The Meeting of the Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation

July 30, 2019 – 9:00 A.M.

The meeting of the FDIC Advisory Committee on Community Banking ("Committee") was called to order by Jelena McWilliams, Chairman, Federal Deposit Insurance Corporation ("FDIC") Board of Directors.

The members of the Committee present at the meeting were: Dick J. Beshear, Chairman, President, and Chief Executive Officer (CEO), First Security Bank and Trust Company, Oklahoma City, Oklahoma; Asif Dakri, Vice Chairman and CEO, Wallis Bank, Houston, Texas; Fred DeBiasi, President and CEO, American Savings Bank, Middletown, Ohio; Christopher Donnelly, President and CEO, Bank of the Prairie, Olathe, Kansas; James J. Edwards, Jr., CEO, United Bank, Zebulon, Georgia; Keith Epstein, Executive Vice President and CEO, Roxboro Savings Bank, SSB, Roxboro, North Carolina; David J. Hanrahan, Sr., Wenonah, New Jersey; Danny J. Kelly, President and CEO, The Hometown Bank of Alabama, Oneonta, Alabama; Kenneth Kelly, Chairman and CEO, First Independence Bank, Detroit, Michigan; Bruce Kimbell, President and CEO, First Community Bank of the Heartland, Clinton, Kentucky; Thomas Leavitt, President and CEO, Northfield Savings Bank, Northfield, Vermont; Lori Maley, President and CEO, Bank of Bird-in-Hand, Bird-in-Hand, Pennsylvania; Tiffany Baer Paine, President and CEO, Security Bank USA, Bemidji, Minnesota; Alan Shettlesworth, President and Chief Operating Officer, Main Bank, Albuquerque, New Mexico; Joseph W. Turner, President and CEO, Great Southern Bank, Springfield, Missouri; Louise Walker, President and CEO, First Northern Bank of Dixon, Dixon, California; and Len E. Williams, CEO, People's Intermountain Bank, American Fork, Utah.

Cathy Stuchlik, Chairwoman and President, Clackamas County Bank, Sandy, Oregon, was absent from the meeting.

Corporation staff who attended the meeting included: Ruth R. Amberg, Daniel J. Bendler, Ryan Billingsley, Rebecca Bittle, Leonard N. Chanin, Kymberly K. Copa, Carolyn D. Curran, Timothy J. Davin, Chad R. Davis, Christine M. Davis, Doreen R. Eberley, Bret D. Edwards, Lekeshia Frasure, Samantha B. Gibson, Bobbie Gray, Patricia S. Gurneau, Emerson B.

Hall, Moneick A. Hendricks, Martin D. Henning, Nicholas S. Kazmerski, Arleas Upton Kea, M. Anthony Lowe, Christopher Lucas, Brandon Milhorn, Jonathan N. Miller, Rae-Ann Miller, Arthur J. Murton, Elizabeth Ortiz, M. Rowie Pangilinan, Nicholas J. Podsiadly, Luke W. Reynolds, Lisa K. Roy, Betty J. Rudolph, Robert Storch, Maureen E. Sweeney, Erica J. Tholmer, Amy C. Thompson, James C. Watkins, and James S. Watts.

Chairman McWilliams opened and presided at the meeting. She noted that during her first year as Chairman she visited bankers in approximately 21 states. She found that many of those bankers were similarly situated to the banks represented on the Committee. She advised that those banks rely on the Committee members to share their perspectives with the FDIC. She then thanked the Committee members for being the voice of community banks.

The Chairman then introduced Mr. Chad R. Davis, Deputy to the Chairman for External Affairs and the Committee's Designated Federal Officer, who moderated the rest of the day's proceedings. Mr. Davis advised that the first item on the agenda was "Committee Member Discussions of Local Banking Conditions." The Committee members then discussed a range of issues, including the following.

Banking Conditions. The members reported that their local areas are economically strong; asset quality and loan growth are strong; delinquencies and problem assets are low; and unemployment rates are at national lows. Although there are no apparent, significant weaknesses generally, bankers are monitoring a range of sectors. These include rural health care as hospitals deal with a mix of payers; potential overdevelopment in certain hospitality markets; the market for renewable energy and solar activity; and the cost of private education. In short, members reported that they are watching for signs of another economic downturn but are not seeing evidence of weaknesses as yet.

Housing Markets. Several members reported that housing market fundamentals remain positive as high employment supported housing demand. However, the high demand for residential and multi-family homes resulted in higher prices and reduced affordability. Member Paine reported that in her area there is great demand on title companies and appraisers. More and more small community banks are opting not to offer in-house mortgages. Member Paine noted that her bank is helping other community banks by underwriting their loans, putting those on the books, and working as a referral service. Her bank started sharing its services in the audit and compliance areas and felt such mortgage support was a natural progression since the bank has the in-house expertise. Member Donnelly noted the challenges in home mortgage lending and ensuring proper mortgage loan documentation. He also stated that in rural areas bankers are observing that houses that used to be owned by local people are being turned into rentals; people are renting instead of buying.

Rural Communities. Members suggested that some rural communities still struggle. Issues noted include rural population declines and sales of multi-generational family farms. Member Danny Kelly pointed out that every rural area needs to focus on training opportunities because there is a strong demand for a skilled workforce. Member

Donnelly, who serves as Chairman of the Kansas Bankers Association, noted discussions with numerous bankers in the state. He indicated that local bankers are trying to help their community survive but as small communities lose population, the communities eventually die, and local banks move out.

Regulatory Issues. Members voiced appreciation for the progress made with respect to the issues of brokered deposits and interest rate restrictions and noted that they are continuing to track those issues with great interest. Member Hanrahan addressed the national rate cap. He found it very helpful to review some of the comment letters received in response to the FDIC's advance notice of proposed rulemaking regarding brokered deposit and interest rate regulations. He suggested there seemed to be a common theme: A need for a formulaic fix to the national rate cap. Member Donnelly also stressed the importance of the rate cap issue given the significant competition for deposits from large credit unions and large banks. Other members said they are monitoring developments with respect to the community bank leverage ratio proposal. They noted that community banks are weighing it as an option but need more information at this stage. Member Maley advised that her bank is seeking guidance with respect to flood insurance provided by mutual aid societies.

Bank Examinations. Several members stated that their banks were examined by the FDIC in the past several months. They appreciated the FDIC's examination planning efforts. They noted that, for banks with limited staff, it is helpful to have time to gather materials and provide information in advance of the examination team's arrival. In addition, Member Maley complimented the communication between staff at her bank and FDIC examination staff.

Staffing and Succession Planning. Members noted that the strong economy presents challenges as banks, like everyone else, have to compete for talent. Member Williams cited the challenges of finding loan officers. Member Edwards stated that his institution began a management training program in an effort to develop talented lenders. Members also touched upon the issue of succession planning. Member Leavitt sought clarification with respect to the breadth and depth of a formal management succession plan.

Consolidation. Several members touched on industry consolidation. Member Kimbell discussed the acquisitions of community banks by credit unions, and he noted that those acquisitions seemed to be increasing. He questioned whether credit unions can address the needs of farmers and other customers as well as community banks can. Member Dakri cited the flurry of acquisition activity. He attributed it to a battle for deposits and noted that banks with stable deposits are looking to sell because there is a market for them. Member DiBiasi discussed the probable merger of his institution. He highlighted the small size of his institution. He noted that, an institution such as his, with $44 million in total assets, is difficult to sustain and cited the long-term need to achieve economies of scale. He touched on the deliberative process that his bank underwent to find the best merger partner.

Minority Depository Institutions. Member Kenneth Kelly thanked the Chairman for her strong support of minority depository institutions, stating that the report included in the materials for the Committee is a testament to the FDIC's commitment to promote minority depository institutions across the country.

Other Issues. Member Turner noted that legalization of marijuana has caused more consternation than anticipated. He raised the issue of having a commercial real estate customer who may have a tenant involved in a marijuana business that is permissible under state law. Member Shettlesworth echoed this issue at a later point in the meeting. Member Beshear stated that banks need clarification as to whether they can provide banking services to medical marijuana businesses.

Member Epstein reported that North Carolina is witnessing a transition from tobacco farming to hemp farming and an influx of out-of-state money to purchase land with the intent to grow hemp. In addition, the state is seeing infrastructure investments in greenhouses as well as warehouse space for distribution.

Member Kenneth Kelly cautioned that technology companies are competing for deposits in ways that banks cannot due to capital constraints. He also suggested that more unbanked or underbanked individuals are receiving their paychecks via debit cards, and this trend discourages these individuals from engaging with the banking system.

Member Maley noted that her bank has had great success with a mobile bank unit; customers can transact any type of business that would typically be done in a branch. The mobile unit helps the bank serve nine communities where people are underbanked. Given the success of this mobile unit, her bank is exploring a second mobile unit.

Member Shettlesworth indicated that some small non-profit organizations have encountered challenges as larger charities apparently trim back initiatives. Consequently, his bank has stepped in to provide working capital for these non-profits.

Following the general discussion by members regarding banking conditions in their communities, Mr. Davis announced that the meeting would briefly recess. Accordingly, the meeting stood in recess at 10:22 a.m.

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The meeting reconvened at 10:36 a.m. that same day, at which time Mr. Davis advised that the next item on the agenda was a Supervision Update. The presentation was delivered by Doreen Eberley, Director, Division of Risk Management Supervision ("RMS"); Rae-Ann Miller, Associate Director, RMS; Robert Storch, Chief Accountant, RMS; Ryan Billingsley, Corporate Expert (Capital Markets), RMS; and Martin Henning, Deputy Director, RMS.

Ms. Eberley provided an overview of the panel's presentation, noting that Mr. Billingsley would address the community bank leverage ratio; Mr. Storch would discuss reduced reporting requirements for certain institutions with assets of less than $5 billion; Ms. Miller would provide

an overview of comments received in response to an advance notice of proposed rulemaking ("ANPR") concerning brokered deposits and interest rate restrictions; and Mr. Henning would review an interagency statement concerning risk-focused Bank Secrecy Act ("BSA") and Anti-Money Laundering ("AML") supervision and examinations. Before opening the panel discussion, however, Ms. Eberley responded to questions raised during the earlier Committee discussion concerning succession planning. She advised that succession planning is appropriate for key employees but is not essential or necessary for all employees. Moreover, RMS relies on each institution to identify those employees it deems key to its operations.

Mr. Billingsley then directed the Committee's attention to the final rule, *Regulatory Capital Rule: Simplifications to the Capital Rule Pursuant to the Economic Growth and Regulatory Paperwork Reduction Act of 1996,* issued by the FDIC, the Office of the Comptroller of the Currency ("OCC"), and the Board of Governors of the Federal Reserve System ("Fed") (collectively, the "agencies"). 84 Fed. Reg. 35234 (July 22, 2019). He reminded the Committee that the agencies published a notice of proposed rulemaking ("NPR") in October 2017 with the goal of reducing regulatory compliance burden, particularly on community banking organizations, by simplifying certain aspects of the agencies' risk-based and leverage capital requirements.

Mr. Billingsley highlighted certain aspects of the final rule. The final rule simplifies the capital treatment for mortgage servicing assets ("MSAs"), certain deferred tax assets ("DTAs"), and investments in the capital instruments of unconsolidated financial institutions. As further detailed in the final rule, non-advanced approaches banking organizations are required to deduct from common equity tier 1 capital any amount of MSAs, temporary difference DTAs, and investments in the capital of unconsolidated financial institutions that individually exceed 25 percent of common equity tier 1 capital of the banking organization (the 25 percent common equity tier 1 capital deduction threshold). Mr. Billingsley noted that the final rule changed the threshold deduction from 10 percent to 25 percent.

Mr. Billingsley also highlighted the final rule's elimination of the aggregate threshold deduction for those three asset classes. In the past, if a bank had MSAs, certain DTAs, or investments in the capital of unconsolidated financial institutions, that in the aggregate exceeded 15 percent of common equity, the bank would also have to take a deduction. He reported that the aggregate threshold was eliminated in the final rule.

Against that background, Mr. Billingsley then turned to the community bank leverage ratio ("CBLR"). He advised that the NPR, *Regulatory Capital Rule: Capital Simplification for Qualifying Community Banking Organizations*, was issued by the agencies in February 2019; the comment period ended April 9, 2019; and the FDIC received over 600 comments in response to the NPR. 84 Fed. Reg. 3062 (Feb. 8, 2019). As outlined in the NPR, the proposed CBLR framework is a simple alternative methodology to measure capital adequacy for qualifying community banks. The proposal is intended to provide material regulatory relief while maintaining safety and soundness in the banking system.

With respect to the comments received in response to the CBLR NPR, common themes included a strong preference for using existing Tier 1 capital in the numerator of the leverage

ratio, opposition to the prompt correction action proxies that the FDIC proposed, and a desire for a leverage ratio lower than the proposed 9 percent. In response to questions posed by the Committee, Mr. Billingsley clarified that the size of qualifying banks is set at total consolidated assets of less than $10 billion and the bank must have off-balance-sheet exposures (excluding most derivative exposures and unconditionally cancelable commitments) of 25 percent or less of total consolidated assets. He anticipated that roughly 80-85 percent of banks with assets under $10 billion would qualify for the CBLR. Going forward, the FDIC will review the comments, coordinate with the OCC and Fed staff, develop recommendations, and prepare a case for Board consideration. Mr. Billingsley assured the Committee that the CBLR is a "front burner" issue.

Next, Mr. Storch provided an update on developments affecting Consolidated Reports of Condition and Income ("Call Reports"). The banking agencies issued a final rule implementing Section 205 of the Economic Growth, Regulatory Relief and Consumer Protection Act in June. The final rule is titled, *Reduced Reporting for Covered Depository Institutions*, and is effective July 22, 2019. 84 Fed. Reg. 29039 (June 21, 2019). Section 205 requires the agencies to issue regulations to allow for reduced reporting in Call Reports in the first and third calendar quarters of a year. The final rule meets the statutory requirements of Section 205 by expanding eligibility for filing the agencies' most streamlined report, the FFIEC 051 Call Report, to include institutions with less than $5 billion in total consolidated assets that meet other criteria. He noted the agencies chose to use the existing 051 Call Report to implement Section 205 because it is already the version that generally collects the least amount of information compared to the other versions (the 041 and the 031 for banks with foreign offices). Further, the majority of institutions with total assets of less than $5 billion that already use the 051 Call Report are familiar with it. Nonetheless, an otherwise eligible institution is not required to file the 051 Call Report and has the option to file the 041 Call Report. However, more than three quarters of the approximately 4,800 institutions with less than $1 billion in assets already file the 051 Call Report, and by expanding eligibility to $5 billion in total assets, about 550 more institutions will be eligible to file the 051 Call Report.

Mr. Storch advised that the agencies also approved a number of reporting changes to the 051 Call Report. These changes include a reduction in the reporting frequency from quarterly to semi-annually for certain existing data items, such as detailed regulatory capital risk-weighting data, details on troubled debt restructurings, website addresses, trade names, and certain trust data. Mr. Storch explained these reporting changes will further increase the number of 051 Call Report data items for which semi-annual reporting will apply.

Mr. Storch then referred to those institutions with $1 billion or more in total assets that are eligible to file the 051 Call Report. He noted that certain data items pertaining to estimated and uninsured deposits, disaggregated data on the credit loss allowances, and certain data on consumer deposit account products, that are currently reported in the 041 Call Report, are being added to the 051 Call Report, but generally will be collected semi-annually or annually rather than quarterly. Mr. Storch clarified that these items would not be required from institutions with less than $1 billion in total assets that file the 051 Call Report. Mr. Storch noted that the agencies are committed to looking for ways to further reduce the reporting burden associated with the 051 Call Report while taking into consideration the need to collect sufficient

information for the agencies to fulfill their statutory roles of chartering, licensing, supervising, and insuring depository institutions.

Mr. Storch next referred to the CBLR and advised that the NPR, if finalized, would have Call Report consequences. He noted that the CBLR proposal is an entirely different framework from the existing risk-based capital framework. Consequently, the CBLR would lead to a change in reporting capital data. Mr. Storch advised that is one possible area where smaller institutions would benefit from a reduced reporting burden. In any event, the agencies separately sought comment on the proposed changes to regulatory reports for qualifying community banking organizations that elect to use the CBLR framework, but no comments regarding the Call Report proposal were received. Ultimately, to the extent modifications are made to the proposed CBLR framework, corresponding changes will be made to the Call Report collection of data for CBLR as well.

Next, Ms. Miller addressed brokered deposit regulations and the interest rate restrictions (or "caps") applicable to banks that are less than well capitalized. She reminded the Committee that the FDIC issued the ANPR titled, *Unsafe and Unsound Banking Practices: Brokered Deposits and Interest Rate Restrictions*, earlier this year. The comment period ended May 7, 2019. 84 Fed. Reg. 2366 (Feb. 6, 2019).

By way of background, she noted that the national rate calculation was implemented in 1992. From 1992 to 2009, the calculation was pegged to rates on similar maturity U.S. Treasury obligations; the cap applicable to less than well capitalized institutions added 75 basis points to that national rate. This approach worked fairly well until the mid-2000s because deposit rates and Treasury obligations moved in the same direction. During the crisis of 2008, however, that relationship between deposit rates and Treasury obligations changed when yields on Treasury obligations plummeted as investors fled to quality. As a result, the "national rate" became artificially low. The FDIC therefore revised the calculation of the national rate in 2009 to an average of actual rates paid by insured depository institutions. Information on the actual rates paid is based on a survey performed for the FDIC by a third-party company. The results are published weekly. In the 2009 rule, the FDIC created a presumption that the prevailing rate in any market would be the national rate. That presumption is rebuttable, in that an institution can seek a higher-rate determination and present evidence that the rate in a particular market is higher than the national rate. If the FDIC agrees with the evidence, a bank may be permitted to pay as much as 75 basis points above the prevailing local rate.

Ms. Miller then discussed some challenges with the current national rate calculations. For example, when interest rates started to rise in 2015, banks, especially large banks, were flush with cash and slow to raise interest rates. While it is true the national rate grew, it grew very slowly. Today the national rate is so low that nearly all the banks that are less than well capitalized are seeking local rate determinations. In addition, Ms. Miller noted the increase in promotional deposit products and products with special features. These products and promotions are generally not compatible with the standard products included in the FDIC's published weekly national rate caps. Therefore, the FDIC believed it appropriate to issue the ANPR to obtain comment on all aspects of its regulatory approach to interest rate restrictions as well as brokered deposits.

Ms. Miller noted that the FDIC received 130 comments in response to the ANPR. She then provided an overview of comments received in response to the ANPR. With regard to the interest rate restrictions, comments included adding credit unions into the national rate calculation; incorporating some factor that takes into account the power of internet banks; rejecting a branch-by-branch approach and using a one-bank, one-vote approach; and reconsidering what it means to be significantly above the prevailing rate. With regard to brokered deposits, comments addressed the meaning of "facilitating" the placement of deposits as well as the impact of new programs such as health savings accounts and prepayment accounts. Ms. Miller indicated that the FDIC is initially focusing on more immediate issues regarding the calculation of the rate cap before turning to the broader policy issues related to brokered deposits. Ms. Miller assured the Committee that FDIC staff is working hard in an effort to craft a proposed rule for Board review and further public comment.

Ms. Miller then touched upon concerns raised by the Committee with respect to "volatile deposits." She advised that the FDIC became aware of the issue last year when banks expressed concern that examiners might be characterizing regular deposits as volatile funding sources in the examination report. Ms. Miller said the FDIC clarified instructions in its examination manual and in its training programs with respect to this issue. More specifically, FDIC examiners are instructed not to list deposits in the examination report as simply "volatile" but to instead outline the characteristics that indicate they are less than stable.

Member Hanrahan suggested that, even though the relationship between market rates and Treasury obligations broke down for a while, intuitively it makes sense to consider a formula pegged at some percent of Treasury obligations. He also asked whether the FDIC is considering a "greater of" test between market rates and Treasury obligations. Member Turner observed that the third-party survey sponsored by the FDIC captures rates offered, not rates paid. Member Epstein also asked, for purposes of setting rate caps, whether the FDIC is considering using another wholesale funding source that takes regional competitive differences into effect, such as Federal Home Loan Bank advance rates. In response to member questions, Ms. Miller noted that the FDIC is considering a range of options and that proposed revisions to the regulation will be open for further comment when the NPR is issued.

Next, Mr. Henning provided an update regarding interagency work to improve the effectiveness and efficiency of BSA/AML supervision. He reminded the Committee that the FDIC, along with the Fed, the National Credit Union Administration, the OCC, and the Financial Crimes Enforcement Network, issued a *Joint Statement on Risk-Focused BSA/AML Supervision* on July 22, 2019 (FIL-43-2019). The statement was the third in a series with the first, *Interagency Statement on Sharing Bank Secrecy Act Resources*, issued October 3, 2018, and the second, *Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing*, issued December 3, 2018.

The July 2019 statement focuses on improving the transparency underlying the agencies' risk-focused approach for planning and conducting BSA/AML examinations. The agencies tailor BSA/AML examination plans and procedures based on the unique risk profile of each bank. The extent of examination activities necessary to evaluate a bank's BSA/AML compliance

program generally depends on the risk profile of the bank and the quality of processes implemented by the bank to identify, measure, monitor, and control risks and to report potential money laundering, terrorist financing, and other illicit financial activity. By way of example, Mr. Henning touched on a bank's independent testing and auditing. That is, if an institution has a strong risk assessment process for understanding its risk and implements a program, and the program is independently tested and audited on an ongoing basis, then examiners can leverage that information to scope examination activities and resources. Mr. Henning also described a new FDIC work program that examiners began using in 2019 to better identify the characteristics of an institution from a BSA/AML standpoint. He concluded his remarks by noting that an interagency working group meets every week, and the agency principals meet each month, all with the goal of improving BSA/AML supervision.

Mr. Davis then introduced Anthony Lowe, FDIC Ombudsman, Office of the Ombudsman ("OO"). Mr. Lowe indicated that he was going to discuss an initiative to review the FDIC's guidelines for filing appeals of material supervisory determinations.

Mr. Lowe noted that the current process was implemented in 1995 as required by the Riegle Community Development and Regulatory Improvement Act of 1994; the FDIC established the Supervision Appeals Review Committee ("SARC") to hear and decide appeals; and the proceedings of the SARC are governed by *Guidelines for Appeals of Material Supervisory Determinations*, issued by the Board of Directors. Mr. Lowe reported that the volume of appeals has represented less than one-tenth of one percent of the aggregate risk management and consumer compliance examinations conducted by the FDIC from 2014 through 2018. The OO believes that low number could be attributable to: (1) an absence of disagreement with examination findings, (2) a lack of industry knowledge about, or confidence in, the appeals process, or (3) an unwillingness to potentially upset a relationship with the examination team. Mr. Lowe acknowledged that the FDIC has not conducted a formal study at this point, but suggested the low number could be due to a combination of all three factors. He advised that the FDIC anticipates that bank staff will engage with examiners during the course of examinations in an effort to resolve any disagreements and escalate disagreements to a management level official if needed. The FDIC recognizes that informal discussions will not always result in a mutually agreeable solution, however, and the appeals process is therefore available. Mr. Lowe then described, for the benefit of the Committee, each step in the process.

Mr. Lowe announced that, in light of the historically low volume of appeals filed as well as anecdotal information from regional ombudsmen, the OO is launching a two-pronged strategy designed to solicit input with respect to the current appeals process. First, the FDIC plans to issue a "request for information" or "RFI," posing questions and soliciting suggestions with respect to all avenues banks use to resolve disputes, whether with examiners, regional office staff, division directors, or the SARC. Second, the OO intends to host a series of "listening sessions" around the country in an effort to gather suggestions to enhance the appeals process.

Chairman McWilliams then referred to the FDIC's "post-examination survey" which is issued to each bank after an examination. She advised that some bankers she met suggested that they declined to complete the survey due to concerns that the results would be shared with the examination team even though the FDIC assures bankers that answers are anonymous. Because

of these concerns, she said, the survey is now being issued by the OO. Overall, Chairman McWilliams advised the Committee that the FDIC can, and will, make constructive changes to the process and to the SARC membership.

Director Gruenberg pointed out that the appeals process is essentially a dispute resolution process when the examiner and the institution have different views with respect to a material supervisory decision. By definition, an appeal all the way through the process to the SARC – an FDIC Board-level committee – is going to be an extraordinary case. Continuing, Director Gruenberg suggested that the number of such cases will necessarily be low. The real test of the system, he suggested, can be found in the earlier stages of the process; how are differences resolved in a more informal way, optimally between the examiner and the institution, but at the regional director level as well? In some sense, he suggested, this is where most of this work is going to get done. Thus, to gauge whether the process is working, we should not only look at appeals going to the division director or to the SARC, but also look at appeals made at the regional director level. Evaluating the regional review process is an important avenue to judging the review process as a whole. He speculated that the large majority, if not the vast majority, of issues are going to be resolved at that level. The overall objective should be a system where there is an understanding by all parties that taking issues up the ladder is part of the process; an institution has to believe it is entitled to have a difference of opinion.

Following Director Gruenberg's remarks, Member Turner commented that the FDIC's first line of defense in the effort to prevent antagonistic relationships between the FDIC and insured institutions is the examiner-in-charge; the most effective examiners-in-charge are those who have a judicial temperament, as opposed to a prosecutorial temperament.

Mr. Davis then introduced Brandon Milhorn, Deputy to the Chairman and Chief of Staff, to discuss the activities of the Subcommittee on Supervision Modernization (the "Subcommittee"). Mr. Milhorn explained that the Subcommittee supports the larger Committee by considering how the FDIC can leverage technology and refine processes to make the examination program more efficient, while managing and training a geographically dispersed workforce. The Subcommittee brings together community banks, former examiners, former regulators, and technology experts to review the FDIC examination process in the context of technology and training and process improvements.

Mr. Milhorn reported that in order to establish a comprehensive understanding of the examination process, the Subcommittee's first meeting focused on educational topics. Subsequently, the Subcommittee divided into multiple working groups. The examination workflow, data, and technology analysis group is looking at the safety and soundness and compliance examination process in an effort to understand how people and technology are deployed. A second group is working to identify the most challenging components of an examination. Based on initial discussions, the loan review component is the most complicated and challenging component. A third group is focusing on a "sentiment" analysis (*i.e.*, contextual mining of text) and open source information, asking whether the FDIC can use available information from outside sources to scope examinations more effectively. A fourth group is looking at the Call Report in order to evaluate how the data we collect is used, and whether – if the mechanism for collecting information is changed – it would change the amount and type of

data needed. Groups are also analyzing examiner deployment, training, and the more effective use of the Division of Insurance and Research to support examination teams.

Mr. Milhorn advised that the aim is to reimagine how the FDIC supervises its institutions. The Subcommittee is asking fundamental questions about the process; urging participants to think about the process in new ways; and considering how FDIC efforts could encourage community banks to adopt new technologies or establish new back office approaches that not only make banks more competitive but also make FDIC supervision more effective. Mr. Milhorn then discussed the application of seed money and the FDIC Tech Lab.

Member Kimbell observed that it is essential for examiners to meet and interact with banking staff, to see the bank's surroundings and its community, and to observe what the bankers deal with day-to-day. He urged the FDIC not to move to a situation where there is no face-to-face interaction. Mr. Milhorn clarified that offsite versus onsite review is not the goal. Rather, the goal is to identify risk early, work with the institution to mitigate risk early, and in the process make supervision more efficient. He agreed that there is no substitute for direct engagement with an institution. Member Paine then discussed the number of community banks and the size of banks represented on the Subcommittee. She cautioned that new technologies could be cost-prohibitive for smaller institutions already dealing with the costs of online banking and information technology ("IT") security. Mr. Milhorn assured the Committee that the FDIC understands cost constraints. He emphasized that a goal of the project is to make it cost effective for small institutions that decide to adopt more technology; however, the FDIC will not mandate the use of technology.

Chairman McWilliams also emphasized that the idea is not to mandate the use of certain technologies. Instead, the focus is to determine what tools banks need from the FDIC and what tools the FDIC could utilize to get to that place. Director Gruenberg then returned to Member Paine's earlier observation that the substantial majority of the institutions supervised by the FDIC have assets under $500 million. Thus, he agreed, issues of technology adoption become particularly sensitive and challenging. He suggested there is room to make the examination process more efficient and hopefully less costly to the bank and the agencies, while recognizing that at the heart of the examination is a supervisory process in which people deal with people and make judgments about the management capabilities or the individuals running the institutions. Mr. Milhorn agreed, noting that the question is, "How can we use technology to enhance that engagement process and make the engagement more effective?" Ultimately, the Subcommittee will suggest improvements to make the supervisory process more effective, more efficient, and less burdensome on community banks, and submit its recommendations to the full Committee for consideration and forwarding to the FDIC as appropriate.

Mr. Davis announced that the meeting would recess for lunch. Accordingly, the meeting stood in recess at 12:16 p.m.

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The meeting reconvened at 1:30 p.m. that same day, at which time Mr. Davis introduced the presenter of the next discussion topic, "Minority and Community Development Financial

Institutions," as Ms. Betty Rudolph, National Director for Minority and Community Development Banking. She advised that she would discuss the FDIC's research report entitled, "*Minority Depository Institutions: Structure, Performance, and Social Impact*" which was released in June 2019; recent FDIC initiatives; creation of a new Subcommittee; and Opportunity Zones.

She explained that a minority depository institution ("MDI") is one that is either 51 percent minority owned or where a majority of the board of directors is minority and the institution serves a minority community. She noted that the MDI industry consists of 148 institutions with $238 billion in total assets and that the median size of an MDI is $336 million in assets. She then recognized the three CEOs of MDIs on the Committee: Mr. Dakri of Wallis Bank; Mr. Kenneth Kelly of First Independence Bank; and Mr. Beshear of First Security Bank and Trust Company.

Turning to the research report, she advised that on June 25, 2019, the FDIC released a study that explored changes in MDIs, their role in the financial services industry, and their impact on the communities they serve. The study period covered 2001 to 2018. A key conclusion of the study is that MDI financial performance has significantly improved over the past five years, particularly in terms of revenue generation and loan performance. The study highlighted that from 2001 to 2018, the number of MDIs declined 9.1 percent, while the number of community banks declined by 42.2 percent. Over this same time period, the number of Asian American, Hispanic American and Native American MDIs increased, while the number of African American MDIs declined by more than half and now represents 15 percent of all MDIs at year-end 2018. In addition, the study concluded that MDIs originate a greater share of mortgages to borrowers in low- and moderate-income census tracts and to minority borrowers than non-MDIs. Ms. Rudolph noted that one of the statutory goals for the MDI program is to preserve the minority character in the event of mergers/acquisitions. She was therefore pleased to report success in preserving the minority character of institutions in cases of voluntary mergers as well as bank failures. In fact, over 85 percent of the assets of failing MDIs over an 18-year period have been absorbed by other MDIs.

Next, Ms. Rudolph noted that the FDIC set ambitious goals for 2019 in terms of increasing engagement and collaboration with MDIs. She outlined several initiatives. She described roundtable discussions that will be hosted by the FDIC to highlight opportunities for larger, non-MDIs to collaborate with MDIs, and she mentioned a pilot roundtable held in June in the New York region. She noted that CRA experts at the FDIC are working with the OCC and the Fed to determine if the performance evaluation can be amended to acknowledge MDI partnerships. Ms. Rudolph mentioned the 2019 interagency MDI conference that the FDIC hosted where MDIs had an opportunity to network, and she touched on webinars that the FDIC is conducting to explain the process for bidding on a failing institution. Additionally, Ms. Rudolph mentioned the FDIC's robust technical assistance program which provides an MDI's board of directors an opportunity to meet with the regional director at least once a year. The final initiative that Ms. Rudolph discussed was a new MDI Subcommittee of the Advisory Committee on Community Banking. She advised that the Subcommittee would focus exclusively on identifying tools and resources to support MDIs as well as barriers to profitability and the ability to serve customers. Staff is currently drafting an initial membership list; and the Subcommittee

would report back to the Committee as a whole. Ms. Rudolph agreed with Member Dakri's observation that it would be helpful to clarify for larger banks and non-MDI banks the specific benefits of collaborating with an MDI.

With respect to Opportunity Zones, Ms. Rudolph explained that the Zones were part of the 2017 Tax Cut and Jobs Act; approximately 8,700 Zones have been approved; and there is no specific role carved out in that tax law for banks, but it does present an investment opportunity. She noted that the FDIC is exploring how we can facilitate ways for banks to take advantage of these investment opportunities. Member Williams noted that cities could identify and recommend areas for inclusion in these Zones, but few did, probably because few understand the program, what it is for, who qualifies, and how it works. Ms. Rudolph answered that the FDIC hopes to serve as a resource by posting information on the FDIC website and highlighting the issue. She emphasized that this is not a federal program; instead, it focuses on state and local laws and tax incentives. The discussion concluded with the Committee Members agreeing that it would be helpful to delve into the issue at greater length at the next Committee meeting.

Mr. Davis introduced the presenters of the next panel, "Updated Money Smart Financial Education Materials," as Luke Reynolds, Chief, Outreach and Program Development, Division of Depositor and Consumer Protection ("DCP"); and Bobbie Gray, Supervisory Community Affairs Specialist, DCP. Mr. Reynolds highlighted that the Money Smart Financial Education Program includes materials for various groups: young people, young adults, adults, older adults and small business. He advised that the Money Smart for Adults Program was refreshed in 2018 and is the most recently updated product. He noted that Money Smart for Adults was refreshed to take into account the latest research as well as feedback from institutions that have used the program over the years. He reviewed the 14 modules that make up the Money Smart for Adults Program. The modules cover a range of issues, including basic bank products and services; spending and saving plans; debt management; housing decisions; and preparing for a disaster. Mr. Reynolds also touched on the Money Smart for Older Adults Program. He reported that Money Smart for Older Adults recently won an award from the American Society of Aging and that over one million copies of that product have been ordered.

Next, Ms. Gray discussed resources available to support those delivering the Money Smart Financial Education Program. These resources include: instructor supplements consisting of a comprehensive presentation guide and real-world scenarios to promote inclusion of individuals with disabilities; promotional flyers and cards; promotional videos; and virtual training through webinars. With respect to delivery of the program, Ms. Gray highlighted examples of how some banks use the Money Smart Program. Some financial institutions partner with community groups and government entities to deliver the program at various locations including homeless shelters, substance abuse centers, and libraries. She advised that the "Money Smart Alliance Program" includes over 1,200 members who partner with the FDIC to teach and promote the program. The FDIC provides resources and free training to instructors, and the instructors deliver the training to the community.

Member Shettlesworth shared with the Committee his experience working with an organization dedicated to helping people pay off car title loans. The key to the program's success was assigning mentors to assist the individual with developing and following a financial

plan. He advised that the Money Smart Program and train-the-trainer materials can enhance the organization's outreach efforts. In response to questions concerning an entrepreneurship component to the program, Mr. Reynolds advised that, with respect to young people, two modules in the Money Smart for Young People Program – the curriculum targeted to grades 9 to 12 – are about entrepreneurship. With respect to adult students, the Money Smart for Small Business curriculum, developed in partnership with the U.S. Small Business Administration ("SBA"), focuses on entrepreneurship. Member Walker then raised the issue of student loans. Mr. Reynolds advised that the Money Smart for Adults content includes information regarding student loan debt, while the program targeted to young people provides an overview of options and helps people connect with the more expansive tools available from the Department of Education and the Consumer Financial Protection Bureau.

Mr. Davis announced that the meeting would take a mid-afternoon break. Accordingly, at 2:17 p.m. the meeting stood in recess. The meeting resumed at 2:32 p.m.

Mr. Davis introduced the presenters of the panel, "FDIC and U.S. Small Business Administration Collaboration Efforts," as Lekeshia Frasure, Acting Chief, Community Affairs, DCP; Allen Gutierrez, Associate Administrator, Office of Entrepreneurial Development, SBA; Emerson Hall, Acting Associate Director, DCP; and James Watkins, Senior Deputy Director, RMS.

Mr. Gutierrez highlighted the work of the SBA's Office of Entrepreneurial Development with resource partners such as the Small Business Development Centers, the Senior Core of Retired Executives or "SCORE," and the Women Business Centers. He then outlined recent initiatives, such as the establishment of regional innovative clusters, implementation of an Emerging Leaders plan, and the launch of the Makerspace Training, Collaboration and Hiring ("MaTCH") Pilot Competition. He noted that the agencies work together under the terms of a memorandum of understanding that guides FDIC and SBA collaboration.

Next, Mr. Hall described work performed with the SBA in the FDIC's regions. The FDIC's Community Affairs Program supports the FDIC's mission to promote stability and public confidence in the financial system by promoting economic inclusion and community development initiatives. The Community Affairs team includes about 35 community affairs specialists throughout the country. He noted that the primary purpose of these specialists is to assist financial institutions in developing those strategies that are responsive to the credit, service, and investment needs of the communities in which they operate. Mr. Hall commented that the SBA has exceptional programs and then provided several examples of FDIC and SBA collaboration. These included a small business lunch-and-learn workshop in the Atlanta region; a rural Illinois small business roundtable hosted by the Chicago region; a "Mississippi Meet the Microlenders in the Delta" workshop hosted by the Dallas region; an Omaha small business lending forum held in the Kansas City region; a small business lending forum held in rural Maryland; and a Washington state banker roundtable. Mr. Hall reflected that, when he is asked why the FDIC is involved in this type of work, he explains that we understand that access to capital is what spurs the economy and that a healthy community sustains a healthy bank. Moreover, the FDIC strives to obtain tangible, measurable results with the goal of transforming communities and changing lives.

Mr. Hall then directed the Committee's attention to the Money Smart for Small Business Program ("MSSB"). He explained that it was developed jointly by the FDIC and SBA; includes 13 modules addressing topics related to starting and managing a business; helps financial institutions collaborate with small business owners; and encourages the development of meaningful relationships between financial institutions and aspiring or existing small business owners. Mr. Gutierrez interjected that the SBA recently launched "Lender Match," a free online referral tool that connects small businesses with participating SBA-approved lenders.

Member Dakri suggested it would be helpful to provide bank examination staff with training to better understand SBA products, including that a portion of a loan might be unguaranteed, but that does not mean it is unsecured. Mr. Watkins responded that many FDIC-supervised banks have active SBA programs. Consequently, the FDIC has implemented internal programs to develop subject-matter experts in areas such as oil and gas lending and real estate lending. Moreover, the FDIC has regular discussions to identify trends and issues that might impinge on the guaranteed portion. Therefore, the FDIC's expectation for examiners is that, when they review the books of an institution, the institution will have sufficient loan policies and procedures in place to underwrite the loans as if they didn't have a guarantee. He explained that the guarantee provides an extraordinary benefit such that even if there is a criticism of the loan, as long as the bank is following its requirements for the SBA, the portion of the loan that is guaranteed would not be subject to criticism. While that is the substance of the training, he advised that FDIC staff would certainly take back the suggestions to ensure that examiners have a better understanding.

Mr. Davis then introduced the final topic of the day, "Update on FDIC Efforts Regarding De Novo Institutions." Mr. Watkins advised that the FDIC approved two new banks since the Committee's March 2019 meeting. The FDIC is currently reviewing 13 applications for deposit insurance. The FDIC is actively engaged with a number of prospective organizers, and some of those groups have submitted draft applications under the FDIC's *Review Process for Draft Deposit Insurance Proposals* announced though FIL-82-2018 (Dec. 6, 2018). Mr. Watkins emphasized that the FDIC supports the formation of new banks, and staff is available in each regional office to assist organizing groups during the application process. In addition, the FDIC published updated sections of the applications procedures manual with plans to publish remaining sections later in the year. The manual, especially the overview section, serves as an additional aid for organizing groups. The FDIC also updated its delegations of authority so that regional directors can approve deposit insurance applications for traditional community bank applications, as well as any change in business plans, without prior consultation with the Washington Office. He reported that the FDIC plans to issue a question-and-answer document clarifying that a specific physical address is not required at the time a deposit insurance application is filed. These various changes are responsive to feedback received during roundtable events that concluded in the first quarter of this year as well as the RFI on the deposit insurance application process that was issued in December 2018. Mr. Watkins also advised that the FDIC has provided additional application-related information through its website as part of the agency's transparency initiative.

Mr. Davis then thanked the Committee members and the presenters.

There being no further business, the meeting was adjourned at 3:12 p.m.

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Robert E. Feldman
Federal Deposit Insurance Corporation
Executive Secretary
and Committee Management Officer
FDIC Advisory Committee on Community Banking

Minutes

of the

Meeting of the FDIC Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation

July 30, 2019 – 9:00 A.M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.

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Jelena McWilliams
Chairman
Board of Directors
Federal Deposit Insurance Corporation