Community Bankers of Michigan Regulatory Dispatch

July 27, 2023

Timely news and resources community bankers can use

to better stay on top of a rapidly changing world.

FDIC ESTIMATED UNINSURED DEPOSITS REPORTING EXPECTATIONS

The FDIC observed that some insured depository institutions (IDIs) are not reporting estimated uninsured deposits in accordance with the instructions to the Consolidated Reports of Condition and Income (Call Report). For example, some institutions incorrectly reduced the amount reported to the extent that the uninsured deposits are collateralized by pledged assets; this is incorrect because in and of itself, the existence of collateral has no bearing on the portion of a deposit that is covered by federal deposit insurance. Additionally, some institutions incorrectly reduced the amount reported on Schedule RC-O by excluding intercompany deposit balances of subsidiaries.

STATEMENT OF APPLICABILITY:
This Financial Institution Letter does not impact institutions with less than $1 billion in total assets that do not report estimated uninsured deposits.

Comment: While limited to banks with over $1 billion in total assets, it's a good reminder that the agencies' concern for uninsured deposits is not going away anytime soon.

Items of Interest

Bank Management

	OCC Hosts Risk Governance and Capital Markets Workshops in Cincinnati (07/20/2023) - WASHINGTON—The Office of the Comptroller of the Currency (OCC) will host two workshops August 8-9 in Cincinnati for directors, senior management, and other key executives of national community banks and federal savings associations. The Risk Governance: Improving Effectiveness workshop on August 8 combines lectures, discussion, and exercises to provide practical information for participants to effectively identify, measure, monitor, and control risk. The workshop also focuses on the OCC's approach to risk-based supervision and major risks in the financial industry. The Capital Markets: Keeping Current workshop on August 9 is designed to help bank leadership better understand balance sheet management risks such as interest rate risk, liquidity risk, and risks associated

with the investment portfolio. Additionally, the workshop will discuss quantifying balance sheet risk related to assets and liabilities.

The Risk Governance workshop fee is $99. Participants receive course materials, supervisory materials, and lunch. The half-day Capital Markets workshop fee is $49, which is waived for participants also attending the previous day's workshop.

To register online and view the schedule and locations of other workshops, visit the OCC's website. For additional questions about the workshops, please contact the OCC Bank Director Workshop Team at (202) 649-6490 or bankdirectorworkshop@occ.treas.gov.

Comment: These workshops are excellent opportunities for national bank directors and senior management to learn directly from the OCC presenters.

FRB G.17 (07/18/2023) – Industrial production declined 0.5 percent in June for a second consecutive month but advanced 0.7 percent at an annual rate for the second quarter as a whole. Manufacturing output moved down 0.3 percent in June but rose 1.5 percent in the second quarter. In June, the indexes for mining and utilities fell 0.2 percent and 2.6 percent, respectively. At 102.2 percent of its 2017 average, total industrial production in June was 0.4 percent below its year-earlier level. Capacity utilization stepped down to 78.9 percent in June, a rate that is 0.8 percentage point below its long-run (1972–2022) average.

Comment: The statistics in this release cover output, capacity, and capacity utilization in the U.S. industrial sector, which is defined by the Federal Reserve to comprise manufacturing, mining, and electric and gas utilities.

BSA / AML

No news to report this week.

Deposit / Retail Operations

FRB Announces The Fednow® Service Is Now Live (07/20/2023) – The Federal Reserve on Thursday announced that its new system for instant payments, the FedNow® Service, is now live. Banks of all sizes can sign up and use this tool to instantly transfer money for their customers, any time of the day, on any day of the year.

"The Federal Reserve built the FedNow Service to help make everyday payments over the coming years faster and more convenient," said Federal Reserve Chair Jerome H. Powell. "Over time, as more banks choose to use this new tool, the benefits to individuals and businesses will include enabling a person to immediately receive a paycheck, or a company to instantly access funds when an invoice is paid."

To start, 35 early-adopting banks and credit unions, as well as the U.S. Department of the Treasury's Bureau of the Fiscal Service, are ready with instant payments capabilities via the FedNow Service. In addition, 16 service providers are ready to support payment processing for banks and credit unions.

When fully available, instant payments will provide substantial benefits for consumers and businesses, such as when rapid access to funds is useful, or when just-in-time payments help manage cash flows in bank accounts. For example, individuals can instantly receive their paychecks and use them the same

	day, and small businesses can more efficiently manage cash flows without processing delays. Over the coming years, customers of banks and credit unions that sign up for the service should be able to use their financial institution's mobile app, website, and other interfaces to send instant payments quickly and securely. As an interbank payment system, the FedNow Service operates alongside other longstanding Federal Reserve payment services such as Fedwire® and FedACH®. The Federal Reserve is committed to working with the more than 9,000 banks and credit unions across the country to support the widespread availability of this service for their customers over time. A list of early adopters with instant payment capabilities is attached. Additional information is available on the Federal Reserve Financial Services website. ***Comment: It is worth noting that only 'depository institutions' can access FedNow. Under current rules third-party payments companies must rely on bank partners to access payment rails.***

Human Resources

	No news to report this week.

Lending

	FRB Furthering the Vision of the Fair Housing Act - Vice Chair for Supervision Michael S. Barr (07/18/2023) – Fair Lending Implications of Innovation - As our financial system evolves, it is critical that we adapt our application of the Fair Housing Act and ECOA to deal with technological change and other developments. The digital economy has produced alternative data sources, some of which can provide a window into the creditworthiness of an individual who does not have a standard credit history. And new artificial intelligence techniques such as machine learning have the potential to leverage these data at scale and at low cost to expand credit to people who otherwise can't access it. While these technologies have enormous potential, they also carry risks of violating fair lending laws and perpetuating the very disparities that they have the potential to address. Use of machine learning or other artificial intelligence may perpetuate or even amplify bias or inaccuracies inherent in the data used to train the system or make incorrect predictions if that data set is incomplete or nonrepresentative. There are also risks that the data points used could be correlated with a protected class and lack a sufficient nexus to creditworthiness. For instance, digital redlining in marketing—the use of criteria to exclude majority-minority communities or minority applications—is one risk, and it has already been the subject of several settlements, including one several years ago involving the NFHA and Facebook. Digital redlining may result if advertisers select their audiences based on a characteristic that is correlated with protected characteristics. New technologies can also result in "reverse redlining," or steering in the advertisement of more expensive or otherwise inferior products to minority communities. These risks are amplified when a model is opaque and lacks a sufficient degree of explainability—the degree to which the bank can understand how data, variables, and other features inform the credit decisions.

	While banks are still in the early days of adopting artificial intelligence and other machine learning technologies, we are working to ensure that our supervision keeps pace. Through our supervisory process, we evaluate whether firms have proper risk management and controls, including with respect to those new technologies. ***Comment: In a nutshell, Gov. Barr cautioned that the 'digital economy' comes negative implications where technologies can potentially violate the fair lending laws and may perpetuate existing disparities and inaccuracies, among other things.***

Technology / Security

	CISA Develops Factsheet for Free Tools for Cloud Environments (07/17/2023) - CISA has developed and published a factsheet, Free Tools for Cloud Environments, to help businesses transitioning into a cloud environment identify proper tools and techniques necessary for the protection of critical assets and data security. Free Tools for Cloud Environments provides network defenders and incident response/analysts open-source tools, methods, and guidance for identifying, mitigating, and detecting cyber threats, known vulnerabilities, and anomalies while operating a cloud or hybrid environment. Cloud service platforms and cloud service providers (CSPs) have developed built-in security capabilities for organizations to enhance security capabilities while operating in cloud environments. Organizations are encouraged to use the built-in security features from CSPs and to take advantage of free CISA- and partner-developed tools/applications to fill security gaps and complement existing security features. Publicly available PowerShell tools exist to all network defenders for investigation and aid of an organization's security posture, including: ▪ Cybersecurity Evaluation Tool (CSET), ▪ Secure Cloud Business Applications (SCuBA) Gear, ▪ Untitled Goose Tool, ▪ Decider, and ▪ Memory Forensic on Cloud (JPCERT/CC). ***Comment: The Treasury Department warned of the potential risks to the banking sector as financial institutions continue to use cloud-based technologies in a April 2023 report. The Treasury report focused on six thematic areas that, if left unaddressed, may detract from the potential benefits of cloud services in the financial sector. These concerns are: (1) insufficient transparency to support due diligence and monitoring by financial institutions; (2) gaps in human capital and a lack of tools to securely deploy cloud services; (3) exposure to potential operational incidents, including those originating at a cloud service provider; (4) the potential impact of market concentration in cloud service offerings; (5) dynamics in contract negotiations given market concentration; and (6) the fragmented regulatory framework. To combat these concerns, the Treasury plans to convene a group of financial regulators to study the cloud-computing industry and recommend ways to manage the potential risks.***
	CISA Oracle Releases Security Updates (07/17/2023) - Oracle has released its Critical Patch Update Advisory, Solaris Third Party Bulletin, and Linux Bulletin for July 2023 to address vulnerabilities affecting multiple products. A remote attacker can exploit some of these vulnerabilities to take control of an affected system. CISA encourages users and administrators to review Oracle's July 2023 Critical Patch Update Advisory, Solaris Third Party Bulletin, and Linux Bulletin and apply the necessary updates.

Comment: Share these alerts with your IT staff.

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.

PROPOSED RULE WITH REQUEST FOR PUBLIC COMMENT

05.01.2023 CFPB Residential Property Assessed Clean Energy Financing (Regulation Z) - SUMMARY: Section 307 of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA) directs the Consumer Financial Protection Bureau (CFPB or Bureau) to prescribe ability-to-repay rules for Property Assessed Clean Energy (PACE) financing and to apply the civil liability provisions of the Truth in Lending Act (TILA) for violations. PACE financing is financing to cover the costs of home improvements that results in a tax assessment on the real property of the consumer. In this notice of proposed rulemaking, the Bureau proposes to implement EGRRCPA section 307 and to amend Regulation Z to address how TILA applies to PACE transactions to account for the unique nature of PACE. **DATES: Comments must be received on or before July 26, 2023.**

06.21.2023 Interagency Guidance on Reconsiderations of Value of Residential Real Estate Valuations- SUMMARY: The OCC, Board, FDIC, NCUA, CFPB, and FHFA (collectively, the agencies) invite comment on a proposed 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 proposal, the agencies would require institutions that engage in certain credit decisions or securitization determinations to 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. **DATES: Comments must be received by August 21, 2023.**