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LEGAL UPDATE

OCC and FDIC Propose Joint Rule to Prohibit Use of Reputation Risk

On October 7, 2025, the Office of the Comptroller of the Currency (the "OCC") and the Federal Deposit Insurance Corporation (the "FDIC" and together, the "Agencies") issued a joint notice of proposed rulemaking to prohibit the Agencies from criticizing or taking adverse action against an institution on the basis of "reputation risk." The proposed rule follows earlier efforts by each of the Agencies to remove references to reputation risk from their respective guidance and manuals, and also is intended to further the purposes behind the August 7, 2025 Executive Order titled "Guaranteeing Fair Banking For All Americans" (the "Executive Order") by prohibiting the use of "reputation risk" from serving as a pretext for restricting access to financial services. (Our previous Legal Update related to the Executive Order can be found here.) Comments on the proposed rule are due within 60 days of publication in the Federal Register.

As noted in the proposed rule, the Agencies found that using reputation risk as a basis for criticism injects subjectivity into the supervisory process. The proposal acknowledges that the Agencies have not historically clearly articulated the criteria for which certain bank activities, or activities of their third-party partners or customers, present reputation risk to the institution, and that past supervision of this risk has been inconsistent, reflecting individual examiner judgments rather than determinations based on data. The Agencies stated that most actions which could negatively impact a bank's reputation already do so through traditional risk channels, such as credit risk, liquidity risk, or operational risk, that are each more concrete and measurable and allow for a more objective assessment of a bank's financial condition. The Agencies concluded that examining for reputation risk diverts their resources from examining for other risks that may present significant, tangible threats, and are more easily quantified and addressed. The Agencies have determined that examining for reputation risk is therefore "inappropriate" given the challenges in accurately measuring and quantifying such a risk, and stated that these types of decisions are best left to bank management's judgment.

The proposed rule would define reputational risk as "any risk, regardless of how the risk is labeled by the institution or the regulators, that an action or activity, or combination of actions or activities, or lack of actions or activities, of an institution could negatively impact public perception of the institution for reasons not clearly and directly related to the financial condition of the institution." The proposed rule would prohibit the Agencies from "criticizing or taking adverse action against an institution on the basis of reputation risk." The prohibited criticism could be formal or informal, verbal or written. "Adverse action" would include the provision of negative feedback (including in a report of examination), a memorandum of understanding, a ratings downgrade, or an enforcement action, and covers any employee action, including those communications characterized as informal, preliminary, or not approved by agency officials or senior staff. In addition, a denial of a filing or licensing application, imposition of capital requirements, burdensome requirements placed on approvals, and additional approval requirements all also qualify as "adverse actions" under the proposed rule. The Agencies also included a general "catch-all" for any other actions that could negatively impact an institution outside of traditional supervisory channels, such as supervisory decisions on applications for waivers outside of the normal licensing or filing channels, applications to engage in certain business activities, or other regulatory decisions affecting institutions.

The proposed rule would also prohibit the Agencies from requiring, instructing, or encouraging banks or their officers or employees from closing accounts, refraining from providing products or services, terminating contracts, ending or avoiding relationships, or modifying the business terms of arrangements, with persons or entities on the basis of the their political, social, cultural, or religious views or beliefs, constitutionally protected speech, or "solely on the basis of the [third parties'] involvement in politically disfavored but lawful business activities perceived to present reputation risk." In the view of the Agencies, this separate prohibition was prompted by examiners implicitly or explicitly directing or encouraging banks to restrict access to services on the basis of those examiners' personal views in these areas.

Takeaways

- The proposed rule largely codifies into a more explicit regulatory standard the intent that prompted the changes the Agencies already made to their guidance and manuals earlier in 2025, and the instructions that they provided to their examination teams at that time. Notably, although the Federal Reserve Board announced in July that it was no longer considering reputational risk as part of its supervisory framework, that agency did not join the OCC and FDIC in this proposed rulemaking.

- Elimination of reputation risk as a consideration in supervisory judgments will be a boon to banks that have struggled to challenge examination determinations, matters requiring attention, or enforcement actions based on individual examiner judgments regarding the potential impacts of a decision, situation, or relationship on the public's perception of the bank. Given the amorphous nature of the reputation risk concept, effectively overturning an examiner's judgment in an appeal or other objection to a supervisory determination proved nearly impossible in practice.

- The proposed rule reinforces the Agencies' shift in supervisory approach to focus nearly exclusively on financial-related metrics and condition, and away from subjective or soft measures that cannot be accurately quantified. This shift is emphasized in other rule proposals and guidance issuances from the Agencies that were announced contemporaneously with this proposed rule.

- While the expansive definition of "adverse action" in the proposed rule, including the catch-all provision, is broad enough to eliminate overt references to reputation risk in nearly all supervisory determinations and decisions, it is important to keep in mind that examiners still exercise discretion in other supervisory judgments, whether or not reputation risk is an explicit factor in the provided rationale.

- Although the proposed rule would prohibit examiners from using Bank Secrecy Act and anti-money laundering concerns as a pretext for reputation risk, the prohibitions do not affect requirements intended to prohibit or reject transactions or accounts associated with OFAC-sanctioned persons, entities, or jurisdictions.

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Luse Gorman, PC regularly advises financial institutions on regulatory and compliance developments of, supervisory relationships with, enforcement actions from, and licensing applications to, the federal banking agencies. If you have any questions related to this Legal Update, please reach out to Brendan Clegg at (202) 274-2034 or bclegg@luselaw.com, or your Luse Gorman contact. To learn more about our firm and services, please visit our website.