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March 27, 2019

Robert E. Feldman
Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, D.C. 20429
(comments@fdic.gov)

Re: Request for Information on the FDIC Deposit Insurance Application Process
RIN 3064-ZA03

Dear Mr. Feldman:

I and my law firm, Baker, Donelson, Bearman, Caldwell & Berkwitz, PC, have worked with over 60 de novo bank institutions for the last 30 plus years. Our legal services include assisting them in obtaining federal and/or state regulatory approval to operate, preparing legal organizational and governance documents, preparing securities disclosure documents, preparing operational documents and policies, and providing other related legal services. As a matter of fact, I personally authored a book entitled Starting De Novo Banks, published by Sheshunoff & Company in 1999. Our firm also has been involved in two de novo bank openings in the last couple of years during a time when there were practically no de novos in the whole country approved and opened.

In advising clients who would like to begin operating a financial institution with insured deposits, we generally discuss alternatives to the de novo charter which are much easier, quicker, and may offer a greater return to shareholders. These include purchasing a currently insured institution outright, affiliating with a currently insured institution to provide capital to grow the bank into new markets, and other partnership or contractual arrangements where a client remains a separate entity but does business with an insured institution. The recent efforts by the FDIC and other regulatory authorities to encourage more de novo charters is applauded, but under the current environment without some significant changes in the approval process, we continue to encourage our clients to seek other alternatives.

Following are some specific suggestions that the FDIC and other federal and state regulators might want to consider to bring the de novo charter process to the top of the list:

1. Transparency for Minimum Capital Requirement. The minimum capital required for a de novo institution as determined by bank regulators has always been a mystery. While the FDIC guidelines suggest that a bank should maintain at least an 8% leverage ratio for three years, this criteria seems seldom to be the basis for the ultimate capital required. When I began forming de novo banks in the 1980s, it was assumed that a de novo institution would experience losses for the first year or two and then begin earning so that the retained earnings account of the bank basically would catch up to $0 at the end of three years[1]. Using the 8% required minimum capital, if the bank projected $100 million in total assets at the end of three years, the minimum required up front would be $8 million. This formula seemed to work until 1989, when The Bank of Nashville, who we represented, proposed $20 million in capital even though its three-year projections were not close to $250 million. The excess capital was proposed by the institution in order to have a buffer to support growth that either exceeded projections or might have occurred after three years. At the time, this was one of the most highly capitalized de novo banks in the country.

After that time, the FDIC continually required banks to propose capital greatly exceeding the 8% required minimum capital to support the projected growth in assets. The explanation was always that the regulators had made a determination of the higher capital requirement based upon internal analysis, but this analysis was never to my knowledge shared with the applicant institution. Were the regulators projecting higher growth, had they internally adopted a higher capital ratio requirement, or were there other factors being considered? One of the main questions that I am always asked by organizers is how much capital will they need to raise, and to this day, I am unable to answer that question. I would request that the regulatory agencies provide more transparency and share their formulas and standard analysis with organizers and their attorneys so that we can better answer this question.

2. Designated Experienced Application Reviewers. The typical regulatory personnel who review applications for deposit insurance seem to be the more experienced case managers located in regional or sub-regional offices. While these personnel have great examination experience for ongoing institutions, with the lack of de novo applications over the last ten years, they do not necessarily have the experience in analyzing the additional factors that would apply to a de novo application especially for non-traditional business plans. Until this experience is built back up, it would be my suggestion that certain application analyst be designated in the Washington office as the main contacts for the applicant in order to provide more standardized analysis and expedited processing.

3. Processing of Bank Holding Company Applications Earlier. This may be more of an issue with the Federal Reserve, but hopefully the agencies can work together to expedite the processing of applications where a de novo bank wishes to form a bank holding company on the

[1] In more recent times, de novo banks begin having earnings much earlier in their first three years, but the startup costs (salaries, facilities, and other organizational expenses), which might be incurred a year or more during the lengthy application process, are all required to be expensed rather than amortized. This is why it takes the bank longer to break even. Maybe the accounting for these expenses could be changed to assist the bank?

front end. Currently, the Federal Reserve will not even consider the bank holding company application until the application for deposit insurance has been approved. This delays the opening process and possibly the capital raising process by at least 60 days, if not more. As a result, many institutions chose not to form a bank holding company on the front end to reduce the delay. Unfortunately, they may lose some of the benefits of having a bank holding company on the front end. An easy fix is for the Federal Reserve to be willing to consider the bank holding company application concurrently with the de novo bank subsidiary application for deposit insurance.

4. Allowing Capital Raise Earlier. The earlier in the process that the de novo institution can begin raising capital the viability of the proposal can better be determined. While this may be more a function of state law for state chartered banks, any barriers in the federal application process that would prevent the institution from raising capital as early in the process as possible should be eliminated. Funds must be placed in escrow anyway and would be refunded to the subscribers in the event the application is not approved or sufficient funds are not raised.

5. Blunt Response to Proposed Directors and Management. In many application processes in which I have been involved, there have been a proposed officer or director that created some questions by the regulators as to their ability or experience to serve as such. Many times, these questions are not raised early in the process, and lengthy conversations and written requests for additional information go back and forth without an ultimate resolution. Without the regulators actually turning someone down, the questions raised and the length of the review process on particular individuals usually leads to the applicant withdrawing such individuals for consideration even when that person might ultimately be determined to have been qualified and an asset to the institution. Also, there is great embarrassment to the person whose name may have to be withdrawn from consideration. My suggestion is that the review process of the proposed officers and directors be a priority in the application review process so that a final decision can be made quickly on whether the person will continue to be included in the proposed application. Also, instead of the regulators "beating around the bush" about an individual, they need to be more straightforward about their concerns and whether the individual ultimately can be approved or not.

6. Allowing Business Plan Amendments During First Three Years. One of the FDIC guidelines and ultimately a condition to any approved de novo application is that any changes in the proposed business plan during the first three years must be preapproved by the regulators. I have no problem with this requirement, but in my experience, such proposed amendments are rarely approved and even discouraged. The banking world is rapidly changing, and there may be opportunities that could benefit a bank and its customers and community if the business plan could be modified. Examples which are very typical are the implementation of specialized lending programs such as a mortgage or SBA department. Even though these are just typical types of lending engaged in by commercial banks, these are considered amendments to the business plan. More flexibility needs to be allowed in considering amendments, or alternatively, not considering slight changes in products and services to even be considered an amendment to the business plan in the first place.

7. Real Analysis of Economic Need. Traditionally, it seems that the regulators only give "lip service" to economic need. I have been told that need is measured more by the organizers ability to raise capital rather than any actual economic analysis or impact on competition in a market. A de novo institution being proposed in a $3 billion deposit market probably does not require much economic analysis, but when the proposal involves a smaller community, the financial impact on competing institutions should be taken into account.

8. Confirmation That Institution Can Be an LLC or Other Type of Non-corporate Entity. Many state laws, such as Tennessee, allow for a bank to be organized as a limited liability company in addition to the traditional corporate structure. While regulators do not seem to oppose this structure, the path of least resistance tends to favor a corporate structure over an LLC structure, even though the LLC may have more desirable tax ramifications for the shareholders. It would be helpful if the bank regulators made a more affirmative statement that LLCs or other types of entities are acceptable.

9. Simplify and Clarify IBFR. This is a broader question than just the de novo application process, but the Interagency Biographical and Financial Report has had almost no changes to it in the 37 years I have been practicing. The complexity of the form causes even the most sophisticated proposed director and officers and their accountants to leave off information so either we as counsel or ultimately the regulatory agencies have to request additional information. I am sure there are a number of questions that have to be answered that really are not even considered by the regulators as being that important; for example, a projection for the next couple of years of cash flow could be argued as relevant, but is it really, especially when it's just a guess anyway? Also, there are a number of questions in the financial section that are proceded by a chart to fill in, but the headings on the chart do not match the questions so that the person filling out the form tends to just answer the question based upon the headings of the chart.[2] Even if the preparer notices that the questions exceed the chart headings, they cannot be answered with the chart since there is just not enough room. Finally the complicated nature and extreme amount of disclosures, which are greatly in excess of what most banks require in their lending function, almost always discourages one or more potential directors to be involved, which limits the director pool from which a de novo bank can access. By simplifying and clarifying the form, I think both the applicants and the regulators examining the information can concentrate on the most relevant information.

10. Application Form Simplification. Similar to the IBFR, I believe a question-by-question review of the application for deposit insurance should be conducted to determine if all of the questions are really necessary. On the other hand, there are always additional questions asked about a proposal that are not included in the application, so any such internal questions

[2] For example, in Schedule F of the Financial Report, the latest version of the IBFR does provide better headings than the old version, but the specific request to provide "the original date, loan amount, and co-makers, if any, and their percent obligation" in the instructions is still not clear when the heading in the chart merely says "Name and Address of Creditor and Loan Origination Information."

that are guidelines to the examiners should be reviewed to determine if any should be in the application form itself.

11. Nontraditional Applicants. Nontraditional applicants such as proposals with unique delivery methods or niche types of lending are becoming more prevalent. On the other hand, any proposal that is not a strict traditional commercial banking proposal seems to take a much longer time to be processed. I understand that such a unique proposal may need more review, but with prevalence of such proposals, the examiners should make additional efforts to expedite the process and not find excuses to slow it down.

This is also an area where Community Reinvestment Act (CRA) changes under consideration need to be made. Many nontraditional proposals will not include typical retail branch locations, which completely throws off the examiners' analysis of CRA compliance. As the heads of various regulatory agencies have recently proclaimed, the ultimate goal of CRA is to make sure that credit needs are being serviced where they are needed the most, and the process of delivering these services should remain flexible. Going back to an application I helped file in the 1990s, this issue was a major holdup for a bank that wanted to deliver its services through third-party agents without any public bank-owned facilities. We were required to hold public hearings on how to assess the needs in the county where the administrative office was located, even though the services were being offered statewide through these third-party agents and traveling loans officers of the bank. We went through considerable trouble and delay just to meet the technical aspects of CRA, and even after the bank was approved, CRA analysis continued to be conducted based on the county, rather than the whole state. Either the de novo application process itself or a full revamp of CRA needs to be made to prevent this situation.

12. "De Novo" Rules. Above, I have already addressed the issues surrounding the transparency of the 8% capital calculation and the strictness of the business plan change rules. In addition, it would be helpful for the regulators to re-examine the limitations placed on what organizers or initial capital contributors can be awarded for their extra time, efforts, and risks taken. Basically, the rules only allow for stock options to be used for this type of incentives or compensation, and the exercise price can be no less than the price of the shares offered to everyone else. I understand that the FDIC does not want the issuance of FDIC insurance to create an automatic shareholder gain, but it is not like these shareholders are going to immediately cash-out and take advantage of that gain. This seems to be the only time that the regulators even consider shareholder value in the analysis, and in this case, the consideration is a negative incentive for the participation of potential organizers and shareholders. Additional incentives, for example, allowing discounted shares or options, should be allowed.

13. Overall Expediency in Processing. The de novo application process is so slow that no matter how much the regulators try to encourage the formation of de novo banks, organizers will always consider alternatives to engaging in the banking business as described in my initial paragraphs above. Similar to the process used by the Federal Reserve in considering various types of applications, I would suggest that the other bank regulators consider either internal or public timeframes for processing the various aspects of the application. For example, when processing a bank holding application, the Federal Reserve typically allows for three

weeks to respond to a draft application, two weeks to either accept or ask for additional information on a final application, and thirty days thereafter for processing an application. The processing period can then be extended, but only for certain reasons. Also, when questions are raised with an applicant, the Federal Reserve typically only allows a certain number of days (usually eight days) for a response to be submitted, subject to extension for good reason. If the de novo application process also was subject to specified timeframes, the whole process could be expedited and more de novo applications would be encouraged.

I am more than happy to discuss these or other related issues with you and your staff directly. Thank you for the opportunity to offer my comments.

Sincerely,

[redacted]

Steven J. Eisen

SJE/plb
cc: Commissioner Greg Gonzales (greg.gonzales@tn.gov)
Colin Barrett, Tennessee Bankers Association (cbarrett@tnbankers.org)