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BANK APPLICATIONS AND REGULATORY APPROVALS UNDER A NEW "CONTROL" PARADIGM

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P R O C E E D I N G S

MR. KIM: Thank everyone for coming. Our topic is regulatory approval under a new control paradigm. So, if you would like to hear about frictionless commerce, and who wouldn't? That would be downstairs. I'll introduce our panel very briefly. On the far right, Mark Van Der Weide, General Counsel, The Federal Reserve. Next to him is Stephen Lybarger, Deputy Comptroller for Licensing, of the OCC. Then Kieran Fallon, Senior Deputy General Counsel with PNC. Then last, Matt Musselman with JP Morgan.

So, to start right in with a control proposal. Mark, this is directed to you. I think, as most of you know, in April, the Fed issued a control proposal. It's relevant in a lot of respects, be it investments in banks by private equity firms, activism, investments by banks and fintech companies, and so forth. So, Mark, if you could just sort of kick it off by talking about what led the Federal Reserve to issue this proposal and what are your objectives here?

MR. VAN DER WEIDE: Thanks, Richard. As usual, the remarks I have today are my own, and they may or may not reflect the views of the Board. I think there are 4 mutually re-enforcing, interlocking objectives behind the control proposal. When they were issued, I thought there were 3, but there’s 4 now.

The first is a logical outgrowth easily from the other 3. The first is transparency enhancement, as Randy Corrals has rhapsodically mused in public. The current control doctrine of the Fed are something of a body of secret law, gnostic knowledge that’s passed down from high level priests to lower level priests to acolytes in the Feds’ temple. It’s known only to them and to a handful of Wall Street lawyers.

MR. KIM: Somewhat ornate, I think he said.

MR. VAN DER WEIDE: Also ornate, yes, I would agree with that too. We want to democratize that body of law and put it out in the public domain and some like disinfectant, all that jazz. So, that’s the first part of it. The second objective is to move to a more rulish approach. Our decision making and control historically has been, I think more ad hoc and more case by case than it needs to be. We would like to have a clear set of rules which we think will better achieve an objective of treating like cases alike. Third, we'd like to speed things up. To get an answer to a control question today, you often need to spend several months talking to your private counsel and then several months negotiating through the Fed bureaucracy to get an answer. We don't think that's good social welfare enhancing stuff a large chunk of the time. We would like to have a set of clear, transparent rules, so that banks can make a quicker assessment of what's legal and what's illegal. Lastly, we'd like to do some target liberalizations of our control precedents. There are a few places over the decades where I think we've been a little too strict and we want to provide a little bit of adjustment in a few places on that dimension. Getting a lot of comments on the proposal. I think Kieran and Matt will talk through some of the main places where the industry didn't think that we quite achieved everything that we should have achieved, but we're going through all the comments now. I think there will be a final rule in the not too distant future.

MR. KIM: Just to be clear, your next step would be a final rule and you would issue another proposal.

MR. VAN DER WEIDE: That’s my expectation.

MR. KIM: Kieran and Matthew, do you want to commence the cross examination?

MR. FALLON: Let me start off by saying we are strongly supportive of the effort and the objectives that the Fed did with the control proposal. Having that sort of more transparent, clearer framework, I think will benefit everyone. I think it will benefit organizations as we look to make business decisions as to whether we’re going to make an investment and what the consequences of that investment would be. Bringing to light a lot of the secret lore that has been hidden within the Fed for some period of time has been great. Certainly there were aspects of the proposal and I do think, objectively speaking, were something of a liberalization from past rules. There are still some areas, though, that I think are safe to say are pretty stringent and much more so than I think one would need to be in order to identify those relationships that would give a bank holding company or any company the ability to have actual control or a controlling influence over the investee. The area, in particular, that drew a lot of comments during the process, and I think that's key to the effectiveness and the workability of the framework going forth to business relationships. So, under the proposal, for example, if an institution of a bank holding company has 15 to 24.9 percent of the voting equity in an organization, the proposal would allow you to have only business relationships that would constitute no more than 2 percent of the revenue or expenses on a reciprocal basis. It could be 2 percent of the revenue or expenses of the investor or 2 percent of the revenue or expenses of the investee.

I think a number of sort of worrisome aspects in there, one is the review of the percentage of the revenues of the investor company, if you think about it. The purpose of the controlling influence determinations to see whether the investor can exercise influence over the investee, the first company and the second company, in the parlance of the proposal. If the second company is doing business with the first company, such that it is a big percentage of the first company's revenue, then theoretically, all that does is would give the second company greater influence over the investor, rather than vice versa, so we really think it doesn't make sense to look at the percentage of the revenue or the expenses of the first company. It really is, to the extent that it's meaningful at all, it should be based just upon the investor company.

Secondly, looking at expenses doesn't seem to really make a lot of sense. Revenues is a much better metric there. If you think about what an expense metric would incent is, you have an investment in 2 companies, exact same size, exact same revenue. One company has lower expenses and therefore is more profitable than the second company. Well, of course, if you have the same level of business relationships are more likely

To be in a control position over the more profitable company because their expenses are going to be lower. So, your business relationships are going to be a much lower advantage than the 2nd companies. From a prudential matter, why are we trying to incent companies to make investments in less profitable companies rather than in more profitable companies. Third, I think the level at which this test is set is just absurdly low, in all deference to the Fed, but 2 percent of revenues of a company would make you, if you think everybody’s sort of equivalent, you could be one of the investor second companies’ top 50 customers, top 50. I think it’s hard to believe that a company at that level of business relationship would really have any meaningful influence, particularly given the fact that business relationships are really a poor way to attempt to exercise a controlling influence versus director relationships or covenants or things like that. Typically you enter into business relationships with a company because their product is better or more efficient. It helps you produce revenues for yourself and meet your customer demand. If you are going to try and use business relationships as a way to really exercise a controlling influence, you are to some extent cutting off your nose to spite your face, because if you are doing business with this company because they have the best product, you are not going to really be inclined to say, oh, I’m going to stop using you because I want you to do “X” for me because again, all you’re doing is you’re hamstringing your own ability to do your business and meet your customers' needs.

Finally, there was some indication it was ambiguous in the proposal as to whether, what time of revenue would be considered in deciding whether you met the threshold. I think it's important that any threshold be limited to any revenues that are between the 2 companies themselves. That's actually what you contract, to the extent you're looking for sort of simplicity and transparency. That is key. If you begin to start thinking, well, you have to subtract revenue that the company may get from your customers -- so, you have shared customers -- that gets really difficult to do, unless you're sharing customers lists. To the extent you're worried about control, you don't want the 2 companies to be sharing customer lists. So, there's really a lot of reasons why the relationship should be based upon what the revenues, what the business relationships are directly between the 2 companies. That's what you can control, to use the phrase. That's really what it should be based upon, but other than that, I thought the proposal was very good.

MR. KIM: Mark, did you want to respond to the points, specifically about business relationships, or should we just let Matt continue with the onslaught.

MR. FALLON: Why don't you just let Matt go?

MR. MUSSELMAN: Not necessarily an onslaught, but obviously another area that the industry commented on was the calculation of total equity under the proposal. So, under the proposal, total equity being one of a variety of control factors. You're looking at voting equity, directors, business relationships as Kieran just discussed. Total equity is another one of the factors. However, it's the -- now, there is the question of whether total equity gives you any influence over the second company at all, but taking the Fed's proposal that it is one of the factors, the calculation of total equity under the proposal is looking at a gap balance sheet and a historical accounting calculation of total equity. For companies that may have little or negative retained earnings over time, at the time that the first company is putting some money in there, the investment could under this calculation method constitute an outsized amount and potentially almost any investment would exceed -- I'll take the first category -- 33 percent total equity limitation in the first year of the Fed's proposal. So, through BPI, it proposed some alternative calculation methodologies to try to address that. I think it would again come up on most early an early stage companies and it could effectively prohibit any investment by bank holding companies in those institutions because it would trip presumption. I guess you could go through a process of approaching a fed and explaining why, but again, for the timing and other reasons, it may just act as a barrier to making any investment in that company.

MR. KIM: Did you want to comment?

MR. FALLON: Sure, although I wasn't really listening for the last 7 minutes.

MR. MUSSELMAN: You stopped when we said we supported the objectives.

MR. FALLON: Exactly. So, the business relationship issue and the total equity issue are 2 of the most common, frequent comments that we did get on the proposal, and as we internally gestate on those comments in the coming months, we're going to spend quite a bit of time reassessing what we did on total equity and business relationships. It can be challenging to take certain elements of an ad hoc framework and try to be rulish about them, and it can sometimes create suboptimalities and common interest. I pointed out some situations, hearing Matt tonight, today, hearing some of those suboptimalities occur. As we go through and try to move it to final, we're going to try and see if we can keep to our generally rulish objective but have fewer false negatives, false positives in the framework.

There may be some areas where we decide we just went too far in the rulishness and we need to keep a case by case by case approach because of some of these fact specific issues, but we are going to see if we can find a way to keep as much of the rulishness as we can, but filter down the rough edges as much as we can to get it to good.

MR. KIM: Mark, I do have one question for you from the audience via the app. How will the final rule impact older investments, analyze existing Framework and relatively, how should banks be thinking about control investments made in this period before the final rule.

MR. VAN DER WEIDE: Yeah, that's a good question. In addition to the 2 issues that Kieran and Matt focused on today, total equity in business relationships, some of the other key comments that we've gotten are we didn't nail it on investment funds and how to determine control in investment funds. Another issue that's come up is how to deal with pre-existing investments where the Fed is given some kind of a case by case blessing and whether they get grandfathered into the new framework. These again are the issues that we are going to consider pretty carefully as we move to final, and I hope on this particular question, the kind of grandfathering transitional question will provide more clarity in the final rule or the final preamble about that.

For people who are making investments tomorrow or the next day, unfortunately there is not a lot of guidance I can provide. We're in a little bit of a transition period for the Fed's control framework, but the proposed rule is not yet final. So, don't count on that at this point and come talk to us if you need more clarity.

MR. KIM: Steve, do you want to talk about the control from the OCC's perspective and how does the OCC approach control and will it be relevant if this proposal is final as respect to your thinking?

MR. LYBARGER: Well, generally most of our large banks and mid-sized banks have holding companies, so really the controllers should defer to the bank holding company. Probably the exception to that is Mount Zion whose collapse its holding company into the bank and could be a potential issue for us. We have had investment funds approach us with regards to potential of their investments, and if they cross the threshold of a change in control. What we've done is try to work with that from a preemptive perspective. In other words, work on them entering into passivity agreements and trying to move that proves that. I think one thing that we understand is that generally their investing companies that are probably traded. And various activities can occur that change your ownership up and down and have a framework that allows for that kind of flexibility. But it isn't the same level of concern or issue. Recently we've had some inquiries about this with us and how we approach it. The one thing is we will allow you to make an argument to rebut presumption of to control without having to start the notice process and filing IBFR's and that kind of thing. We'll address the presumption first. If you don't rebut the presumption, then we'll take you through the notice process. We think that's an effective way to approach it and it tries to conserve resources on your side and people not having to disclose financial information, that in the end may not be relevant to the discussion.

MR. KIM: Great. Thanks. Steve, if we could stay with you and shift the topic to bank M&A, can you talk about what you're seeing at the OCC? Anything interesting recently?

MR. LYBARGER: Well, not as interesting as BB&T and SunTrust. You know, right now it's pretty steady and we're seeing our particularly smaller companies trying to assess where their role may be in the banking environment going forward. I think part of that is do we need size or do we think we can't compete in them looking for merger partners. Obviously under current statutory frameworks, our larger banks are limited in what they can do in the M&A world. I think some of the M&A we will see will be more of the mid-sized companies, but it's steady. Nothing that I see trends going one way or the other. I think it will be continually driven by business needed and expectations.

MR. KIM: Again, Mark, same question for you from your prospective.

MR. VAN DER WEIDE: I think steady is a pretty good word. I think I could use it too. If you look at just M&A application volumes that we've received, project forward what we saw in the first half of 2019 through the entire year of 2019, it would be the lowest number of transactions, number of application that we've received for bank M&A since the crisis. Before 2019, 2018 was the lowest number. Before 2018 was the lowest number, 2017 was the lowest number. So, it's been a steadily slowly declining number of applications on bank M&A that we've gotten over the last few years. So, at least for now EGRRCPA does not appear to have unleased the hounds of bank M&A. It appears to be still the numbers of transactions are steadily declining. There have been some bigger deals in the last year announced or consummated, Fifth Third and BB&T and SunTrust and First Horizon, Iberia, but numbers of transactions have been on a steady downward sloping curve. BB&T, SunTrust was kind of the big Kahuna for 2019, but I think that also kind of reflects a steady analysis by the Fed consistent with all of our long-term historical precedents for how we analyze the statutory factors. It was the biggest bank M&A deal since the crisis, $65 billion transaction value, $450 billion consolidated assets for the Proforma Firm, 8th largest bank holding company, 6th largest commercial bank holding company. Merge of equals, somewhat interesting. You don't see a lot of those in bank M&A or M&A more generally. Hopefully that will go well.

Anti-trust issues were present in the application. The two firms had somewhat overlapping operations in the Southeastern United States. We required 30 branches to be divested, about $250 billion in deposits. SunTrust had some compliance issues. So, there was a simultaneous enforcement action against SunTrust at the same time we approved the BB&T application. Important to us was that BB&T committed to abide by the terms of the enforcement action that we did with SunTrust. BB&T will also be putting its UDAP compliance program in place at the combined firm and UDAP was the area where SunTrust stepped, did not do so well. That was kind of the big transaction for the year. A few more large transactions, but transaction volume steadily declined.

MR. KIM: Okay. I guess in terms of application processing, more generally, it seems like deals are getting approved more quickly by both of your agencies. Can you talk about that a bit? First of all, is this a sustainable trend? What have you done to sort of speed up the process? Steve, can we start with you?

MR. LYBARGER: I think the main thing, one reason you're seeing that, is – I do a lot of work with Amy. Amy was there, and how we deal with public comments, and the fact is evaluating applications for merger should be based on existing records and conclusionary information. I think one of the things we were struggling with is when you get a public comment and there are allegations made of potential wrongdoing, particularly when it's based on a group or individual's analysis of come to data and they're suggesting a certain thing. I think we got ourselves caught up in some way to think we have to run that to ground and have some conclusionary information. In sort of watching that, what I started realizing is in the licensing setting you could spend 6 months; you could spend 9 months, but you're never going to have a conclusionary basis to know whether what their allegations are factual or are not. What we started realizing is the licensing environment is not the environment. It has to get over to our supervisory office. It has to get scoped into an activity, and our supervision folks need to do the work that's necessary to determine if there is facts, and if there is an issue or concern within the supervisory environment, we have all the tools and corrective actions that need to be dealt with. I think that's gone a long way. It's the other thing that I've kind of driven with the staff and the supervisory staff, the recommendations. You've got to deal with the record now, and that's kind of the driving force. Ii think we also realized that when you guys enter into these transactions and agreements, their value can be implicated on us not acting well. The value can go away. There is also significant impacts on the target. Once you announce that, we know that employees of that target, vendors of that target, have to start thinking about their future and whether they play. If we don’t get these done or if they fall apart, we could be putting a weaker institution back into the system which is not what we want to do.

MR. MUSSELMAN: At that side, I would say the data would suggest that our processing time for bank M&A deals is not much different in 2019, say, than 2015. There’s been a pretty, pretty steady average processing time for applications from 2015 forward. That’s about 60 days is the average processing time, 40 days it the median processing time. The one area where we have made some advancement in improving the processing time in applications is kind of similar to where Steve started. In applications where we get an adverse comment, we have been able to reduce the processing time, but those are a pretty small percentage of the deals that we get. I think roughly over the last 5 years, maybe 6 to 8 percent of bank M&A applications the Fed get protested.

But in that small subset of applications, we have made some material improvements in the way we process those applications. Part of that, I think, is more faithfully executing on a long-term policy that we've had that distinguishes between substantive adverse comments and non-substantive adverse comments. Substantive comments are ones where there are facts to back up the claims in the comment and situations where the commenter is making a claim that we have not seen before recently and already analyzed and already come to the conclusion that it wasn't, didn't have enough merit to it. So, we have been trying to distinguish between substantive and no-substantive comments and we've done a lot to improve processing time where the comments we've received are non-substantive. We also have a couple of other projects in train that I would think over time would speed up and expedite some of our applications. We did a bunch of new, a cluster of new delegations to the reserve banks this summer for some commitment relief, actions, some red K proposals, and additional chunk of anti-trust cases, a few other areas. I think over time that should have at least a small impact in expediting processing. If we get the control framework right, I think going forward that might also make things move faster, should reduce time on some deals between, might expedite the announcement time of the deal, might expedite the amount of time between announcement and filing of the application and then might expedite the processing time of the Fed and the application. So, going forward, I see other green shoots of possibilities of more expedition.

MR. LYBARGER: I want to add onto Mark's comment about it being substantive. If it is substantive, you've got facts that we can run to ground and make conclusions, it's going to be dealt with in the licensing environment, but if that's not the case, it's got to go over to the supervisory office. One of the things we are doing is screening comments up front and if it isn't substantive, we're actually going back to the commenter, giving him the opportunity to provide some additional facts without extending out our time frames at all or extending comment periods, but we'll give them that opportunity and if they do take it into consideration. If they don't, we're going to work it into a scope supervisory activity.

MR. KIM: Thanks. Do you want to talk about your perspective? What’s been your recent experience in filing applications, not just for M&A, but more generally?

MR. FALLON: I think in this case, I won’t talk about specific applications, but I’ll address my comments to Steve and the OCC. In this case we have a very good relationship with the licensing department. I’ve found in my dealings with them to be very proactive, talking about what they want to see. They want to see a, b, c and d, and whatever the particular application is, and they’re proactive about making sure that it’s going to be included in whatever we submit. Then assuming we provide them all that information, they will have the information they need to make a decision relatively quickly. They process things relatively quickly, whether it’s a positive or a negative conclusion, but processing it very quickly. So, I think at least my experience has been with the licensing department, that they make the process easier and streamlined by being proactive, that they can get to the substance of the application and focus on that.

MR. KIM: Kieran, do you want to comment on that?

MR. FALLON: Yes. I would just one area where the OCC has taken some action that has significantly streamlined the process for engaging new activities proved to be very helpful. So, I believe it as last year, the OCC issued an interpretative letter, 1160, relating to commodity derivative transactions and the OCC had found many, many years ago that engaging in customer driven, commodity driven transactions was a bank permissible activity. It was part of the intermediation function, et cetera, but over time, a process had been kind of developed where in order to begin trading in a new index or a new underlying commodity, regardless of how closely connected it was to what you were doing before. Maybe you're trading, helping your customers execute derivatives on West Texas crude, and now you want to rent crude. There had been a process where you had to go to the OCC, request approval formed as a supervisory non-objection in order to do that. I think quite rightfully the OCC took a new look at that and said well, this is fundamentally a bank permissible activity, whether you're doing it on West Texas intermediator or rent crude. So, what Steve had kind of indicated, to the extent there may be supervisory concerns, maybe you don't have the right internal controls related to whatever, those are things that can be dealt with through the supervisory process. It doesn't need to be dealt with through sort of the extant approval process. They changed the framework for those kinds of activities. Now, you provide notice to the OCC and the examiner in charge. It's a matter of good business practice. We would have always done that anyway, to keep our local team of the OCC informed, yet provide them with information on sort of how we've gone through the approval process to make sure we've got the right systems and policies and procedures to handle that. That just allows you to respond to your customer needs in a more faster way and we're hopeful that that becomes a model for maybe further actions by the OCC in other areas where there is that kind of approval process, that maybe there's the opportunities to streamline that in the coming year.

MR. VAN DER WEIDE: I would maybe just add something you've said, Kieran, is that something we've found as well is that -- not that we would not keep our local – we would keep our local exam team that we were going to file a licensing application, but I can see from the OCC's licensing department, they're very focused on making sure that the information is flowed and that it's sent back to the exam team as well. So, you can see both parts, the licensing group and the exam team, working together to keep themselves informed on whatever the application is.

MR. KIM: Is there anything, anything at all, Matt, that you'd like to say about the Fed's application process?

MR. MUSSELMAN: After Gremlee's by leave, the Section 4 stuff, that was a huge benefit. Just simply post notice, I don't think you can make it any more streamlined than that.

MR. KIM: Mark, we would have to extend our time if we talked about all the great things the Fed has done. We do have one question for you. Should we expect public hearings on large applications in banking going forward, like what BB&T and SunTrust had in the spring?

MR. LYBARGER: So, in each case, we make a case by case decision about whether to do public hearings on a bank M&A application. Many factors go into that decision, including the size of the deal and the relevant, the size and the extent of the public interest in the transaction. I think similar transactions in the future, you'll probably see public hearings, but in each case, we do an ad hoc decision.

MR. KIM: Steve, I guess one more question, on banking. I've heard you say in the past that there's more supervised discretion nowadays when a bank is deemed to be in a penalty box, unable to do bank M&A. I mean, it used to be the case that if you had a CAMELS 3 or a management rating or you had a BSA enforcing action, you shouldn't even bother if you could acquire a bank. What is the OCC's thinking today?

MR. LYBARGER: This thinking has been going on for quite a few years now, but I think what we realize now is just because it's a 3 rating, in and of itself, should not be a no-go. What we've been asked by Mr. Curry, we were asked by Keith Noriega, when he was acting by Mr. Otting is to look at the facts, make some case by case basis. What it really deals with, if an institution just came under a 3 rating for any of those issues, obviously it's going to be difficult for you to move forward because you hadn't had a time to address the particular issue. But if time has passed, if there is a suggestion that an acquisition could help address the deficiency that's in place, we're looking at those factors and taking them into consideration in determining whether a transaction should go forward or not. What we have asked is for the banks to reach out to us with licensing or supervisory folks and we can make an informed decision and assist you where we stand. Before you're signing on the dotted line, you sort of know what the probabilities are, but in and of itself, just because a 3 rating is there, you should not assume that it is not something that can move forward. We're going to look at the facts and whether it makes sense and go forward from there. We are kind of taking that same approach if you've got an unsatisfactory CRA rating. Again, if the transaction would make sense, if it helps address the CRA issue, you know, and the issue with CRA is really unique because CRA exams are generally 3 years apart. We don't want to put a bank in a penalty box for 3 years until the next exam. We actually want to create some motivation to address the deficiency. That's the motivation we can say is look, if you address the deficiency, we're not going to hold you in that penalty box and what we need to know is understand how you've addressed it and where you're at and if it makes sense, go forward as well. Also, we kind of realize with the CRA fact, is that there may be situations where unfortunately the only bank that's available to an acquisition and a failure environment has a 3 rated CRA and from an industry perspective, are we really not going to allow that transaction to go forward? So, we're going to stay open. We're going to look at the facts and determine what's appropriate for the industry and the banking environment in moving forward.

MR. KIM: Mark, is that consistent with the Fed's thinking?

MR. VAN DER WEIDE: It is pretty consistent. We've had kind of a longstanding policy that if you've got a not so good supervisory rating, that it's going to be hard to get an application approved, but there is this kind of mezzanine tranche of not so good, but not horrible ratings where we do a case by case analysist of each transaction. And we look at a number of factors. We provided some transparency around this policy in our SR letter 14-2, but in general, we're going to look at whether the applicant has improved or mediated to any significant extent, but kinds of problems they identified that resulted in the not so good rating or the enforcement action. We're going to look at the size of the acquisition that they want to do. We're going to look at whether the acquisition is something that might distract or exacerbate some of the problems that the firm has. For example, if the firm has a pretty significant BSAAML problems in their international remittances business line, and they want to do an acquisition in the international business, we're probably not going to approve that, but if they want to do a small acquisition in unrelated space and they're making progress on remediating their BSAAML problems, that might get a green light. So, case-by-case decision making in that kind of a mezzanine supervisory assessment area.

MR. KIM: Kieran, would you like to comment, not to suggest you have anything else imperfect. Any Observations?

MR. FALLON: No.

MR. KIM: Next topic. So, I guess moving on to fintech, Steve, can you talk about the fintech charter, especially in light of last month's court ruling that went against the OCC?

MR. LYBARGER: The ruling went against us but I'll be honest. I don't feel like it went against us because we're busy and the industry is interesting because people are anticipating the direction and a lot of the folks that were interested in the charter started realizing the road forward may involve having to be a full service bank with a positive insurance. The number of companies we have talked, we probably talked with Knickerbocker and her group. We talked with folks in my area, about the special purpose charter. I think when they saw sort of the direction that New York was going, that essentially started thinking about their alternatives. We've had a number of conversations with these companies who are looking at do we charter a full-service bank with insurance? Do we acquire an existing insured institution? I think the thing is, they see the value of a charter, the fact that a number of these companies are existing companies operating in multiple states, 20, 30. There's a couple that are probably 50. I had one company, a retail company, down South, that does it's own financing. They're in 8 states. They were coming in and approaching us about a CIBA credit card charter which we haven't done in a long time, but they're seeing the fact that the ability to have a single Federal regulator, not having to do licenses in multiple states, there's value. If that means getting deposit insurance, moving down that route, they're prepared to do that.

MR. KIM: Can you actually talk a little bit about CIBA credit card banks? It felt like the door was closed there for a while with respect to new charters. Is that not so?

MR. LYBARGER: You know, it's really funny because when Amy was the General Counsel, she kept coming to me and said when do we start our moratorium on CIBA credit card banks. I said, well, other than the moratorium that was in place under Dot Frank, to study the issue with ILC, the OCC has never formally had a meritorious on the CIBA credit card charter. The CIBA credit card charter is interesting as that when it first became available, there were a number of retail institutions that took an interest in it and got the charter.

Essentially what happened is they found out what it's like to be regulated by a Federal bank regulator. It isn't exactly what they wanted. I think most of those charters were acquired by city affiliate. There are only a handful of those charters available, but we never said we wouldn't do it. It's just that, I think, like anything, once people had some experience with it and realized it didn't really work the way they thought, they got out. That CIBA charter has always been there. It's one of the available vehicles for companies to move forward. The uninsured trust charter is still available as well. My guess is the industry -- when things are evolving, you really can't stop it. I won't be surprised if folks come to us with some novel approaches and things that we need to think about and consider as possibilities.

MR. KIM: Okay. Thanks. So, Mark, as fintech companies seek bank charters, it's certainly my impression as people back away from the idea of an industrial bank, just so they are so hard to get, they obviously have to form bank holding companies as well. Can you comment on sort of the efforts you've seen in this area?

MR. VAN DER WEIDE: Sure. I'm a little sad because I have no charters to market, but I'll do what I can. That is just totally pro-innovation, by the way. We talk with lots of fintech companies about making controlling and non-controlling investments in banks. We talk with a lot of banks who are trying to make investments in fintech companies or entrance in business relationships with fintech companies. It is a large sub-set of the kinds of things we do in our legal and supervisor functions at the Fed.

We had been spending some time thinking about the special purpose national bank charter that the OCC put out not too long ago. I’d say it was kind of a medium burner project for us to figure out what access such a charter would have to Fed services. I think watching the litigation it’s maybe moved 0back a little further back on the stove. We also watch carefully the ILC debate. It’s again not our decision. That an FDIC and State banking commissioner sort of decision, but we do watch what’s going on there. The Fed has had a traditionally pretty negative fear and loathing sort of a view about industrial loan companies. That’s for a lot of different reasons. In 2016, the Board actually made a public proposal to Congress to eliminate the ILA loophole, which his very consistent with our longstanding views. Our concerns have always revolved around an unholy trinity of anxieties around ILC’s. One is the mixture of banking and commerce that becomes possible. The ILA has a pretty close to full-service bank charter at this point, FDIC insurance, access to the Fed’s discount window, access to the Fed payments, system services. So, it’s a mixture of banking and commerce. It’s lack of consolidated supervision for the holding company of these firms and it’s an unlevel playing field with other banks and thrifts. I think when we watch that situation, we have traditionally had some concerns about it, but very limited power to do anything. It's a clear exception to the bank holding company.

MR. KIM: Anybody else want to comment on this?

MR. MUSSELMAN: One thing I do want to say is some of these proposals that we're talking to today, I mean under the special purpose charter, if they would have been uninsured, they would not have been bank holding companies, but it isn't just a decision about being insured. It's the decision of being a bank holding company. A number of these realized they're going to be bank holding companies and they're going to be insured. So, if this moves forward the way I think, both the Fed and the FDIC is going to be in partnership with us and looking at these.

MR. KIM: Yeah. That's a good place.

MR. VAN DER WEIDE: I mean I could see where you were saying, Steven, that you're hearing from companies talking about, as you said, there's a real difference between what the OCC was proposing with their fintech charter, consequences for the holding company being a bank holding company. They may now, with the uncertainty around the litigation, then seek to talk about a full-fledged charter, but there are real differences at the level of supervision at the parent holding company that they will have to face.

MR. MUSSELMAN: Yes. On the aisles we do think it's a topic and a policy issue that really warrants a lot of attention. We are pleased to see that there are now 2 bills in Congress. One has been introduced by Senator Kennedy, one that's been introduced by Representative Garcia to address the ILC loophole. We are all in favor of competition, but we want competition to be on a level playing field. If an institution or any of these are going to be able to acquire and operate a full service bank, they should be subject to the same consolidated supervision, the capital, the liquidity, other requirements that apply to a bank holding company, the same limitations to our ability to engage in commercial activities, things of that nature. We are hopeful that there gets to be some traction on that in the not too distant future. We are concerned that there are some pending applications with the FDIC currently, including one by Rakuten, which is commonly referred to as the Amazon of Japan. It was 15, 20 years ago when Walmart attempted to acquire an ILC that sort of finally brought some attention to that loophole. Congress stepped in and fortunately just imposed a moratorium, having closed the loophole finally. We have no concerns with the people that have an ILC currently, but this is a matter where if Congress and policy makers aren't careful, there can be a very fundamental change in structure of the U.S. financial system, aggregation of power, et cetera through the exploitation of a loophole that really – -and there is a debate as to whether it was intended, instead of grandfathering the institution, but it grandfathered the States which at that point in time weren't active in chartering these institutions. Now there is an active and thriving ILC lobby out there, because it is a way that any kind of firm, including Facebook, Amazon, Walmart again, can acquire a full-service bank. So, that's pretty troubling.

MR. KIM: For at least fintech. Keiron, can you talk a little bit about how PNC and JP Morgan are approaching fintech? What are the common regulatory issues you can see or the common regulatory constraints and how should they be addressed?

MR. FALLON: Sure. I mean I think our approach, and I'm in the legal department. So, I'm not a banker or one of our folks doing the strategic investments or M&A, but our approach is similar to many other firms. It's a build it yourself, buy the capability or partner with someone to do that. The factors that would go into each of them will be different, for the most part, business related decisions. So, you might build it if you build off of an existing capability that you already have in house. Obviously, we have a robust technology group within. So, building some fintech capabilities that enhance what we already have. Buying might be something if there is something out there that's unique or maybe acquiring unique talent at a company. Or partnering, which is probably what I see most, is for a variety of reasons, but it might be to accelerate a product to market and speed development, build off of something that you have, but you need that to accelerate it and get it to market. Obviously, especially in the marketing context, some of issues that we talked about earlier when we started here, on control. So, if you're making an investment, perhaps in that partnership and you're going to have a significant business relationship, then you have to start analyzing it under the Fed's control framework.

MR. MUSSELMAN: I think our approach is very similar. We don't have a fintech strategy per se. We're not out there to like make investments in fintech companies. It's not like just because we think they're neat. We have a banking strategy and so we're looking at ways to improve our products and services, and to some extent, fintech, they're raised the game in terms of what customers expect these days. They want to be able to transact everything on their mobile device or via an internet portal. It needs to be transparent, easy to click through, frictionless, all those things that you hear. We're moving our systems to that, moving to new digital cores. As we do that, it's the same kind of analysis, like okay, well, we can build this ourselves. We can partner with somebody and then if you're going to partner with that person, do you want to maybe take advantage of, have a little equity interest? So, you're participating in the profit-making opportunity that you're giving to them, but we do see a lot of -- early on, I think there was the perception that fintechs were good out there, they were going to eat banks' lunch. Banks would all be dinosaurs. I think that has not yet come to be. Hopefully it never does. You see more and more fintech's realizing that banks, we have the infrastructure. We have the relationships, working with us in ways that improve our products and services, in maybe even sort of a white label arrangement. So, it's more of a symbiotic relationship than I think people would have expected or at least was perceived a few years ago.

MR. KIM: Thanks. We've got about 10 minutes left. I'd like to open it up for questions. I've got 2 on the app. Then we can just have people raise their hand the old-fashioned way. I guess first, Mark, back to you, back to the control proposal, what can we expect on timing on the control rule?

MR. VAN DER WEIDE: Not too distant future.

MR. FALLON: You're not going to use the old fallback "soon"?

MR. VAN DER WEIDE: I try to mix it up a little bit.

MR. FALLON: They mean the same thing.

MR. KIM: Steven, for you, for the OCC, can you explain the OCC's recent change in policy regarding the application of the National Historic Preservation Act to charter and other application?

MR. LYBARGER: Yeah, that's really interesting. One, we're following the Fed here. The issue is, is that whether a licensing application in front of the SEC is an undertaking under the Act When you look at what you're evaluating in a licensing activity, you're evaluating a business activity, not construction of a building and branching applications. We don't dictate or address how you build a building. You follow local and State building codes and requirements. What we really started seeing, and one of the things that this discussion started with Amy and got further pushed with Jonathan and our discussions with him as the new chief counsel. You know, we would have banks that would target a particular locality for a branch. We'd have them reach out to the Shippo. The Shippo would say there's an issue. Then we got into a process that got really kind of cumbersome, but the issue was if Walmart came in and had an interest in that exact same bank, unless the State or local laws on historical preservation came in and acted, then Walmart could level that building and nothing could be done. It seemed like a very level playing field. It isn't that we do not support or see the value of historical preservation, but I think what we realize is strong historical preservation really starts with the State and local laws of historical preservation. That really, we didn't control that and it wasn't an appropriate position, and we actually looked at how the Fed was doing this and looked further at how the act was laid out and came to a legal conclusion that Jonathan supported, that this was not an undertaking for the act in an application setting. That's why we made the shift we did.

MR. KIM: Thanks. Another question for you. When can we expect to see revisions to Reg W to implement the Dodd-Frank changes to 23 and 23B?

MR. VAN DER WEIDE: I'm very tempted to give the same answer, but I'll speciate a little bit. I think we have been working on a First Amendment to Reg W for more than a decade, since even before the Dodd-Frank Act was passed. And in 2010 the statute passed but gave us like 200 different new rule making responsibilities and there was this Bozzle cord thing, Bozzle 3, that had about another 8 or 10 major regulatory responsibilities. And the Reg W project got triaged to the back of the line. It is like one of my favorite regulations about time. So I'm personally very disappointed that gate has gone by and not being able to get the First Amendment to Reg W out the door. It is something that we have been continuously working on at the back of the line. We've got documents that are very advanced, but there's just been too many rules to get done, Bozzle 3, Dodd-Frank, Egrippa. I think there are little bitty rays of sunshine. The clouds have parted in 2019 and I have some optimism in 2010 we can focus on some of these longstanding projects like Reg W. I think in one of the issues that we've wrestled with is, do we just want to limit our work to execute on the specific things that are in Dodd-Frank or do we want to do a more general kind of First Amendment to Reg W. I'm inclined to do at least some things beyond Dodd-Frank. The regulation was issued 15 years ago or so. It needs some general updating in a few areas. I'm hoping to do some general updating, implement the Dodd-Frank provisions. I think the recent interagency proposal to eliminate initial margin requirements on derivatives between banks and affiliates has moved Reg W a little farther up in the line in the triage department. Hopefully in the not too distant future, we'll get out Reg W, First Amendment, NPR.

MR. KIM: I have to ask. With Pam Arleta, the longtime Reg W expert retiring, who is the new resident expert at the Feds?

MR. VAN DER WEIDE: If I had to name one person, it would be Lucy Chang. Pam was an amazing colleague, mentor of mine, taught me everything I know about 23-A and so much else. I miss her deeply. There is no replacement for Pam or Lily, but Lucy Chang is the new queen of 23-A.

MR. KIM: That's all the questions we have on the app. Does anyone have any questions from the audience?

SPEAKER: I think Mark mentioned a little earlier there may be a few other projects related to applications in the hopper that you would like to address.

NR, VAN DER WEIDE: I think I've addressed most of it. We are in a broader process now. Now, that we've gotten almost all of the Dogg-Frank, Bozzle 3 things done, again the EG, our CPA stuff done. I do feel that 2020 can be the year where we can do some cleanup of the general regulatory framework that's long, long, long overdue, Reg Y, Reg K, Reg W, Reg 4. So, if we could find the time, I'd like to take a look at some of those old traditional regs, including some of the applications related and use elements of those and see if there is a way to make them better, time permitting.

SPEAKER: (off mic)

MR. LYBURGER: No. We can still charter CIBNA banks.

MR. FALLON: There's credit card banks.

There are non-depository stress banks. There are specific limitations on the activities they can engage in. They are open, so they could be a new, any of those established new today. IOC is the other large one in there. As we've said, if you can get a new IOC charter and those specific western states that qualify for the grandfather.

MR. LYBARGER: The interest is primarily a credit card bank, with the IOC charter.

MR. KIM: Okay. Anyone else? Go ahead.

SPEAKER: This question is for Mark.

MR. VAN DER WEIDE: That's a remarkably narrow question, but a really lovely one. Yeah, so we've had, I think, a pretty long-standing general tradition that to make a 4C6 investment, you've got to stay under 5 percent of voting securities and not be controlling. I don't recall. Mark Bereston could probably give you a more accurate answer to this question, my colleague here. It's really his responsibility to get this thing done. Much of why he's here, wasting his time. He should be working on it. But so, that's' kind of a historical tradition. I don't think we proposed to like to change our basic approach to 4C6. The most likely outcome is that we'll hold to our traditional position there, which means to do a 4C6 investment, you just stay under 5 percent of voting securities and not be in control, but you'll have a new more rulish, more transparent, a regulatory framework around making those controlled, non-controlled decisions.

SPEAKER: Would that mean that something that met the criteria in the first tier of the proposal would also would qualify as a good 4C6 investment?

MR. VAN DER WEIDE: I believe you are correct.

MR. KIM: In general, presumptions, rebuttal or presumptions?

SPEAKER: (off mic)

MR. LYBARGER: The limitations, the covenants that would provide you a controlling influence, I think one of the significant questions is whether you are below 5 percent, you also cannot have one of those covenants, because that would then make it potentially a non-passive 4C6.

MR. VAN DER WEIDE: Let me just take that question back with me and consult with the other Mark and see if we can provide some more clarify on that in the final rule.

MR. KIM: Anybody else? Okay, I think that's it. Thank you, everybody.

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