The FDIC Podcast – Keeping Up with Technology

BRIAN SULLIVAN: Welcome back to the FDIC Podcast, a place to talk about our banks as a way of understanding a bit more about our own money. I'm Brian Sullivan with the Federal Deposit Insurance Corporation and in this episode we're going to talk about the technological wave that is sweeping over our banking system and what that means for you…and for thousands of smaller community banks around this country.

We're not talking about the big international, national or even regional banks. We're talking about that bank with just a handful of branches or maybe even a handful of employees…sometimes located in a single state or even a single town! Those small town banks that provide loans and other financial services to rural communities and lower income urban areas where, if not for these banks, there may not be a bank at all.

Joining us to help understand both the opportunities and the challenges of this tech explosion is Brandon Milhorn. Brandon who is no stranger to the IT world. He's held senior positions in the private sector, he's worked in leadership positions at the U.S. Senate and even the Central Intelligence Agency. And he's currently the Chief of Staff at the FDIC…who, along with Chairman Jelena McWilliams and many others…is leading a charge to embrace new technologies in banking. Brandon, thank you so much for being with us.

BRANDON MILHORN: Brian, thanks for having me.

BRIAN SULLIVAN: How serious is this tech gap and why should we care?

BRANDON MILHORN: I think the tech gap is important for all of us really to consider because community banks play such an important role in the fabric of America. You know, our banking system is much different from the systems in other countries. We have thousands of banks and these community banks have relationships in their small towns with the small businesses, with families who have lived there and preserving that is an incredibly important topic for us and technology is going to allow these community banks to continue to compete. Over the last several years, we've seen a pretty significant decline in the number of community banks and Chairman McWilliams sees technology as a mechanism for them to continue to compete in this market, not just among themselves or in their small communities, but to reach out to new customers, to use technology, to offer new products and services in a way that maybe they haven't in the past, but still to maintain those relationship bank services that are so critical to community banks.

BRIAN SULLIVAN: And so Chairman McWilliams launches FDiTech. Tell us how about that.

BRANDON MILHORN: So FDiTech is our is our tech lab. The mission is twofold. One, to foster innovation in the financial services sector in the market, to encourage that and second, to make sure that the FDIC’s own operations utilize technology efficiently and effectively. And we see these missions as related. If our banks are more technologically proficient, they're using more technology for their operations. That allows us to use more technology from a supervisory standpoint which makes our supervision more efficient.

BRIAN SULLIVAN: Because you've got to make sure these banks are safe.

BRANDON MILHORN: Right. I mean, ultimately the mission of the FDIC is to ensure financial stability in the United States, promote the safe and sound operation of banks, and to make sure consumers that are using those banks are protected.

BRIAN SULLIVAN: Right, because most folks think the FDC is just insuring their deposits, but you go behind the scenes to make sure that….

BRANDON MILHORN: Right. We're not just an insurer, we're engaged in the ongoing supervision of banks to make sure that their risk profiles and their insurance are aligned.

BRIAN SULLIVAN: Recently, the FDIC asked banks and tech companies and the public at large to offer comments about how the agency can speed the adoption of new technologies throughout the banking sector. How do you intend to do that?

BRANDON MILHORN: Yeah, so we put out an RFI – a request for information – that proposes a third-party certification model. But before I really get into detail on the RFI, it's probably important to talk about why that's so important, particularly for our community banks. The chairman's gone on a 50-state listening tour across the United States. We've talked to banks, we've talked to community groups, we've talked to technology companies and the one thing that they've said is this, we need more effective ways to onboard new technology. When you get a tech company that wants to go into a bank, banks are required to manage that relationship, the risk associated with that relationship. And so, they do due diligence on the tech company itself. They want to look and do due diligence and review.

BRIAN SULLIVAN: Because that’s people's money after all…

BRANDON MILHORN: Right and they want to review the technology that the company is going to bring to the bank. That's a costly process, particularly for community banks who may lack the on-staff expertise. They may not have a CFO and the tech officer might also be the teller you know, at night. So we've got to accommodate their needs in the space because if we want them to be dynamic, if we want them to be able to use technology to compete, we have to find a way to cut cost and reduce unnecessary regulatory burden in the space. And also, just the operational uncertainty that can go along with bringing on these new companies. So, taking it back to our RFI, what we've heard from the tech companies and the banks is this can be a costly process. If I'm a tech company and I go to one bank, their process is one way. You go to a second bank, their process is a little different. Everyone wants a little bit different and there's no standardization. So that adds to the cost and complexity of a tech company coming in and really competing in this market. So, our RFI is designed to do two things. It's designed to provide some standardization to that due diligence and onboarding process and designed to give banks some ability to rely on a certification process that tells them this vendor meets our standards. This technology meets our standards. And when I say ‘our standards,’ in the RFI, what we've laid out is a public-private partnership between the regulators, the FDIC and the private sector to develop these standards. So, we all sit at the same table. We develop standards for due diligence. We develop standards for particular technologies or models, and then there'd be certifying organizations empowered by the SSO to review vendors who voluntarily decided to comply.

BRIAN SULLIVAN: So the standard setting organizations would provide people a seal of approval as it is so certified certifying. Okay. And that could, once you have that, then it just cuts time and time is money.

BRANDON MILHORN: Well, and it provides standard…

BRIAN SULLIVAN: …right, so you don't have to keep doing it over.

BRANDON MILHORN: Right. So if you're a community bank that's on the fence or nervous about the regulatory impact of bringing a new technology on or concerned about the impact of integrating that technology, you'd be able to look at that certification and recognize that one, it's a standard that the FDIC and other regulators hopefully were involved in developing. And there's a certifying and auditing function that stands behind that certification, so you'd be able to onboard that vendor, onboard that technology and effectively. Now, Brian, you'd also still have to manage the relationship with that vendor. Ultimately, a bank is going to continue to be responsible for its operations and how its technology affects its customers. But having that, the ability to rely on that certification at the beginning of the relationship just gets rid of some of that uncertainty and cuts some of the costs for these institutions. And we think that can help get those institutions that might have been nervous or may have been a little anxious over the hump and allow them to bring in new technology.

BRIAN SULLIVAN: Now earlier you had talked about a trend in this country that’s been going on for quite some time. We have fewer banks generally, fewer community banks, fewer minority owned and managed banks…we call them ‘minority depository institutions. Lots of consolidation taking place and people have probably noticed it with their *own* banks. It used to be one bank and now it’s another bank. Is this a life or death moment for these institutions…get on board with this tech age or else?

BRANDON MILHORN: That's a great question and I think I'd answer it this way. If you can use technology to cut your cost of operations, if you can use technology to reach new customers with new products and services, you can continue to compete in the marketplace, right?

It's not as easy as walking down to a branch anymore, if I'm a customer. It used to be you'd walk down to the branch, you'd go in, you'd get your product, your checking account, your loan, you do that in the bank and you'd go home with your loan. Now, the competition is incredible and it's not just from banks. There are non-banks in this mix too. And they're all vying for your consumer's attention. They're all offering products and services.

What I think *we* offer, what *our* FDIC-supervised banks offer is we can bring that technology in, provide competitive products and services, we're also and our banks are doing it in an environment that's supervised by the FDIC, looking out for not just the safety and soundness of the institution, but the consumers themselves.

BRIAN SULLIVAN: What are you doing to make sure the FDIC itself, as a *supervisor* of these banks, keeps pace?

BRANDON MILHORN: Thanks. You know, our supervisory model is really, at this point-in-time supervisory model right now. Now for our larger banks, we have ongoing interactions with them. We get good data from them on a more regular basis but for the bulk of our institutions, our supervision is point-in-time and by that I mean we get quarterly call reports from the banks. We do a 12 or 18-month exam of all our institutions based on their size, complexity and health. When you want a dynamic system where banks are bringing in new products and services, they're bringing on new technologies, you have to have a supervisory system that matches that. And you need to move away from a more point-in-time model. I think of it as a continuous engagement model where you're working along with the institution to identify risks early and take actions to mitigate risk early, instead of waiting until the end of an exam cycle to….

BRIAN SULLIVAN: 18 months later, when you go, oh, we have a real problem….

BRANDON MILHORN: Right. And technology, Brian, can empower that. We can use technology to form the foundation for that. But that's really tricky. As I noted earlier in our conversation, our banks, our community banks come in all different shapes and sizes. Some are very tech forward. They've adopted technology, they're using it, it's part of their operations. Some of our smaller banks, still keep their loan forms in triplicate in their vault. And we have to be able to supervise all those institutions, but if we can set up mechanisms that encourage institutions to adopt technology, think of our RFI, think of the work that we've done on third-party partnerships and in other areas, then we can also use technology to supervise them more effectively.

BRIAN SULLIVAN: So, Chairman McWilliams and you seem to taking this issue pretty personally. I recall some comments she made to the University of Chicago Law School where she made this very point…

CHAIRMAN JELENA MCWILLIAMS: So, a significant part of my focus as the FDIC Chairman has been bridging the gap between those who 'belong' and those who do not. Because the FDIC is a bank regulatory agency, we have approached this issue from the perspective of financial services. We know that individuals from low- and moderate-income communities are often the least likely to have the very banking and financial services they need most. With respect to minority communities in particular, despite meaningful improvements in recent years, the rates for black and Hispanic households who do not have a checking or savings account at a bank remains substantially higher than the overall unbanked rate.

BRIAN SULLIVAN: Is it safe to say that making the adoption of new technology easier for these smaller banks is about making sure *everyone* has access to banking? This is almost a financial inclusion aspect…

BRANDON MILHORN: Oh, absolutely. Particularly as you think about things like alternative data where you're taking information that's not normally part of a person's credit file such as the amount of income that's coming in, when it's coming in and using that to make credit decisions provides an enormous enabler for our low- and moderate-income customers who may not normally have had access to standard credit score-based products. And that's technology that enables that. And if they can access our system, if they can be part of the institutions that provide access to credit that helped them buy a home, invest in a business, you know, as the chairman just recently said, it gives a sense of belonging in their communities that may not exist without those financial services. So yeah, I know she takes that very personally based on her background. And I'm just excited about the ability to use technology to reach those customers because not only it will cut banks costs, it provides more opportunities for competition, opportunities to lower costs for these consumers. It just creates a more vibrant and dynamic marketplace and all supervised by the FDIC. So, yes, I'm a little bit excited about technology. I'm excited about what it can do for our banks and for their customers. That's what I'm excited about.

BRIAN SULLIVAN: Brandon Milhorn, thank you so much for joining us.