



**INDEPENDENT COMMUNITY
BANKERS of AMERICA**

June 11, 2009

The Honorable Timothy F. Geithner
Secretary of the Treasury
U.S. Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

Dear Mr. Secretary:

I am writing on behalf of the Independent Community Bankers of America¹ and the nation's 8,000 community banks to express our views on several core principles that will be part of the upcoming debate on financial regulatory restructuring and reform.

As you know, the community banking segment of the financial services industry is strong, and community bankers are doing their part to help in the economic recovery. Most community banks are actively lending in their communities to support small businesses and promote job retention and development. Our industry is generally well capitalized and extensively regulated and, because we did not engage in the kind of reckless lending and leveraging practices that were at the root of the current crisis, has fewer problem assets than other segments of the financial services industry.

Nonetheless, ICBA is a strong supporter of properly directed regulatory reform in an attempt to prevent, or at least mitigate, future financial crises. While no one can be expected to forecast when the next economic crisis will occur, it is our duty as government and industry leaders to reorder the financial system so it can withstand the stress without inflicting undue economic suffering on the nation. We strongly support meaningful and reasonable regulatory reform focused on addressing the challenges posed by the unregulated lenders and investment banks that helped create the systemic risks that contributed to this financial crisis. Toward that end, regulatory reform should target

¹ *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace. With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than \$908 billion in assets, \$726 billion in deposits, and more than \$619 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.*

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systemic-risk institutions to reduce the dangerous concentration of financial and economic assets.

A Monolithic Bank Regulator is Dangerous and Would Undermine the Dual Banking System

ICBA is adamantly opposed to consolidating the existing regulatory regime into a single, monolithic federal banking regulator for all banking institutions. This is a flawed, shortsighted and dangerous approach that would ultimately disadvantage community banks and the cities, towns and rural areas across America that they serve.

Overwhelming concentration of power in any governmental or economic sector is counterproductive and unwise. Having more than a single federal agency regulating depository institutions brings balance and perspective and provides valuable regulatory checks-and-balances over the use (and sometimes abuse) of power. Having more than a single regulator promotes “best practices” among those agencies – much like having multiple branches of government. The collaboration that is required by multiple federal agencies on each interagency regulation insures that all perspectives and interests are represented, that no one type of institution will benefit over another, and that the resulting regulatory or supervisory product is superior.

Further, independent bank regulatory agencies are more insulated from political pressures, allowing them to deal more objectively with those they are charged to regulate.

A monolithic federal regulator, such as the U.K.’s Financial Services Authority, would be dangerous and unwise in a country with a financial services sector as diverse as the United States. Efficiency must be balanced against good public policy. With the enormous power of bank regulators and the critical role of banks in the health and vitality of the national economy, it is imperative that the bank regulatory system preserves real choice, and allows for both state and federal regulation.

ICBA believes strongly in maintaining the dual banking system because it allows for a diversity of financial institutions, is sensitive to financial institutions of various complexity and size, and promotes consumer choice. The dual banking system has served our nation well for generations, and has helped create a unique banking structure that is the envy of the world. That role would be undermined by giving a monolithic federal regulator which charters national banks the authority to review supervision of state banks by state regulators. Over time, this could lead to bias by the federal regulator towards federally chartered institutions and the perception of the state charter as being inferior. Community banks value the productive tension between state and federal regulators, and that benefit would be significantly devalued through federal review of state agencies.

Our banking sector has long been the strongest and most resilient financial system ever created. But recently we have gotten off track. Non-bank financial regulation has been lax and our system has allowed – and even encouraged – the establishment of financial institutions that are too big to manage, too big to regulate, and too big to fail.

Strong Systemic Risk Regulation is Needed

The Administration need not waste time rearranging the regulatory boxes to change the system of community bank regulation. That system has worked, is working, and will work in the future. The failure occurred in the too-big-to-fail sector. This is the sector that must be fixed with the following steps:

- Congress should direct a fully staffed interagency task force to immediately identify financial institutions that pose a systemic risk to the economy based on size, complexity or activity.
- These institutions should be put immediately under prudential supervision by a Federal agency – most likely the Federal Reserve.
- The Federal systemic risk agency should impose two fees on these institutions that would:
 - compensate the agency for the cost of supervision; and
 - capitalize a systemic risk fund comparable to the FDIC's Deposit Insurance Fund.
- The FDIC should impose a systemic risk premium on any insured bank that by itself is systemically important or affiliated with a firm that is systemically important.
- The systemic risk regulator should impose higher capital and stronger risk management requirements to protect against systemic risk.
- Congress should vest the FDIC with authority to resolve and unwind systemic risk institutions found by the systemic risk regulator to be in default or in danger of default.
- Congress should direct the interagency systemic risk task force to order the downsizing of systemic risk institutions over a five year period.
- Congress should direct the systemic risk regulator to review all proposed mergers of major financial institutions and to block any merger that would result in the creation of a systemic risk institution.
- Congress should direct the systemic risk regulator to take action to ameliorate any financial activity that threatens to impose a systemic risk.

The only way to maintain a vibrant banking system where small and large institutions are able to fairly compete – and to protect taxpayers – is to aggressively regulate, assess, and eventually reduce the size of those institutions that pose a risk to our entire economy. Proportional regulation based on risk is long overdue.

FDIC Should Have Resolution Authority for Systemic Risk Institutions

ICBA strongly supports your proposal to vest the FDIC with resolution authority over systemic risk institutions that fail or are in danger of failing, modeled after Section 11 of the FDI Act. The FDIC has extensive experience administering the resolution of banks and thrifts, and has an infrastructure in place to exercise conservatorship and receivership powers over banks that can be extended to other types of financial companies, including holding companies and their non-depository subsidiaries. Other federal agencies would

have to build such an infrastructure from scratch, which would be costly, inefficient and time-consuming.

However, the Deposit Insurance Fund (DIF) must not be used to directly or indirectly subsidize the expenses of resolving the failure of systemically important non-bank institutions. But as long as a separate, segregated fund is set up to cover the potential and actual FDIC expenses that would result from this new authority, the DIF should not be at risk of exposure. This may also require the establishment of a legally separate division within the FDIC to handle only the resolution of systemic risk non-bank institutions and that is completely funded from premiums assessed on those institutions.

Consumer Protection Should Not Be Separated from Safety and Soundness Regulation

We also have very serious concerns with the concept of a “financial products safety commission,” patterned loosely on the Consumer Products Safety Commission, to regulate the financial products and services being offered to consumers. While ICBA believes that effective consumer protection is an integral part of financial services regulation, a financial products safety commission would not provide consumers with greater protection, but would increase the regulatory burden on an already over-burdened community banking industry.

This seemingly well-intentioned concept would not address the core problem -- lack of supervision in the non-bank lending sector. As you are aware, non-bank lenders, such as mortgage companies, are not subject to supervision and examination by the financial services agencies. ICBA believes that the examinations regularly conducted by bank regulatory agencies are the best means to ensure compliance with consumer protection requirements established by statute and regulation. The primary issue we need to address to avoid future abuse in the marketplace is this lack of oversight of non-bank entities, not creating yet another regulator and layer of bureaucracy for financial institutions, especially community banks that are already heavily regulated.

In addition, establishing such a commission unwisely would separate consumer policy from enforcement and safety and soundness when all of these elements must co-exist and be balanced for effective financial services regulation. Such a commission would not have the big picture view of banking regulators that onsite examination and supervision can provide. The bank safety and soundness regulators have developed practical expertise in balancing the safe and sound operation of FDIC-insured institutions with the need to provide consumers protection from unfair and harmful practices, and this perspective should not be lost. Because of their hands-on supervisory role, bank examiners have the best view of how consumer protection rules affect bank customers and the bank itself. If the consumer products regulator is not equally interested in the safety and soundness of the lender, it is likely to promulgate burdensome regulations that make many safe financial products, which are beneficial to consumers, unobtainable or too costly to offer.

Further, consumer protection laws regulating such products as credit cards and mortgage loans have been reviewed and updated by Congress and the financial services regulators to address problems that lack of adequate regulation may have caused. The enforcement of these updated consumer protection laws on both bank and non-bank financial institutions should provide greater consumer protection in the future, thereby eliminating the need for another regulator and level of bureaucracy.

Core Principles for Regulatory Reform

We realize that these observations just brush the surface of a comprehensive plan to address weaknesses in our financial regulatory system. Our nation's community bankers welcome the opportunity to work with you to ensure that regulatory restructuring is properly targeted and strikes the right balance between risk and regulation. We believe such a plan should at a minimum adopt the following core principles for financial reform:

- **Address Systemic Risk Institutions.** It is clear that reckless lending and leveraging practices by systemically important institutions were at the root of the current economic crisis, and the issues of over-concentration and too-big-to-manage, -regulate and -fail must be addressed. Eventually, these institutions must be downsized so they no longer pose a risk to our entire economy.
- **Support Multiple Federal Banking Regulators.** Having more than a single federal agency regulating depository institutions provides valuable regulatory checks-and-balances and promotes "best practices" among those agencies – much like having multiple branches of government.
- **Maintain the Dual Banking System.** Having multiple charter options -- both federal and state -- is essential for maintaining an innovative and resilient regulatory system.
- **Access to FDIC Deposit Insurance for All Commercial Banks, Both Federal and State Chartered.** Deposit insurance as an explicit government guarantee has been the stabilizing force of our nation's banking system for seventy-five years.
- **Reform FDIC Risk-Based Assessment System.** To make the FDIC risk-based assessment system more sensitive to risk in the banking system, the FDIC should charge a systemic risk premium to all systemically important depository institutions to account for the risks that these institutions represent to the Deposit Insurance Fund and the taxpayers. In addition, the FDIC assessment base should be broadened to all assets minus tangible equity. The amount of assets that a bank holds is a more accurate gauge of an institution's risk to the DIF than the amount of its deposits.
- **Protection for Customers of Depository Institutions in the Current Federal Bank Regulatory Structure.** One benefit of the current regulatory structure is that the federal banking agencies have coordinated their efforts and developed consistent approaches to enforcement of consumer regulations, both informally and formally, as they do through the Federal Financial Institutions Examination Council (FFIEC).

- **Reduce or Strengthen the 10 Percent Deposit Concentration Cap.** The current economic crisis highlights the dangers of overconcentration of financial resources in too few hands.
- **Support the Savings Institution Charter and the OTS.** Savings institutions play an essential role in providing residential mortgage credit in the U.S. The thrift charter should not be eliminated and the Office of Thrift Supervision should not be merged into the Office of the Comptroller of the Currency.
- **Preserve the GSEs' Liquidity Role.** Many community bankers rely on Federal Home Loan Banks for liquidity and asset/liability management through the advance window.
- **Maintain the Separation of Banking and Commerce and Close the ILC Loophole.** Mixing banking and commerce has a history of failure throughout the world, and has led to prolonged and deep recessions. The U.S. does not need to go down that road.
- **Establish an Office of Community Financial Institutions within the Treasury Department.** This office, which should be headed by an Assistant Secretary, will ensure that the unique needs and interests of community banks are being considered. (We strongly support the Oversight for Community Financial Institutions Act of 2009, H.R. 2676, introduced by Rep. Dennis Cardoza, which would create an Assistant Secretary for Community Financial Institutions within the Treasury Department.)

Mr. Secretary, to say financial regulatory reform is a complex and complicated undertaking is a tremendous understatement. Current circumstances demand our utmost attention and consideration. We recognize that many of the principles laid out in this letter may be controversial, but ICBA strongly believes they are necessary to preserve and maintain America's great financial system and ensure that it is even stronger coming out of this crisis.

Thank you for considering the views of our nation's community bankers.

Sincerely,

/s/

R. Michael S. Menzies, Sr.
ICBA Chairman

/s/

Camden R. Fine
President and CEO