

March 21, 2010

The Honorable Sheila Bair  
Chairman  
Federal Deposit Insurance Corporation  
550 17th Street, NW  
Washington, DC 20429-9990

Dear Chairman Bair:

Thank you for speaking to our members at the recent Government Relations Summit of the American Bankers Association. We have all been living through a very challenging period of time. Certainly for you, as Chairman of the FDIC, there could have been few scenarios with as many important issues to face and decisions to make. I appreciate your dedication, and as an officer of the ABA as well as a banker, I thank you for your openness to the banking industry and willingness to listen to our concerns. The challenges that bankers face have been no less grave. In fact, for many of us the very existence of our institutions—and the services we provide to our communities—have been at stake.

We had at the Government Relations Summit a full house of close to a thousand bankers, representative of our membership from all across the country. As you saw from the show of hands, community bankers, like myself, overwhelmingly predominated in the attendance at the Summit. This is not unusual. Community bankers are deeply involved in the policy development and advocacy efforts of the ABA. ABA is proud to represent the entire banking industry, with members off all charter types, sizes, and geographies. More than 90% of the members of the ABA are community banks like mine, with less than \$1 billion in assets, and the majority of ABA member banks have less than \$165 million in assets.

I was Chairman of the ABA Government Relations Council when the bankers on that Council developed the list of principles that we believed were needed for genuine reform legislation, legislation that in 2008 we encouraged the Congress take up. Those principles were considered and unanimously adopted by the bankers on the ABA Board of Directors. They strongly reflected the views of our community bank membership.

I say that, because I want to emphasize that our members have been deeply involved in developing our regulatory reform policies, and I want to help show why we feel so strongly about the Dodd-Frank Act and the related burdens that are threatening not just our industry but our very banks. The most conservative estimates that we have seen predict that by the end of the decade there will be one thousand fewer banks in the United States than there are today. Consider the thousand people in the audience that you addressed, and think of each audience member as a bank that will be gone from the scene in the next few years, and you can sense why we are passionate about these issues.

Several elements of the ABA reform principles ultimately were reflected in the Dodd-Frank Act. Unfortunately, others were not; indeed, several provisions of the final legislation were in direct conflict with those principles and harmful to the ability of all banks—and community banks in particular—to continue to provide the products and services that our customers want and that our communities need for robust and sustained economic growth and prosperity. For that reason, after careful evaluation, the bankers on the ABA Board of Directors unanimously decided to oppose the bill.

In saying that, I do not want to pass over provisions in the Dodd-Frank Act that ABA advocated and supported. ABA called for the creation of an interagency council tasked with monitoring systemic risk, which concept can be seen in the new Financial Stability Oversight Council. ABA strongly urged that the systemic consequences of accounting standards be included in the oversight duties of the Council, an idea that was made part of the law. ABA members' concerns about the outdated regulatory definition of core funding are addressed by the mandate in the law for a careful study of updating the definition. ABA was in the forefront of efforts to preserve the savings association charter, which maintained charter choice for hundreds of mutual and stock savings associations. Bankers were pleased that the legislation made permanent the already existing increase in deposit insurance to \$250,000 per account, since letting it expire was acknowledged by policymakers as unthinkable. These and other positive elements of the final legislation do not and cannot, however, overcome what bankers believe are serious problems in the Dodd-Frank Act, problems that bankers hope can be addressed and corrected in the implementation phase, either through appropriate regulations or wise corrections of the statute.

I do not propose to recount a lengthy list of provisions in the Dodd-Frank Act, but let me highlight a few that will have a significantly negative impact on community banks.

**Debit-Card Interchange.** Dodd-Frank places severe limitations on interchange income earned by banks servicing the debit-card transactions of our customers. Interchange is one of the most important sources of non-interest income for community banks, and the severe reduction in debit-card interchange income that would result from implementation of the Durbin amendment would be a major hit to the overall earnings of community banks. Your comments on the problems with this provision are very much appreciated.

**The Bureau of Consumer Financial Protection.** This new Bureau unwisely divorces consumer protection from safety and soundness concerns. Debit-card interchange is a good illustration of the problems with doing so. Advocates of the amendment claimed that it was supposed to help consumers, but Federal Reserve Board Chairman Bernanke testified that it is doubtful that any of the reduced interchange fees will ever find their way to consumers. It is clear, however, that this provision will dramatically reduce bank earnings, which will undermine the safety and soundness of banks, earnings being a key safety and soundness measure. How many similar mistakes might the Bureau make, pursuing chimerical consumer benefits for very real harm to bank safety?

As you know, the Bureau has no meaningful oversight and a very thin directive to “consult” with safety and soundness regulators. Moreover, even if it does not examine community banks, the Bureau will set the rules for nearly all of community bank business (since community banks depend heavily on providing retail banking services), bad news for community banks already collapsing under mountainous regulatory burdens.

Announced plans by Bureau proponents to “simplify” bank products will result in standardization that plays to the competitive advantage of banks that enjoy economies of scale and will restrict the ability of community banks to continue to offer the customized services that have been an important part of the small bank business model.

**New Capital Standards.** Dodd-Frank dramatically constricts the sources of capital for many community banks even while regulators and examiners are demanding more capital. Large banks will retain and develop alternative sources of capital that are not as readily accessible by community banks.

**Major New Reporting Regimes.** The new Bureau is authorized to require any information or reports that it wants from any bank at any time and in any form. Similarly broad information authority is given to the new Office of Financial Research, authority that is not limited to information from large banks. All banks will be subject to extensive new reporting requirements on business with women-owned, minority-owned, and small business firms, as well as some 20 new reporting obligations under the Home Mortgage Disclosure Act. Many studies have shown how community banks incur disproportionately higher costs for compliance with information reporting requirements.

**The Qualified Residential Mortgage (QRM) Definition and Risk Retention.** Dodd-Frank imposes dramatically more burdensome requirements on mortgage lending, which can only be avoided for loans called “Qualified Residential Mortgages.” All indications are that the QRM definition will be narrow and likely to curtail much of the ordinary mortgage lending currently done by lenders of all sizes. This will be especially harmful for community banks, because loans outside the safe harbor will require additional capital that is especially difficult and costly for smaller institutions to raise. Lately there also are proposals to use this rule as a vehicle for onerous new mortgage servicing rules, which will lead to more banks exiting or curtailing their mortgage lending businesses.

Moreover, many of what may appear to be benefits of Dodd-Frank are likely to be fleeting. The change in assessment base for deposit insurance premiums is likely to provide only temporary advantage at best for many community banks. Once deposit competition heats up, a mere increase of as little as 5 basis points in deposit interest rates would erase any gains obtained by banks from the shift to an asset-based assessment formula. Furthermore, Dodd-Frank removed the statutory ceiling on the Deposit Insurance Fund (DIF) ratio, the new authority for which the FDIC promptly exercised to double the target level of reserves for the insurance fund (despite Dodd-Frank provisions designed to reduce the likelihood and severity of bank failures).

I was troubled by your complaint that you only hear from bankers about problems, but never hear from bankers when we agree with FDIC actions. I had ABA staff check the record.

A review of ABA comment letters submitted to the FDIC over the past several years shows a very consistent pattern. The typical ABA comment letter acknowledges the elements of FDIC proposals with which bankers agree and respectfully points out what bankers believe can be improved and offers recommendations for improvements.

For example, ABA recently wrote in support of FDIC updates to Call Reports, noting that the FDIC proposal showed sensitivity to the already high reporting burden of banks. On the regulations implementing the change in the assessment base, we favorably commented on the FDIC's careful attention to implementing the law as written, and ABA wrote in support of the FDIC's proposal to use the Tier 1 capital measure to define tangible equity capital as well as the other steps that the FDIC took to simplify implementation of the new standard and not create new reporting requirements.

With regard to one of the most important emergency measures that the FDIC needed to take during the financial turmoil, ABA expressed support for FDIC's plan to require that banks pay three years of deposit insurance in advance. On a significant safety and soundness issue, the ABA publicly endorsed FDIC's overall plans to place deposit interest rate restrictions on troubled banks. With regard to Basel capital rules, we expressed public appreciation for FDIC's proposal to develop a menu of capital options, including the so-called Standardized Approach, to ensure that the complexity of the capital program matched the complexity of the operations of the bank. As you noted in your speech to the Government Relations Summit, ABA has supported robust orderly liquidation authority measures as a crucial part of ending too-big-to-fail. There are many more examples, but I think these make it clear that ABA support for FDIC proposals is not a rarity.

Bankers do not expect that regulators will always agree with us, nor should regulators expect that we will always agree with them. While we look at much the same issues, we look at them from different perspectives. Very often there is agreement. Equally important, the disagreement results in reconsiderations and reevaluations that often take initial ideas and proposals—whether from industry or from regulators—and make them better. The most fundamental issue that we agree on, and which makes for an enduring working relationship, is that all regulation must in the end benefit the customers.

In conclusion, I agree with your statement to the bankers at the Government Relations Summit, that, “the success of the financial sector is not an end in itself, but a means to an end – which is to support the vitality of the real economy and the livelihood of the American people.” Every day, every successful banker is thinking about how he or she can more effectively serve his or her customers and community, and fulfillment of that purpose is why bankers take pride in their banks. History shows that a healthy and prosperous banking industry is part of the real economy and that banks are deeply involved in the promotion of the vitality of the economy and the well-being of the American people.

Sincerely,

A handwritten signature in black ink, appearing to read "Stephen P. Wilson". The signature is written in a cursive, flowing style with some loops and flourishes.

Stephen P. Wilson  
Chairman and CEO  
LCNB National Bank