LUSE GORMAN

Volume 24 | December 2025

The Bankers' Bulletin

Regulatory and Enforcement Insights on ***Recent Bank Industry Developments***

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INDUSTRY SNAPSHOT

month over month

- ↓ OCC Charter Applications Filed: **1**
- ↑ FDIC Insurance Applications Filed: **2**
- — FDIC Insurance Applications Approved: **0**
- ↑ Bank Enforcement Actions Announced: **1**
- ↑ Bank Enforcement Actions Terminated: **8**

Check out what Luse Gorman was up to last month here:

Bank Acquisition Closure ($44.0M) || Branch Acquisition Closure ($553.0M)
Merger Announcement ($243.0M) || Subordinated Debt Issuance ($50.0M)

Federal Reserve Issues Memorandum Revising its Supervisory Procedures

Summary

On Nov. 18, the FRB publicly released an internal memorandum outlining broad changes to how the agency will conduct supervision going forward, labeling the planned changes a "significant shift from past operating practices."

Highlights

1) Examiners are directed to prioritize attention on regulated entities' material financial risks and not become "distracted" by "devoting excessive attention" to processes, procedures, and documentation. This mirrors the approach of the FDIC and OCC proposed MRA rule. A future rule on the FRB's use of MRAs is teased in the memo.
2) Shortcomings that do not rise to the level of MRAs will be addressed through nonbinding supervisory observations.
3) The FRB will defer more to state banking regulator exams, relying to the "extent possible" on the state's work.
4) For bank holding companies, examiners are instructed to rely on the examination results from the subsidiary bank's regulators. FRB staff should not conduct their own exam unless it is "impossible" to rely on such results.

Practical Tips

- If a bank's internal audit is satisfactory and it validated that MRA or enforcement action corrective actions were taken, FRB staff will no longer perform duplicative validation of those actions. This incentivizes effective audit practices.
- Banks should actively engage with and seek clarification from their supervisory teams regarding the scope of corrective actions needed to satisfy MRAs. The memo explicitly encourages dialogue to avoid miscommunication.

Takeaway

While the FRB enshrined many of the same supervisory principles as the OCC and FDIC, the choice to utilize an internal procedure over a rulemaking allows additional flexibility—but eases the path to rescind it later. Focus on financial risks and avoidance of process and documentation criticisms should dramatically reduce the number of corrective actions member banks face. Emphasis on clarity, definitions, and dialogue will reduce the need for banks to escalate challenges.

Federal Banking Agencies Adjust Asset Thresholds for Capital, Audits

Summary

On Nov. 25, the OCC, FDIC, and FRB issued a joint proposed rule to modify the community bank leverage ratio (CBLR) from 9% to 8%. On the same day, the FDIC finalized its rule to adjust the audit-related asset thresholds in Part 363.

Highlights

1) In addition to reducing the CBLR, the agencies' joint proposal would extend the permitted grace period from two to four quarters, but would cap a bank's use of the grace period at eight quarters over any five-year period.
2) The FDIC's rule increases asset thresholds as proposed: from $500MM-$1B (annual rpt. including audited financials, independent accountant's rpt., management rpt.); $1B-$5B (assessment of the effectiveness of internal controls over financial reporting and use of an independent audit committee); $3B-$5B (additional audit committee requirements).
3) The new Part 363 will employ an indexing methodology: it will generally adjust the dollar thresholds at the end of every consecutive two-year period based on a metric that considers inflation, but is not solely based on inflation.

Practical Tips

- While the agencies expanded banks' ability to use the CBLR grace period, they acknowledged they will monitor banks' usage of it. They explicitly reserve the authority to apply different capital requirements depending on circumstances.
- Banks that qualified under Part 363's 2025 thresholds for prospective filing and compliance requirements, but which will no longer qualify as of Jan. 1, 2026 based on the new thresholds, don't need to comply with those requirements.

Takeaway

Modifying the CBLR should drive an uptick in community banks' usage of that capital measure, which the agencies noted was an intended effect of the change. Banks that already have established independent audit report frameworks and audit committee structures are unlikely to abandon those governance measures solely due to the changed asset thresholds. But the redrawing of those lines will reduce banks' enforcement exposure should they have any foot faults.

This month's big number:

475

The number of additional community banks that would qualify to participate in the revised community bank leverage ratio (CBLR) framework, if it is re-calibrated down from 9% to 8%, according the federal banking agencies' Nov. 25 proposed rule. The agencies estimate that 95% of community banks would qualify to participate.

Appellate Court Issues Decision Permitting Colorado to Enforce Usury Laws

Summary

On Nov. 10, the Tenth Circuit Court of Appeals issued an opinion that allows Colorado (CO) to set interest rate caps for loans by out-of-state banks to borrowers in CO, reversing a district court injunction that had blocked CO's law.

Highlights

1) The case centers on a 2023 law in which CO "opted out" of a separate provision in federal law that allows out-of-state banks to avoid CO's interest rate caps for loans made in CO. CO tried to stem the rise of nonbank lenders partnering with out-of-state banks with higher interest rate caps to make loans to CO borrowers above CO's caps.
2) In a case of first impression, the court held that the key phrase in the federal opt out provision—which refers to loans "made in" the opting out state—encompasses loans in which either the bank *or a borrower* is located in the opt-out state. By covering loans made to *borrowers* located in CO, the decision will affect state banks located nationwide.
3) The court considered, but ultimately rejected, the argument made by the banks challenging CO's law that they would be disadvantaged by this interpretation as compared to national banks, which are unaffected by the ruling.

Practical Tips

- The case is likely subject to further litigation, either within the Tenth Circuit or at the Supreme Court level. For now, state banks located outside CO must be prepared to treat CO borrowers differently in terms of setting interest rates.
- The court declined to grant deference to previous FDIC and OTS interpretations on this question, not due to 2024's *Loper Bright* holding, but because the agencies' interpretive position had been inconsistent over time.

Takeaway

With Colorado's legal victory, more states may push to pass opt out laws blocking out-of-state banks from charging borrowers in their states interest rates above their own caps. This could lead to a patchwork of state interest rates that banks need to monitor and adjust for. This in turn could fuel more interest in conversions to national bank charters.

FDIC and OCC Adjust Scope and Frequency of CRA, BSA Examinations

Summary

On Nov. 7, the FDIC announced updates to its Consumer Compliance Examination Manual to change the examination frequency for consumer and CRA reviews. On Nov. 24, the OCC issued new community bank BSA/AML exam procedures.

Highlights

1) The FDIC removed the one-size-fits-all exam cycle table for banks over $350MM, opting to create a new tier of institutions between $350MM and $3B. Banks in that size range will be eligible for a 54-66 month consumer/CRA cycle, with only a "mid-point risk analysis" conducted in the interim for banks with satisfactory and above ratings.
2) Institutions that receive adverse consumer or CRA ratings will get more FDIC visits, but the cycle itself will not reset.
3) The OCC's new procedures would apply to national banks and FSAs under $30B and allow examiners to rely on satisfactory independent testing as a basis for conclusions in the exam report, carry forward prior conclusions for the training and BSA officer pillars, and use discretion as to whether transaction testing needs to be performed.

Practical Tips

- While the FDIC's new cycles could grant many banks a reprieve for the next three years, the proposed gap is so long that banks should be prepared that a new Administration could reverse the changes and return earlier than expected.
- The OCC's procedures will reward banks that have a strong, effective BSA Officer and comprehensive training by relieving burden. A thorough independent BSA report will go a long way to averting duplicative examiner reviews.

Takeaway

The agencies' guidance revisions—although relating to different subject matter—serve as additional examples of Gould and Hill's pledges to ease the burdens of examinations on community banks. But both agencies leave the door open to exam teams using discretion to carry out specific exam activities or complete certain processes (the guidance relies on phrases like, "as determined to be appropriate"), which practically may cause slower or inconsistent uptake.

> "There's a misunderstanding out there that somehow just a fintech can show up and say, 'Hey, I'd like a skinny master account.' No. You've got to be an eligible depository institution . . . . So it is technically, you have to have a bank charter. So if you're not a bank, you don't have a bank charter, you don't have the right to ask for one at all."

Federal Reserve Governor Christopher Waller,
seeking to clarify a proposal he had previously floated to create a tailored version of a Fed master account,
during a panel at an event held in conjunction with the Bank of Canada (Nov. 6).

CFPB Issues Dual Proposals to Amend ECOA Reg While it Prepares to Close

Summary

On Nov. 13, the CFPB issued two proposed rules to amend Reg. B under ECOA: the first would remove references to disparate impact, while the second would pare back the small business lending provisions under Section 1071.

Highlights

1) In the first proposal, the CFPB explains that in the "best reading of the statute," disparate impact claims are not authorized under ECOA. The proposal would add language stating ECOA does not prohibit facially neutral practices.
2) The proposed revisions to the 1071 rule issued under Chopra substantially pare back the scope of the data points that lenders must collect. Rather than use agency discretion to impose collection requirements for dozens of data points, the proposal will limit the collection scope primarily to those data points chosen by Congress in Dodd-Frank.
3) The proposal would significantly narrow the (i) definition of small business, by changing the annual revenue threshold from $5MM to $1MM, and (ii) banks subject to the rule, by increasing the number of transactions to qualify.

Practical Tips

- Tucked away in the first proposal are prohibitions and restrictions on using certain characteristics as eligibility criteria for special purpose credit programs (SPCPs), requiring major structural overhauls for banks using SPCPs.
- Banks that have stopped and started work on implementing a small business lending data collection framework—following the twists and turns in litigation over the prior rule—should consider preparing an alternative, slimmed down version aligning with this proposal. But given the uncertainty, banks should not overinvest their resources yet.

Takeaway

Whether the CFPB functions long enough to finalize either proposal is in doubt. On Nov. 10, the CFPB filed in federal court a notice stating it anticipates exhausting all its available funds in early 2026. Under a DOJ legal opinion it provided to the court, the Bureau claimed it cannot draw more funds from the Federal Reserve. Absent court or congressional action, the CFPB will likely put its remaining employees on leave or try to terminate them before the rules are completed.

Other Developments You May Have Missed Last Month . . .

Sen. Tillis Introduces Discussion Draft of Fair Access Bill. On Oct. 30, Sen. Tillis (R-N.C.) introduced a draft of the Ensuring Fair Access to Banking Act, which proposes a federal "fair access standard" designed to prohibit banks from refusing services based on customers' free speech exercise or their business activities. The draft also wraps in existing proposed bills to ban reputation risk and increase SAR thresholds.

Bottom Line**:** According to Tillis, the legislation is designed in part to preempt state-level fair access laws that have created an "operationally daunting patchwork" of conflicting legal requirements for banks. States that impose stricter requirements than the federal proposal may object to what they perceive to be an overly-diluted standard. Notably, the bill would allow state regulators, including state AGs, to pursue litigation on behalf of customers for alleged violations, potentially exposing banks to suits in every state in which their customers reside.

Tenth Circuit Panel Rejects Claim of Entitlement to Master Account. On Oct. 31, the federal Tenth Circuit Court of Appeals issued an opinion concluding that federal statute gives the Federal Reserve Banks discretion to reject eligible entities' requests for master account access. The court affirmed the district court's denial of a complaint filed by Custodia Bank, a Wyoming-chartered Special Purpose Depository Institution.

Bottom Line**:** Despite a dissent, the panel's ruling will likely serve as an important precedent in future litigation on this issue. The decision cites only three other district court cases on this question, each reaching the same conclusion. Given the proliferation of non-traditional banking charters in various states, it is likely that newer institutions that are eligible to obtain master accounts under statute and FRB guidance because they possess charters—however novel—will piggyback off the dissent's reasoning to try to create a circuit split and force a Supreme Court ruling.

Bankers Association Files Petition to Challenge Florida Debanking Rules. On Nov. 13, the FBA filed a petition with the state's Division of Administrative Hearings challenging the debanking rules recently issued by the state's banking regulator, the Office of Financial Regulation (OFR). The petition alleges the rules exceed the scope of the authority granted by statute and impose substantial costs on banks in the state.

Bottom Line**:** The move by Florida's trade association could portend future challenges of fair access and debanking initiatives at both the state and federal level as the issue continues to gather steam at agencies and with legislative officials. In addition to resolving questions regarding state regulators' power to issue rules related to debanking, the FBA's petition raises important questions regarding whether national banks will be forced to comply with these broadly-worded state laws, and whether BSA/AML confidentiality restrictions will be weakened.

OCC Issues Guidance Permitting National Banks to Hold Crypto-Assets. On Nov. 18, the OCC issued Interpretive Letter No. 1186 (IL 1186), confirming that national banks can pay network fees on blockchain networks to facilitate other permissible activities, and hold, as principal, amounts of crypto-assets on their balance sheets necessary to pay network fees. IL 1186 also confirmed that national banks may hold amounts of crypto-assets necessary to test permissible crypto-asset related platforms that the banks develop in-house or acquire from a third-party.

Bottom Line**:** The OCC's permissibility analysis focuses heavily on comparing these functions to more traditional, well-established bank practices relating to payments. The opinion also highlights the potential costs and risks introduced by outsourcing these functions to third-parties. Future requests for approval to engage in crypto-related activities should lean into these arguments. The requesting bank's pledge to perform a risk assessment and align the proposed activities with its business strategies also played a role in securing the OCC's approval.

About Us

Luse Gorman, PC is a Washington DC-based law firm that specializes in representing regional and community banks across the country. Our attorneys have served with the federal banking and securities agencies and regularly engage with these agencies on a broad range of complex and novel compliance, regulatory, enforcement, transactional, application, and licensing issues. Our firm also specializes in mergers and acquisitions, capital raising transactions, general corporate and securities issues, and tax, executive compensation and employee benefits matters.

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