank was growing imprudently but there was still an opportunity to reduce the IRR exposure at a modest loss. Trying to hedge by mid-2022 would have only locked in the unrealized losses.

It's not even clear that SVB would have met the "likely material loss" standard in late 2022. Most of its securities were in the held-to-maturity category where bank management and its accountants asserted SVB had the intent and ability to hold to maturity. The last major runup in interest rates was nearly 30 years earlier (1994) and proved short-lived, returning to previous levels in only about a year. Riding out the adverse rate cycle was not entirely implausible.

It's quite possible that if the proposed framework were in effect from 2021 to 2023, it would have precluded even the Federal Reserve's modest and insufficient actions to address SVB's interest rate risk. The FDIC's supervision of First Republic Bank might provide a better indicator of things to come. That bank's failure cost the FDIC $15.6 billion. Yet until March 31, 2023, the bank had no outstanding MRBAs, with both management and liquidity rated "1." The FDIC made some eleventh-hour ratings downgrades and added an MRBA, but these actions were much too late to stave off failure or even to mitigate losses to the FDIC.

**Question 15: If the agencies adopt the proposed standard for the issuance of an MRA, how should the agencies determine when to close an MRA? Should the agencies provide additional clarity in a final rule? Are there unique verification and validation concerns associated with the proposed standard that the agencies should consider? Should verification and validation procedures be tailored for different types of institutions,**

**considering factors like the sophistication of an institution and the frequency of examinations? Should there be a limit (e.g., one or two quarters; one examination cycle) to the duration that an MRA may remain open after an institution corrects the practice resulting in the MRA? If an MRA is not remediated for a certain period of time, what steps should the agencies take?**

Current OCC guidance on MRA remediation verifies that the bank has taken steps to address the deficiency and goes through a validation process to ensure that the actions are both effective and sustainable. That is a reasonable standard. There should be specific timeframes for providing feedback to the bank if the supervisors deem the corrections either insufficient or unsustainable. However, it makes no sense for supervisors to pretend that corrective actions are sufficient and sustainable merely to meet some imposed deadlines. Such an approach would likely disincentivize banks to take the necessary (and sometimes costly) steps to correct problems when running out the clock would have the same effect.

**Question 16: Should the proposal provide any clarity around timeframes for remediating MRAs? If so, should small institutions (and those with limited resources) be provided with longer timeframes to address MRAs? Should institutions with more severe vulnerabilities (such as 5-rated institutions) be provided shorter timeframes?**

Large Bank Supervision at OCC used an 18-month timeframe as a rough guideline, with the idea that deficiencies requiring longer timeframes may be better suited for formal enforcement actions. It makes sense for the agencies to lay out their expectations for MRA remediation timelines while also allowing flexibility to adjust to individual circumstances.

**Question 17: Should the proposed standard for issuing MRAs also apply to issuing violations of law? Why or why not? If a different standard should apply, please describe the standard and explain why. If the agencies did not use MRAs for violations of law, how should the agencies approach violations of law?**

No. Violations of law, which include regulatory violations, need not follow some material financial harm test. A violation is a violation and bank supervisors must enforce the law. Moreover, with the effective dismantling of the CFPB, banking regulators need to take a more, rather than less active role in enforcing consumer banking laws and regulations.

**Question 20: Should the agencies require any downgrade to a CAMELS composite rating of 3 or below to be accompanied by an MRA or enforcement action? Are there instances in which, for example, general economic conditions or idiosyncratic risk factors could cause financial deterioration without evidence of objectionable practices, acts, or failures to act? Could such a provision incentivize issuing more MRAs? Please explain.**

There are really two separate issues here, one vastly more important than the other. If a bank's condition is less than satisfactory, there is naturally some presumption that it needs to take some actions to improve its condition, or at least not make the situation worse. However, the more important issue is the proposal's presumption that outstanding MRAs are a prerequisite to downgrades to "3" or worse. That approach might have made sense using the current criteria for issuing MRAs. It makes no sense under the current proposal, which applies essentially the same "unsafe or unsound" threshold to MRAs. In effect it would also require unsafe or unsound practices or conditions to downgrade to a "3" rating. However, the Interagency Financial Institution Rating System, unchanged for nearly 30 years, associates "unsafe or unsound" with 4- or 5-rated banks. A 3-rating corresponds to a less than satisfactory condition that requires more than normal supervision, not to unsafe or unsound practices, much less to the likelihood of material financial losses that threaten a bank's viability.

This could lead to two, presumably unintended consequences from the proposal. First, the Federal Reserve has not joined the proposal, which could lead to ratings inconsistencies between state-chartered member banks (supervised by the Fed) and FDIC or OCC-regulated banks. It could also lead to inconsistencies between banks with the same regulator. The proposal focuses only on rating downgrades. What happens to banks already rated 3? Would the change mean that supervisors would rush to upgrade these banks, based not on improvements to their condition or practices but because their practices were merely deficient rather than life-threatening?

**Question 21: To what extent should the agencies use MRAs to address banks that are vulnerable to potential economic or other shocks? For example, before the Federal Reserve began raising interest rates in 2022, or shortly after it began raising interest rates, at what point, if any, would it have been appropriate for a banking agency to issue MRAs to institutions that were vulnerable to a rise in interest rates? Does the proposal appropriately allow MRAs in such cases, if applicable? Under the proposal, are there other supervisory tools to address such risks?**

MRAs can be an effective tool to address a bank's vulnerability to economic shocks, such as rising market interest rates or erosion of credit quality. Longer term interest rates started rising in early 2022, which would have been the most effective time for intervention. Waiting until rates had already risen substantially would have only locked in losses. The proposal does not appear allow MRAs in such cases since a "material financial loss" due to interest rate exposure does not become "likely" *prior to* a sharp rise in rates. That rarely becomes apparent until after the fact. The wording of the proposed regulation is quite vague, which could theoretically allow an earlier intervention if both examiners and senior agency leadership showed great prescience. That appears unlikely since the creators of this proposal appear to lack a fundamental understanding of financial risk.

**Question 26: What additional steps should the agencies consider to reform supervision, consistent with the goals of the proposal? The agencies have an extensive supervisory framework including examination manuals, regulations, guidance, and internal procedures governing how banks are supervised. What modifications to these various documents are warranted? How should the agencies sequence these actions?**

The agencies need to take a pause. The agencies have rushed out a series of ill-considered actions, from drastically cutting staff, to watering down capital requirements, to the current proposal. These actions may please bank lobbyists, but it makes for terrible public policy. Acting hastily without evaluating the effects of previous decisions is likely to exacerbate the situation. First, do no harm!

Thank you for the opportunity to comment on this important proposal.

Sincerely,

Neal Moran