ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA

May 30, 2001

Robert E. Feldman, Executive Secretary
Attention: Comments/OES
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

Public Information Room
Office of the Comptroller of the Currency
250 E Street, SW
Mailstop 1-5
Washington, DC 20219
Attention: Docket No. 01-06

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551

Re: Prohibition Against Use of Interstate Branches Primarily for Deposit Production

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the agencies joint proposal to amend their respective regulations to implement changes made by the Gramm-Leach-Bliley Act (GLBA). GLBA amended the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal) by expanding the prohibition against the use of interstate branches for deposit production to include *any* branch of a bank controlled by an out-of-state bank holding company. This proposal would implement those changes.

Background

Riegle-Neal includes a provision that is intended to ensure that banks do not use their interstate branching authority to remove deposits from a community without reasonably helping to meet the credit needs of that community. The federal banking

[1] ICBA is the primary voice for the nation's community banks, representing 5,300 institutions at over 16,900 locations nationwide. Community banks are independently owned and operated and are characterized by attention to customer service, lower fees and small business, agricultural and consumer lending. ICBA's members hold more than $486 billion in insured deposits, $592 billion in assets and more than $355 billion in loans for consumers, small businesses and farms. They employ over 239,000 citizens in the communities they serve.

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agencies issued a rule in 1997 that provides that no sooner than one year after a bank establishes or acquires a covered interstate branch, the appropriate supervisor will determine whether the bank satisfies an established loan-to-deposit ratio screen.

The screen examines the loan-to-deposit of the bank's interstate branches in the state in question against all banks chartered or headquartered in that state. If the bank's statewide loan-to-deposit ratio is at least 50 percent of the host state loan-to-deposit ratio, it is considered acceptable. But, if the ratio is less than 50 percent, the agency must conduct a credit needs determination to assess whether the bank is meeting the credit needs of the communities served by the bank in the host state. If a bank fails to meet these tests, it could be subject to sanctions.

Revision

However, prior to GLBA there was a gap in coverage of the prohibition since it did not apply to all branches controlled by an out-of-state holding company. For example, branches retained in the original home state by a national bank that relocated a main office across state lines were not covered. To rectify this situation, the GLBA changed the definition of an interstate branch to include *any* branch of a bank controlled by an out-of-state bank holding company. And pre-GLBA, the prohibition only applied to out-of-state branches. It now applies to a bank controlled by an out-of-state bank holding company. The ICBA strongly applauds these steps taken by GLBA.

The proposed rule change would implement this statutory change and broaden the regulatory prohibition to include any bank or branch of a bank controlled by an out-of-state bank holding company (including a bank consisting solely of a main office).

ICBA Comments

The ICBA does not object to the agencies' proposal to revise the regulatory definitions in the rule to implement the changes made by the GLBA.

However, as we expressed in our May 5, 1997 comment letter (attached), the ICBA is still seriously concerned about the mechanism that the agencies are using to determine a host-state's loan-to-deposit ratio. Currently, the agencies are using a weighted mechanism that uses data from the Summary of Deposits report in conjunction with the Call Report data to produce an annual Host State Loan-to-Deposit Ratio report. The ICBA does not believe that this provides an accurate picture of loan-to-deposit ratios.

According to the agencies, their primary guiding force in developing this system was the Riegle-Neal mandate that they not impose any additional regulatory burden or data collection requirements on banks. However, we believe that this misplaces the emphasis on the Congressional directive in Riegle-Neal. As a result, there is a distortion of the primary purpose of Section 109 of Riegle-Neal and the mandate that interstate branches not be used as deposit production offices that siphon needed funds out of communities.

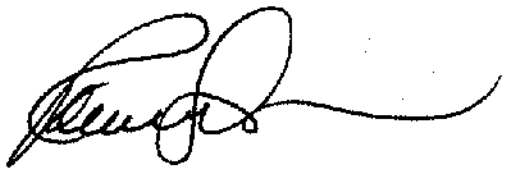
To comply with the primary mandate of Section 109 of Riegle-Neal, the agencies should require banks to report deposits and loans by state, for the reasons more fully expressed in our May 5, 1997 letter. Many banks should already have such information available through geocoding and other mechanisms.

Second, we must reiterate our concerns that the ratios are computed using June 30 Call Report data. While we understand that the agencies have an interest in using loan and deposit data that is produced as of the same date, and that the Summary of Deposits information is only provided as of June 30, the ICBA is concerned that this may understand host state loan to deposit ratios due to the cycle of agricultural loans which peak in the September 30 Call Report. Therefore, the ICBA again urges the agencies' to take this into consideration in calculating the host state loan-to-deposit ratios.

Finally, in the preamble to the current proposal, the agencies note that the Bank Holding Company Act defines the "home state" of a bank holding company as that state where total deposits of all banking subsidiaries are the greatest on the later of July 1, 1996 or the date the company becomes a bank holding company. The designation as of the 1996 date is now dispositive, even though deposit status may later change. However, because that definition was incorporated into statute by GLBA, the agencies feel they are bound by the determination as of July 1, 1996 (or the date the company becomes a bank holding company). Given that deposit levels change over, the ICBA believes this will lead to distortions that will become more and more pronounced. Therefore, the ICBA urges the agencies to support such a step if and when Congress considers it.

Thank you for the opportunity to comment. If you have any questions or need any additional information, please contact Rob Rowe, ICBA's regulatory counsel, at 202-659-8111 or at robert_rowe@icba.org.

Sincerely,



Robert I. Gulledge
Chairman

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Executive Vice President

May 5, 1997

Communications Division
First Floor
Office of the Comptroller of the Currency
250 E Street, SW
Washington, DC 20219
Docket No. 97-04

William W. Wiles, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Ave, NW
Washington, DC 20551
Docket No. R-0962

Jerry L. Langley, Executive Secretary
Federal Deposit Insurance Corporation
Attention: Room F-400
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: **Prohibition Against Use of Interstate Branches Primarily for Deposit Production**

Dear Sir/Madam:

The Independent Banker's Association of America (IBAA) is pleased to comment on the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Board of Governors of the Federal Reserve System (Federal Reserve) proposed rule prohibiting any bank from operating branches outside of its home state primarily for the purpose of deposit production, as required by section 109 of the 1994 Riegle-Neal interstate branching law. (P.L. 103-328, Title 1, Sec.109)

The IBAA is the only national trade association that exclusively represents the interests of the nation's community banks. IBAA represents 5,500 independent community banks nationwide that hold nearly $375 billion in insured deposits, $445 billion in assets, and more than $240 billion in loans for consumers, small businesses and farms in the communities they serve. IBAA members also employ more than 200,000 people in their communities.

Background and General Comments

Section 109 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal) directs the bank agencies to issue regulations to prohibit any out-of-state bank from using any authority in Riegle-Neal to engage in interstate branching primarily for the purpose of deposit production. These regulations are to include guidelines to ensure that interstate branches operated by an out-of-state bank are reasonably helping to meet the credit needs of that community. The statute also requires the agencies to determine whether the out-of-state bank's loan-to-deposit ratio in the host state is at least half the ratio of the total loans to total deposits for banks headquartered in that state. If it is determined that the bank's loan-to-deposit ratio in the host state is less than half of the host state average, then the loan portfolio must be reviewed in order to determine whether the out-of-state branches are reasonably helping to meet the credit needs of the communities they serve. If not, then the agencies may order that an interstate branch or branches of that bank be closed or may prohibit the out-of-state bank from operating a new interstate branch in the host state unless the bank provides reasonable assurances to the satisfaction of the agency that the bank has an acceptable plan to help meet the credit needs of the community.

The IBAA believes that the regulations proposed by the agencies under section 109 will not accomplish the stated Congressional intent of prohibiting the use of interstate branches primarily for deposit production. Data that is currently required to be reported by banks have significant limitations for purposes of section 109. For instance, banks are not currently required to submit loan or deposit data to the agencies on a state-by-state or branch-by-branch uniform basis. Without a reliable and accurate system to track loans and deposits for interstate branches, the agencies will not be able to make the determination, as required by the statute, whether the loan-to-deposit ratio screen is met or whether the interstate branch is serving the credit needs of the community.

In order to have accurate data on loans and deposits for purposes of section 109, the agencies would need to require additional reporting requirements, such as adding geographic data to the Call Report. Therefore, we believe there is a fundamental discrepancy between the requirements of section 109 and the one sentence in the legislative history that states: "The Conferees do not intend that section 109 create any additional regulatory or paperwork burden for any institution." Because the statutory language takes precedent over legislative history, the agencies' obligation is to write a regulation that will implement the statutory requirements. They certainly may--and we encourage them--to do so with a minimum of regulatory and paperwork burden, but the fact remains that they must adopt regulations as necessary to implement the requirements of section 109. Our specific comments on elements of this proposal follow.

Need for Loan and Deposit Data of Interstate Banks

Section 109 of the statute directs the agencies to calculate the loan-to-deposit ratios of interstate branches in a state using available information, including sampling the bank's loan files during an examination, or using other available data. In determining whether to sample a

bank's loan and deposit records, the agencies would consider whether the information would accurately reflect the bank's activities in a host state, and whether the information could be obtained without imposing undue regulatory burden. A credit needs determination would be conducted in all cases where the agencies conclude that sufficient data were not available without imposing additional regulatory burden.

However, the proposal itself discusses the significant limitations of currently available data. For example, Call Report data is not reported on a state-by-state basis. Also, the breakdown of loan and deposit data maintained by banks themselves differs from bank to bank. IBAA questions whether obtaining the information through "loan sampling" would result in accurate data, unless the sampling were extensive enough to provide a complete picture. And extensive loan sampling could by its nature impose significant regulatory burden.

In addition, reviewing the bank's loan files during an examination to calculate this loan-to-deposit ratio could produce unreliable data if a bank books loans or deposits at locations outside the state where the borrowers or depositors are located. For example, commercial loans and deposits may be consolidated at a bank's main office, while mortgage lending may be booked at a mortgage lending subsidiary. Although the loans may have been made at the branch, they would not be booked at that branch. Lastly, sampling of loan files would not provide information of loans that have been sold.

IBAA strongly believes that in order to properly accomplish the goal of prohibiting the use of interstate branches primarily for deposit production, an accurate system should be established by interstate banks to track loans and deposits by state, geographic area or branch. Again, we believe that the agencies will be unable to make the determination that the interstate branches meet the loan-to-deposit ratio screen or are serving the credit needs of the community without imposing additional reporting requirements on interstate banks to ensure deposits and loans are appropriately attributed to interstate branches.

Deficiency of Current Call Report and Summary of Deposits Data

Currently, Call Report loan and deposit data is collected on a consolidated basis and are not segregated by state, geographic area or branch. In addition, Call Reports reflect loans actually held on the books of the bank as of the end of the reporting period and do not reflect loans that have been originated and sold or that have been booked through affiliates. Those institutions subject to reporting requirements of HMDA and CRA (small business loan reporting by large banks) may have available lending data broken down by geographical location, but due to the limited nature of the data it is not that useful for the purposes of calculating loan-to-deposit ratios.

The Summary of Deposits Report collects deposit data on a branch-by-branch basis and can be aggregated by state or other geographical region. However, the Summary of Deposits Report does provide the most comprehensive information on bank deposits by location, but only provides information on the total bank deposits based on the branch in which

the account is located, it does not necessarily identify the location of the depositor and, thus, the location from which the funds come. Also, deposits may be booked at centralized locations and may include deposits from other states. The Summary of Deposits Report will not provide the data necessary to calculate the loan-to-deposit ratios of interstate branches or to determine whether the branch is meeting the credit needs of the community it serves. Additionally, the data does not track loans by branch and is only collected yearly.

Coding Loans and Deposits of Interstate Banks

In order to properly account for loans and deposits, we suggest the interstate banks use geo-coding by zip code of depositor or borrower address (or other appropriate coding method). The coding system for interstate branches must be monitored regularly so that the bank does not inadvertently violate the regulations on interstate branching by incorrectly assigning or omitting a deposit or loan. At this time, there is no regulation that prevents a bank from taking a deposit or loan at one branch, yet accounting for the deposit or loan elsewhere.

Looking at the Call Report and the Summary of Deposits Report, the IBAA agrees with the FDIC's conclusion that the Call Report is the most useful source of aggregate data. In establishing an alternative method of reporting geographic loan and deposit data for banks with interstate branches, the IBAA suggests that the Call Report include the information in the Summary of Deposits form, along with additional geographic data on loans and deposits by state. This information could be reported as a schedule in the Call Report twice a year. Reporting the information twice a year will eliminate the problem of stale data and enable interstate branches to properly comply with section 109.[1]

This information is also necessary for the agencies to implement Sections 101 and 102 of Riegle-Neal. Sections 101 and 102 and many state laws impose state deposit concentration caps to limit the percentage of deposits that one bank may hold in that state.[2] Some large banks have reached their state deposit concentration limits and are looking for ways to increase deposits. Unless properly restricted, banks with interstate branches may gather deposits in one state, but "book" them at a branch in another state in order to avoid violation of section 109 or a state deposit concentration limit. Establishing a universal coding method for interstate banks to track loans and deposits thus would aid the agencies in implementing other provisions of Riegle-Neal.

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[1]Colorado requires annual reporting of this type of loan and deposit data by MSA for banks that accept deposits or have branches in Colorado. The agencies may wish to review the Colorado requirements as an example of how one state has chosen to collect this data. For purposes of section 109, however, a state-by-state breakdown of data should be sufficient to determine whether the loan-to-deposit screen is met.

[2]Under sections 101 and 102, the agencies may not approve a merger or acquisition application that would result in a violation of the state deposit concentration limits.

General Accounting Office Data Study Erroneous

When Riegle-Neal was passed, Congress was concerned that information regarding the distribution of bank deposits and loans by state would be lost. As a result, a mandated study was performed by the General Accounting Office (GAO) entitled, "Material Loss of Oversight Information From Interstate Banking is Unlikely",[3] regarding the type of information reported to regulators that would be lost as a result of the implementation of Riegle-Neal.

In a flawed analysis, the GAO concluded that the implementation of Riegle-Neal is unlikely to result in a material loss of information necessary to perform regulatory and congressional oversight of banks. The study compared the information that existed prior to Riegle-Neal's enactment to determine whether, once enacted, it would likely result in a material loss of information. Ironically, GAO reached the conclusion that a material loss of information was unlikely because *current* record keeping and reporting requirements are already insufficient to accurately measure loan and deposit data by state. Incredibly, in assessing whether regulators have information necessary to perform their duties, the GAO failed to take proper account of the provisions of the Riegle-Neal Act itself which necessitate loan and deposit data by state in order to be properly implemented--namely, sections 101 and 102 imposing state deposit concentration limits, and section 109 prohibiting deposit production offices.

In comments submitted on the GAO report, the FDIC expressed concern with study's conclusions. The FDIC noted that until the 1990's the Call Report served as a reasonable proxy for geographic data because banks generally operated within one state. Riegle-Neal's authorization of interstate branching will change that dramatically. As the FDIC pointed out, "For the last decade banks have expanded their lending beyond traditionally geographic boundaries. To the extent this trend continues, the usefulness of institution-level data will continue to erode." According to the FDIC, its "primary concern with the GAO Report is that it does not emphasize that, given the current institution-based reporting scheme, interstate branching will exacerbate this adverse trend and eventually lead to what the FDIC considers to be a material loss of information used for statistical and economic studies that assist the FDIC in fulfilling its responsibilities." (GAO Report, page 21.) IBAA agrees that the "material loss of information" for regulatory and congressional oversight due to expanded interstate branching will be significant.

The GAO itself outlines the shortcomings of current record keeping and reporting requirements. It states that, "To the extent that interstate branching becomes prevalent, call report data--as currently collected and reported--will become less useful for approximating bank loan and deposit activity within a state" (GAO Report, page 3). "If a study were trying to determine the amount of loans made by banks to borrowers in a state or region, call report

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[3]BANK DATA Material Loss of Oversight Information From Interstate Banking is Unlikely (GAO/GGD-97-49, March 1997).

data alone, at least as currently collected and reported, could not answer the question" (GAO Report, page 8). In addition, the study points out that the Summary of Deposits data would still be available to measure deposit activities that are booked to a particular state, but would not provide information on the geographic source of the deposits (GAO Report, page 4).

Surprisingly, although the study reports that, "To the extent that interstate branching becomes prevalent, the usefulness of information reported to bank regulators, which is currently used to compile banking data on a state-by-state basis, would become even more problematic" (GAO Report, page 9), the GAO concludes that regulatory oversight will not be diminished.

Finally, we note the FDIC's specific comments on the GAO study directly addressing the deposit production office prohibition of section 109 of Riegle-Neal: "GAO's characterization of the requirements of section 109 of Riegle-Neal...differs from the FDIC's understanding of that section. In our opinion, the federal regulators do not have, at this time, sufficient information on total deposits and total loans by state in which the depositor or borrower is located to appropriately determine" bank compliance with the loan-to-deposit ratio established by section 109. GAO Report, page 23.

IBAA strongly believes that in order to properly comply with Riegle-Neal, this problem needs to be resolved. IBAA, therefore, urges the agencies to implement appropriate record keeping and reporting requirements in order to collect the data necessary to properly enforce the deposit production office provision of Riegle-Neal.

Host State Loan-to-Deposit Ratio

The agencies anticipate that the host state loan-to-deposit ratio would be calculated jointly by the agencies from the data reported by banks in the Call Reports by dividing the total dollar amount of outstanding loans held by home state banks by the total dollar amount of deposits held by such banks. However, data for specialized banks that do not engage in traditional deposit taking or lending may distort the host state loan-to-deposit ratio. Limited purpose banks, such as credit card banks and wholesale banks, could have very large loan portfolios, but few, if any deposits. The agencies anticipate that the host state loan-to-deposit ratio would exclude these types of banks.

Additionally, the agencies note that deposit taking and lending activities of multistate banks could distort the ratios. Call Reports do not allow the assignment of a multistate bank's loans and deposits to particular states. Excluding multistate banks completely could distort the host state loan-to-deposit ratio. The proposal suggests that multistate banks that have more than 50 percent of their branches outside of their home state could be excluded, however, any methodology that excludes multistate banks could eventually result in a host state with few, if any, banks eligible for calculating the host state loan-to-deposit ratio as interstate branching becomes more prevalent.

These factors lend strong support to IBAA's argument that multistate banks should be required to report their loans and deposits by state. With this information, the agencies would be able to calculate host state loan-to-deposit ratios that would not be distorted because all loans and deposits of a multistate bank were assigned to its home state. Again, IBAA urges the agencies to establish appropriate measures to gather reliable state-by-state data about an interstate bank's loans and deposits.

We also urge the agencies to use September 30 figures when computing the statewide average loan-to-deposit ratios in rural/agricultural states because of seasonal lending in these states. The September 30 quarter is typically when the agricultural lenders have the highest loan-to-deposit ratio during the course of the year. Using data from any other quarter end would understate the true loan-to-deposit ratio for host state banks in these states and would set the loan-to-deposit ratio screen for interstate branches at an artificially low level.

Credit Needs Determination

IBAA agrees that the factors identified by the agencies as relevant to make the credit needs determination are appropriate. Indeed, they are taken directly from section 109 (c)(2) of Riegle-Neal.[4] However, Riegle-Neal also requires the regulations issued by the agencies under section 109 to "include guidelines to ensure that interstate branches operated by an out-of-State bank in a host State are reasonably helping to meet the credit needs of the communities which the branches serve" (section 109 (b)). We question, however, whether by merely reciting the statutory factors listed in section 109(c)(2), the agencies have met the requirement to issue guidelines under section 109 (b).

We agree with the agencies that the information from a CRA performance examination should be particularly relevant in determining compliance with section 109 because it directly evaluates a bank's efforts to assist in meeting the credit needs of its communities. In addition, for banks with interstate branches, the agencies are required to write separate CRA evaluations for each state and discuss separately the bank's CRA performance in each metropolitan area, as well as the non-metropolitan area of the state.

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[4]In the making the determination whether the bank is reasonably helping to meet the credit needs of the communities it serves in the host state, Section 109(c)(2) requires the agency to review the loan portfolio of the bank and consider the following: 1) whether the interstate branch was formerly part of a failed or failing institution; 2) whether the interstate branches were acquired under circumstances where there was a low loan-to-deposit ratio because of the nature of the acquired institution's business; 3) whether the interstate branch have a higher concentration of commercial or credit card lending, trust services, or other specialized activities; 4) the ratings received by the bank under CRA; 5) economic conditions, including the level of loan demand within the community; and 6) the safe and sound operation and condition of the bank.

However, CRA regulations and exam procedures for large banks do not specify how often each metropolitan area will be assessed. In fact, the exam procedures direct the examiner to use a sampling of assessment areas and "choose *one* or more assessment areas in each state for examination using these procedures" (emphasis added). Since these exam procedures are not scheduled to be implemented until July 1, 1997, we currently do not know how thorough the agencies will be in covering all the interstate branches in a host state. Thus, the available CRA performance evaluation for a given interstate bank may be insufficient to adequately make the credit needs determination for purposes of section 109. For banks that do not meet the loan-to-deposit ratio screen, the agencies should assess the adequacy of the existing CRA evaluation for purposes of section 109 and conduct further investigation as warranted.

Timing of Reviews

According to the proposal, the agencies expect to review a bank for compliance with the deposit production office rule when it initially rates the CRA performance of an interstate bank in a particular state. Subsequent reviews will be conducted as the agencies "deem appropriate." As such, the proposal does not provide for regular periodic review of an interstate bank's compliance with section 109. In our opinion, this omission is not consistent with the statute. Proper enforcement requires regular periodic reviews. The IBAA strongly recommends that the agencies revise the proposed rules to require review of compliance on an annual basis.

Loan-to-Deposit Screen

Section 109 applies a loan-to-deposit ratio screen of 50 percent of the average loan-to-deposit ratio of host state banks. IBAA believes this test is extremely easy to meet, as the loan-to-deposit ratio requirements are extremely low and the banking agencies are given broad latitude to determine if the interstate offices are meeting the local community credit needs (if the banks do not meet the ratio). In turn, a statewide test is inadequate to protect many Main Street towns and communities. While we recognize a statutory amendment would be required, making the test a bright line test, unless very stringently drawn circumstances apply, would help. Additionally, IBAA supports an increase in the average loan-to-deposit ratio threshold from 50 percent to 80 percent, which would also require a legislative change.

Conclusion

The IBAA strongly believes that as banks continue to expand their lending beyond traditional boundaries and establish interstate branches, they must be closely monitored to ensure that they do not operate these branches as deposit production offices, draining deposits and lendable funds away from host state communities. However, currently available data is insufficient for this purpose. Without a reliable and accurate system of reporting loans and deposits by state, the agencies will be severely hamstrung in their ability to enforce section 109 of Riegle-Neal. As proposed, we do not believe that the regulations under section 109 will accomplish the goal of prohibiting the use of interstate branches primarily for deposit production. We urge the agencies to implement appropriate record keeping and reporting

requirements for interstate banks in order to collect the data necessary to properly enforce the deposit production office provision of Riegle-Neal.

Thank you for the opportunity to comment.

Sincerely,

Bill Sones
President