Community Bankers of Michigan Regulatory Dispatch

June 26, 2024

Timely news and resources community bankers can use

to better stay on top of a rapidly changing world.

OCC Report Highlights Key Risks in Federal Banking System

WASHINGTON—The Office of the Comptroller of the Currency (OCC) reported the key issues facing the federal banking system in its Semiannual Risk Perspective for Spring 2024.

The OCC reported that the overall condition of the federal banking system remains sound. However, the maturing economic cycle may cause consumer headwinds. It is important for banks to continue identifying material risks and their interconnected impacts. Continuous risk management improvement remains appropriate as this allows banks to guard against complacency.

The OCC highlighted credit, market, operational, and compliance risks, as the key risk themes in the report. Highlights from the report include:

- Credit risk is increasing. Commercial real estate sectors, primarily the office sector and some multifamily property types, are experiencing stress due to a higher rate environment and structural changes. Office and multifamily loans, particularly those with interest-only terms, set to refinance over the next three years pose additional risk. Sticky inflation and elevated interest rates may increase consumer financial stress in some households and weigh on overall consumption growth.

- From a market risk perspective, net interest margins (NIMs) are under pressure due to strong deposit competition. Trends observed, however, indicate that pressure on funding costs and NIMs may be nearing a peak. The future direction, timing, and extent of rate movements and uncharted depositor behavior present risk management challenges. Wholesale funding usage continued to grow albeit at a slower pace going into 2024. Investment portfolio depreciation improved but unrealized losses remain elevated as banks continue to increase asset liquidity and interest rates remain elevated.

- Operational risk is elevated. The financial industry is responding to an evolving and increasingly complex operating environment. Cyber threats continue as malicious actors target the financial services industry and their key service providers with ransomware and other attacks. Increasing digitalization, new and innovative product and service adoption, and third-party use increase bank operating environment complexity creating both opportunities and risks. Continued check and wire transfer fraud and increased payment fraud incidents both underscore the importance of fraud risk management.

- Banks are operating in a dynamic banking environment because of changing customer needs and preferences related to products, services, and delivery channels. Risks are compounded if products and services, including changes, are not delivered or implemented in a fair and equitable manner. It remains important for banks to maintain a compliance risk management framework that is commensurate with their risk profiles and capable of growing and evolving as their risk profiles change. Fraud continues to be significant risk for banks. Effective processes to prevent, identify and file suspicious activity reports on fraudulent activity in a timely manner remain important to protect both banks and consumers. As banks work to process checks and other payments in a safe, fair, and efficient manner, check and wire fraud, and P2P transaction scams have become more prevalent. The OCC continues to assess banks' Community Reinvestment Act performance under the 1995/2021 regulatory framework.

The report highlights the necessity of firmwide resilience efforts as risks may be interconnected and events could simultaneously affect multiple risk categories. It is crucial that banks establish an appropriate risk culture that identifies potential risk, particularly before times of stress. Each stress event may vary (e.g., operational, liquidity, credit, compliance, and other) and resiliency implications need to be proactively considered. Prudent planning from a firmwide perspective can enhance a bank's ability to maintain operations, remain financially sound, and service customers in times of stress.

The report covers risks facing national banks, federal savings associations, and federal branches and agencies based on data as of December 31, 2023, unless otherwise indicated. The report presents information in four main areas: the special topic, operating environment, bank performance, and trends in key risks. The report focuses on issues that pose threats to those financial institutions regulated by the OCC and is intended as a resource to the industry, examiners, and the public.

Comment: A year ago in the same report, the OCC warned banks to 'guard against complacency' and nothing there has changed. By addressing these risks and enhancing risk management practices in areas addressed, community banks can better navigate the evolving financial landscape and continue to serve their customers effectively.

CBM Insights

Q: We have a question as to what name the bank should use when opening an individual's account. We have some who think that we should use the name on their SSN card. They say this because that is the name the IRS matches when reporting interest to the IRS. Others think we should use the name that is on the driver's license. Does the state have anything that can help us determine which name to use?

A: Logically, the SSN card is as good a source of verification of an account holder's TIN, but that is it. A state issued driver's license is verification of the account holders name, address and date of birth.

Since all states have adopted REAL ID standards and that uses the 'full legal name' as a documentation standard to obtain a REAL ID, that would be the name to use for the account holder to open the account and for CIP purposes.

Visit your state's driver's licensing agency website to find out exactly what documentation is required to obtain a REAL ID. At a minimum, you must provide documentation showing: ***1) Full Legal Name;*** *2) Date of Birth; 3) Social Security Number; 4) Two Proofs of Address of Principal Residence; and 5) Lawful Status.*

States may impose additional requirements, so check with your state's driver's licensing agency website, before visiting them in person, for additional guidance and assistance.

Source link.

The account holder can call themselves anything on the account itself if your system accommodates that. For example, John James Smith may go by ‘JJ Smith’ and he may want his checks and debit card to say ‘JJ Smith.’

Items of Interest

Bank Management

	FRB Speech by Governor Kugler on the Economic Outlook and Monetary Policy (06/18/2024) – *A second reason for my optimism about continued disinflation is slower growth in the costs faced by businesses. Among those, nominal wages are a big part of total costs in the services sector. Nominal wage growth has continued to trend down, consistent with a labor market where supply and demand are coming into better balance. Of course, as a general matter, I want to see Americans experiencing strong wage growth, but for that wage growth to be sustainable, it must be consistent with our inflation target. Notably, as inflation has come down, real wages have been rising and now exceed pre-pandemic levels, which means that the purchasing power of workers has also been increasing. But at the same time, we have seen slowing growth in nominal labor costs. For example, the 12-month increase in average hourly earnings has been running just above 4 percent over the past couple of months after peaking at around 6 percent in 2022 and falling more or less steadily since then. The latest readings compare with an average of around 3 percent a year before the pandemic, when inflation was running below our 2 percent goal. Wage moderation is especially evident in some service sectors for which labor is a large share of costs. If this moderation in wage growth continues, it will soon be at levels consistent with price stability. And I note that the market-based services inflation measure I mentioned earlier tends to move closely with wage growth.*
	CSBS FDIC Needs Clearer, More Transparent Bank Merger Policy Proposal (06/17/2024) – Washington, D.C.: The FDIC’s proposed bank merger policy would create more challenges than benefits for the banking industry, especially for community banks, state regulators said in a comment letter. New charters and beneficial mergers are crucial components of a dynamic and competitive banking system. However, the FDIC’s proposed merger policy would add uncertainty, cost, and burden to an already complex and lengthy merger application process. “The FDIC should get back to basics – the specific requirements of the Bank Merger Act – and establish an unbiased and objective policy that promotes healthy mergers,” said CSBS President and CEO Brandon Milhorn. “Sound merger policy, and additional support for de novo charter activity, are essential for consumers and a vibrant financial system.” Mergers are an important business option for banks seeking to enter new markets, invest in new technology, and keep up with evolving market and economic conditions. Discouraging mergers could threaten the stability of individual banks and the broader financial system, especially with rising costs and federal regulatory burdens. For some community banks, particularly in rural and underserved areas, a merger may be the key to survival. The FDIC should establish clear and transparent standards for merger and de novo applications to encourage bank growth and investment in local communities.
	OCC Announces Enforcement Actions for June 2024 (06/17/2024) – WASHINGTON—The Office of the Comptroller of the Currency (OCC) released enforcement actions taken against national banks and federal

	savings associations (banks), and individuals currently and formerly affiliated with banks the OCC supervises. The OCC uses enforcement actions against banks to require the board of directors and management to take timely actions to correct the deficient practices or violations identified. Actions taken against banks include: Formal Agreement with Touchmark National Bank, Alpharetta, Georgia, for unsafe or unsound practices, including those relating to the bank's strategic planning, board and management oversight, liquidity risk management, interest risk management, credit risk management, audit, and information technology. (Docket No. AA-SO-2024-25) ***Comment: This is noteworthy because reading enforcement actions of late, there seems to be more criticism of bank strategic plans. Other than the usual comments, this passage seemed particularly telling: "product and service development, and market segments that the Bank intends to promote or develop,..." Does your bank have a Change Management Plan?***
	FRB Speech by Governor Bowman on Innovation in the Financial System (06/17/2024) – *Openness to Innovation - Earlier I mentioned the importance of ensuring the regulator understands the new technology. But while education is an important first step, it often runs headlong into regulatory skepticism. Often, a regulator's first reaction to proposed innovation in the banking system is not one of openness and acceptance but rather suspicion and concern. The use of emerging technology and innovation may require a change in policy or supervisory approach. It also very often requires regulatory feedback—ideally before the innovation is introduced or after it has been integrated by a bank and is reviewed during the supervisory process.* *To be sure, skepticism is an understandable first reaction to new activities, particularly those that someone seeks to conduct within the regulatory perimeter after its integration. For regulators, the challenge is one of balance. How do we allow innovation to flourish, with sensible supervision and regulation, so that our financial system can reap the gains of innovation while preserving safety and soundness and consumer compliance?* *Regulators need to ask whether we have considered the intended and unintended outcomes of a new innovation, and do the benefits of the new technology outweigh its risks? Would the introduction of a new technology or innovation in the banking system require updating our regulatory framework to incorporate clear oversight? Who should have responsibility for oversight, and what roles do we see for different regulators at both the state and federal level?* *Transformational technology requires clear, consistent, and transparent guardrails and expectations to govern the activities that are allowed into the regulated financial system. Where current regulation does not contemplate a new activity, should it be acceptable for financial agencies to regulate the activity through supervision and enforcement alone? Or should congressional action address the treatment of these activities in the financial system?* *I think it is vital that regulators work with banks through all stages of the innovation life cycle to achieve that baseline understanding I mentioned before. But it is incumbent on regulators to fight the temptation to say "no" and resist new technology and instead focus on solutions—how can we mitigate the risk of new technology? What benefits will technology bring to the financial system? How can we provide clear regulatory expectations?*

BSA / AML

	Joint Anti-Money Laundering and Countering the Financing of Terrorism Program Requirements (06/20/2024) – The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation (FDIC), and the National Credit Union Administration (NCUA) (collectively, 'the Agencies' or 'Agency' when referencing the singular) are inviting comment on a proposed rule that would amend the requirements that each Agency has issued for its supervised banks (currently referred to as "Bank Secrecy Act (BSA) compliance programs") to establish, implement, and maintain effective, risk-based, and reasonably designed Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT) programs. The amendments are intended to align with changes that are being concurrently proposed by the Financial Crimes Enforcement Network (FinCEN) as a result of the Anti-Money Laundering Act of 2020 (AML Act). The proposed rule incorporates a risk assessment process in the AML/CFT program rules that requires, among other things, consideration of the national AML/CFT Priorities published by FinCEN. The proposed rule also would add customer due diligence requirements to reflect prior amendments to FinCEN's rule and, concurrently with FinCEN, propose clarifying and other amendments to codify longstanding supervisory expectations and conform to AML Act changes. ***Comment: The long-anticipated reconciliation of the CTA with existing CDD will hopefully help with the beneficial ownership collection requirements but does nothing for SAR and CTR thresholds.***

Deposit / Retail Operations

	FTC How to Keep Hackers Out of Your Accounts (06/17/2024) – Like most people, you probably use a strong password to protect your accounts. But hackers can steal your passwords through phishing attacks. And scammers can buy passwords exposed in a data breach. The best way to protect your accounts? Use two-factor authentication. More and more sites and apps are offering two-factor authentication. But you usually have to turn it on. So, spend a few minutes to turn it on now – and save yourself the countless hours it'll take to recover a hacked account later. ***Comment: You are never done educating and alerting your customers. Continue to find creative ways to share this type of information.***

Human Resources

	No news to report this week.

Lending

	Joint Quality Control Standards for Automated Valuation Models (06/20/2024) – The OCC, Board, FDIC, NCUA, CFPB, and FHFA (collectively, the agencies) are adopting a final rule to implement the quality control standards mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) for the use of automated valuation models (AVMs) by mortgage originators and secondary market issuers in determining the collateral worth of a mortgage secured by a consumer's principal dwelling. Under the final rule, institutions that engage in certain credit decisions or securitization determinations must adopt policies, practices, procedures, and control systems to ensure that AVMs used in these transactions to determine the value of mortgage collateral adhere to quality control standards

	designed to ensure a high level of confidence in the estimates produced by AVMs; protect against the manipulation of data; seek to avoid conflicts of interest; require random sample testing and reviews; and comply with applicable nondiscrimination laws. ***Comment: The final rule requires that mortgage lenders and secondary market investors apply if they rely on AVMs to conduct random sample testing and review of those models. With this new rule, the agencies are trying to address both higher costs due to appraiser shortages and the concerns about bias in home valuations.***
	FFIEC Home Mortgage Disclosure Act: FFIEC's 2024 'A Guide to HMDA Reporting: Getting It Right!' (06/17/2024) – The Guide is a valuable resource for assisting all institutions in their HMDA reporting. It includes a summary of responsibilities and requirements, directions for assembling the necessary tools, and instructions for reporting HMDA data. Highlights The 2024 guide discusses: • institutions covered by Regulation C. • transactions covered by Regulation C. • information that covered institutions are required to collect, record, and report. • requirements for reporting and disclosing data. ***Comment: The 'Rosetta stone' for HMDA filers. Share this information with your staff and ensure they are using the most recent guide.***
	Bloomberg Warning Signals Are Flashing for Homeowners in Texas and Florida (06/14/2024) – In some Texas and Florida cities, foreclosures are rising, suggesting early signs of distress in the once booming housing market. The likely reasons: rising property taxes and insurance premiums and higher interest rates that make it increasingly difficult for homeowners struggling with mortgage payments to sell their properties or refinance their way out of trouble. ***Comment: Keep abreast of these delinquency upticks and ensure you are monitoring for any early signs of distress with customers.***

Technology / Security

	CISA and Partners Release Guidance for Modern Approaches to Network Access Security (06/18/2024) – CISA, in partnership with the Federal Bureau of Investigation (FBI), released guidance, Modern Approaches to Network Access Security, along with the following organizations: ▪ New Zealand's Government Communications Security Bureau (GCSB); ▪ New Zealand's Computer Emergency Response Team (CERT-NZ); and ▪ The Canadian Centre for Cyber Security (CCCS). The guidance urges business owners of all sizes to move toward more robust security solutions—such as Zero Trust, Secure Service Edge (SSE), and Secure Access Service Edge (SASE)—that provide greater visibility of network activity. Additionally, this guidance helps organizations to better understand the vulnerabilities, threats, and practices associated with traditional remote access and VPN deployment, as well as the inherent business risk posed to an organization's network by remote access misconfiguration.

CISA and its partners encourage leaders to review the guidance to help with the prioritization and protection of remote computing environments.

For more information and guidance on protection against the most common and impactful tactics, techniques, and procedures for network access security, visit CISA's Cross-Sector Cybersecurity Performance Goals. For more information on zero trust, visit CISA's Zero Trust Maturity Model.

Selected federal rules – proposed

Proposed rules are included only when community banks may want to comment. Date posted may not be the same as the Federal Register Date.

06.11.2024 CFPB Prohibition on Creditors and Consumer Reporting Agencies Concerning Medical Information (Regulation V) Summary: The Consumer Financial Protection Bureau (CFPB) is seeking public comment on a proposed rule amending Regulation V, which implements the Fair Credit Reporting Act (FCRA), concerning medical information. The CFPB is proposing to remove a regulatory exception in Regulation V from the limitation in the FCRA on creditors obtaining or using information on medical debts for credit eligibility determinations. The proposed rule would also provide that a consumer reporting agency generally may not furnish to a creditor a consumer report containing information on medical debt that the creditor is prohibited from using. **DATES: Comments must be received on or before August 12, 2024.**