

Community Banking in Oregon, Regulatory Perspectives

Oregon Bank 2021 Leadership Symposium

TK Keen, Administrator



Regulatory perspectives

- Overview
 - Who we are and what we do
 - Oregon banking program
 - Update on the Oregon economy
- Major policy issues
 - Climate-related financial risk
 - Wildfire rebuild
 - Diversity, equity, and inclusion
 - Cryptocurrency (digital and digitized asset)
 - Upcoming legislative sessions

Who we are, what we do

- The state's regulator of community banks, credit unions, insurance companies, securities offerings, and more than 10 nondepository programs with a staff of more than 180 FTE.
- Key staff members:
 - Andrew Stolfi, DCBS Director and Insurance Commissioner
 - TK Keen, DFR Administrator
 - Kirsten Anderson, DFR Deputy Administrator
 - Alex Cheng, DFR Deputy Administrator
 - Jesse O'Brien, DFR Policy Team Manager, Legislative Contact
 - Steve Gordon, Chief of Banking and Securities



Oregon Banking Program

- 12 Oregon-chartered banks with approximately \$38 billion in assets and \$33 billion in deposits.
- Upcoming rulemaking – Amending OAR 441-505-3030 to increase the threshold for residential real estate transactions requiring an appraisal from \$250,000 to \$400,000 to conform to federal law.
- Cybersecurity notice – On **Nov. 18, 2021**, federal bank regulatory agencies approved a final rule requiring banking organizations to notify regulators of “any significant computer-security incident” as soon as possible and no later than 36 hours after a determination that such an incident occurred.
 - Effective date: **April 1, 2022**; Compliance date: **May 1, 2022**.
- Staffing and attracting talent into state system



Upcoming CSBS accreditation

- The Conference of State Bank Supervisors (CSBS) is the nationwide organization of financial regulators and is our accrediting body.
- The CSBS Accreditation Program involves an in-depth review of our division's policies, procedures, and operations to determine if it meets the standards set forth by the Performance Standards Committee (PSC).
- Benefits of the Accreditation Program
 - Obtain guidance and assistance through self-evaluation and self-improvement
 - Help standardize state banking processes through documentation
 - Demonstrate that the agency meets the standards for state supervision
 - Share ideas and best practices for state regulation of financial services
 - Strengthen state financial regulation by meeting a shared set of principles
- Next accreditation review is scheduled for August 2022.



Community banking conditions

- Nationally, post-pandemic concerns affecting banking include abundant liquidity and a decline in lending, particularly in the business, agricultural, and commercial real estate categories.
- Community banks nationwide have historic levels of deposits and narrow interest margins as competition for available credits has increased.
- Leverage capital ratios declined with increased PPP and PPPLF participation; however, the ratios for Oregon chartered banks remain above regulatory requirements.
- Ongoing industry labor issues attracting talent.



2021 CSBS Community Bank Survey key findings

- Net interest margins were most important external challenge.
 - Community banks nationwide have historic levels of deposits and narrow interest margins as competition for available credits has increased.
 - Competition has been exacerbated by low net interest margins that push bankers to seek new sources of revenue.
- Cybersecurity was the top internal risk.
- Operational changes imposed during the pandemic created long-term benefits in bank efficiency and customer engagement.
- Relative compliance costs declined.
- Some new issues emerged, primarily abundant liquidity and a decline in lending, particularly in the business, agricultural, and commercial real estate categories.



Oregon economy update, December 2021

- Oregon state economists say economic recovery from the pandemic continues to be robust:
 - Booming wage gains are now offsetting the fading federal aid; household incomes and consumer spending remain strong, supporting an overall bright outlook; the economy is set to reach full employment a year from now, or three times faster than in the aftermath of the Great Recession.
- The revenue boom is being supported by a wide range of income sources, including healthy gains in labor income that have generated personal income tax payments.
- Persistently tight labor market is putting upward pressure on wages.
- <https://www.oregon.gov/DAS/OEA/pages/index.aspx>



Major policy issues affecting banking



Climate-related financial risks

- In April 2021, the Basel Committee published two analytical reports on climate-related financial risks:
 - Climate-related risk drivers and their transmission channels
 - Climate-related financial risks – measurement methodologies
- The climate-related risk drivers report focuses on the **physical risks and transition risks that can arise and affect both banks and the banking system via micro- and macroeconomic transmission channels.**
- The climate-related financial risks report provides an overview of conceptual issues related to climate-related financial risk **measurement and methodologies, as well as practical implementation by banks and banking supervisors.**



Basel climate-related risk drivers findings

- The economic and financial market impacts of climate-related risks can vary according to geography, sector, and economic and financial system development.
- Traditional risk categories used by financial institutions and reflected in the Basel Framework (credit risk, market risk, liquidity risk, operational risk) can be used to capture climate-related financial risks.
- More research is required: There is limited research and accompanying data that explore how climate-related risks feed into the traditional risks faced by banks.



Basel climate-related measurement methodologies

- To date, measurement of climate-related financial risks has centered on mapping near-term transition risk drivers into bank exposures.
- Credit risk measurement has attracted the most effort, with a lesser focus on other risk categories. **Initial scenario analyses and stress tests have, in many cases, focused on selected portfolios or exposures for transition risks and selected hazards for physical risks.**
- More analysis is required: Methodologies to address uncertainties associated with the nature of climate change and the potentially longer-time horizon for risks to manifest.



DCBS perspectives on climate change

- In light of recent events, climate change and response is a high-profile issue for our agency.
- Director Stolfi serves on key national groups that are conducting surveys of insurance companies and how they assess climate risk.
- Aware of other state actions on the topic and want to come up with a collaborative approach.
- Anticipate having a meeting with our depository institutions in January.



Wildfire build and recovery efforts

- **July 2021:** Oregon Legislature allocated \$150 million through HB 5006 to support Wildfire Recovery Housing Programs at OHCS. OHCS was able to draw upon the work of the Oregon Disaster Housing Task Force and the Disaster Housing Recovery Action Plan to begin immediately programming these legislative resources.
- **September 2021:** Congress passed continuing resolution appropriating \$5 billion in relief for states that experienced presidentially declared disasters in 2020 and 2021.
- **Nov. 1, 2021,** the U.S. Department of Housing and Urban Development announced it is approving the allocation of more than \$422 million of the original \$5 billion federal appropriation for Community Development Block Grant Disaster Recovery and Mitigation to Oregon for recovery efforts due to the 2020 Labor Day wildfires.



Diversity, equity, and inclusion - profitability

- Jack Hartings, Chairman, The Peoples Bank Co., Coldwater, Ohio, on attending ICBA's Breaking Barriers Symposium: "I learned that diversity, equity, and inclusion are not just about doing the right thing for our banks and our communities. Though that's a great place to start, **there are concrete business benefits to having a more inclusive staff and board.**"
- **"Diverse teams make better decisions 87% of the time. And those stronger choices lead to increased profitability:** According to McKinsey, **companies in the top quartile for gender diversity on executive teams were 25% more likely to have above-average profitability, and in the case of ethnic and cultural diversity, that number rises to 36%.**"
- Community Banker University and employment law firm Jackson Lewis have teamed to offer ICBA members a complimentary, three-part webinar series that explores workplace diversity, equity, and inclusion.
- <https://www.icba.org/education/webinars/diversity-equity-and-inclusion-webinar-series>



DCBS diversity, equity, and inclusion

- Agency planning and involvement
- Governor's Racial Justice Council contributions
- Division plan



State regulation of cryptocurrency

- Cryptocurrency falls within the definition of “money” under the Oregon Bank Act and the state’s money transmitter law.
- ORS 706.005(6)(a) of the Bank Act defines the “business of banking” as “a regular business of receiving or accepting money or **the equivalent of money** on deposit, whether the deposit is made subject to check or is evidenced by a certificate of deposit, a pass book or other writing or evidence.”
- Like other state regulators, the division has asserted jurisdiction over virtual currency businesses by requiring a money transmitter license to transfer digital currency from one person to another; however, digital currency exchange companies that only turn cash into digital currency are not required to be licensed (cryptocurrency ATMs).



Cryptocurrency and the UCC

- Article 9 of the Uniform Commercial Code (UCC) falls short of providing adequate guidance on how to create or perfect a security interest in these currencies.
- The proposed amendments to the UCC by the Uniform Law Commission and the American Law Institute in 2019 organized the Uniform Commercial Code and Emerging Technologies Committee include amendments to Articles 1 and 9 intended to address the concept of “intangible money” and then provide for its perfection by control.
- Once finalized, Oregon will need to adopt the UCC amendments.



Cryptocurrency/permissible banking activities

- Under the Trump Administration, the OCC issued interpretive letters stating that national banks may provide cryptocurrency custody services, and they may use new technologies, including independent node verification networks (INVN) and related stablecoins, to carry out bank-permissible functions, such as payment activities.
- Current Acting Comptroller of the Currency Michael Hsu has requested a review of the “interpretive letters and guidance regarding cryptocurrencies and digital assets,” as well as the updates to the “framework for chartering national banks and trust companies.”
- Oregon and the FDIC continue to study the issues. On May 17, 2021, the FDIC requested information and comment on insured depository institutions’ current and potential digital asset activities, including custodial activities.



Upcoming legislative sessions

- Special Session on Housing and Evictions, Dec. 13
- 2022 Session (short)
 - Unlikely to have agency bills
 - Aware of bills on a wide range of topics, including possible state bank concept
- 2023 Session (long)
 - Preparing and vetting agency bills over next few months
 - Right now, none of our agency bills would touch on the Bank Act or bank issues



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