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December 9, 2018

Via Electronic Submission

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

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

Dear Mr. Feldman:

University Bank[1] is pleased to comment on the Request for Information on the FDIC's Deposit Insurance Application Process. Our comments focus solely on question #12[2] and question #1.[3] We will first address question #1, then question #12:

1. Make it easy for existing banks and bank holding companies in good standing to form a new bank charter. Create a streamlined process for them to make it easy and paperwork light.

An existing bank or bank holding company may want to raise capital and form a de novo bank for a niche business opportunity or to enter a new geographical area. The existing bank shareholders may not want to dilute their interest in the existing bank or bank management may believe that it is easier to recruit the talent and raise the capital for the new business opportunity under a new bank charter. The FDIC should encourage this and offer a streamlined process for them to apply for and

[1] Founded in 1890, University Bank® is the 15th oldest bank headquartered in Michigan. We are proud to have been selected as the "Community Bankers of the Year" by both American Banker magazine and the American Bankers Association and as the second fastest growing business of any type in the Greater Detroit Region by Crain's Detroit Business. As of 9/30/2018, University Bank was managing over $21.6 billion in financial assets for over 125,000 customers and our 394 employees make us the 5th largest bank based in Michigan. University Bank is a state chartered community bank, with on balance sheet assets totaling approximately $265.6 Million. We operate one branch office in Ann Arbor Michigan.
[2] "12. Are there legal, regulatory, economic, technological, or other factors separate from the application process that discourage potential applicants from submitting applications for deposit insurance that the FDIC should be aware of? If so, are there steps the FDIC could or should take to mitigate the impact of such factors?"
[3] "1. What steps, if any, can the FDIC take to improve the de novo application process?"

obtain a new bank charter under the same bank holding company, a new or existing separate bank holding company, or as a standalone bank without a bank holding company. If the new bank charter meets certain criteria, such as having proven in common management, in common board members, in common compliance, in common infrastructure and in common core IT systems with an existing successful bank, the process should be made very light and easy. Banks and bank holding companies with CAMELS ratings of 1 or 2 and compliance ratings of 1 or 2 should be able to access this streamlined process.

In addition, for all bank deposit insurance applicants, the FDIC should create and offer an intelligent web form based service that acts as an expert system to guide applicants through the application process and actually helps them create the actual application to be submitted to the FDIC. It should be easy enough that an experienced bank CEO could, without any outside consulting assistance, complete all the forms online. Outside consultants, while useful, are expensive and this expense deters applications and is just another barrier that is unnecessary.

Now turning to question #12:

12. All De Novo Banks Begin Life as Community Banks. Raising Capital for Community Banks has become Unnecessarily Difficult Due to Bad Government Regulation

The new Chair of the SEC, Walter Joseph "Jay" Clayton III, recently stated, "The total number of listed companies in 2016 was approximately 4,300, compared to about 8,100 in 1996,", "…the [roughly 50%] reduction in the number of U.S.-listed public companies is a serious issue for our markets and the country more generally", and "I believe we need to increase the attractiveness of our public capital markets without adversely affecting the availability of capital from our private markets."[4]

Similarly, the new Chair of the FDIC, Jelena McWilliams, recently stated, "The lack of de novos—with just a handful since Dodd-Frank was passed—has accelerated an already rapid consolidation trend, and there are now less than 5,600 U.S. bank charters."[5]

When I entered community banking 30 years ago, back in 1988, the banking industry was still expanding. The number of banks was around 20,000 — and growing every year. The nearly 75% reduction in the number of banks is driven by a number of trends including a new and improper focus by bank supervision on an unattainable and counterproductive goal and a ill-considered philosophy that drives bank legal compliance that is both hugely expensive and of no benefit to consumers, and that economically encourages banks to merge[6]. However, the barriers to raising

[4] https://www.sec.gov/news/speech/remarks-economic-club-new-york
[5] https://bankingjournal.aba.com/2018/12/a-fresh-perspective/

[6] The focus of bank regulation has changed radically over the past 30 years and is now focused on ensuring that banks don't fail. This goal actually increases the number of banks that merge or fail. Another key factor driving regulatory costs higher is a philosophy that detailed legal disclosures are beneficial to consumers — as best exemplified by mortgage disclosures that now stack six to nine inches high — yet these documents are expensive to create and in the real world consumers don't actually read them. See: American Banker, "Don't let community banking go from endangered to extinct", by Stephen Lange Ranzini (October 17 2017). The text of this article is appended to this comment letter as an endnote.

capital are a major contributing factor to the rapid decline in the number of banks, as they cause more banks to fail and also reduce the rate at which new banks are formed.

By modifying these bad government regulations governing capital raising, the FDIC and SEC could serve the nation more successfully in encouraging capital formation and investment in entrepreneurial small and medium sized businesses, and especially how to encourage companies to go and stay public, an area where the U.S. has unfortunately fallen behind several other more advanced countries around the world. If this problem could be solved, many benefits would accrue to our nation, including a faster rate of long term economic growth and job creation, a key priority of our national leaders.

I have had the privilege of serving as the President & CEO of a bank holding company, University Bancorp, Inc., for the past 30 years. From January 1990 to January 2009 our firm was publicly traded on NASDAQ and our common stock was SEC registered. Our story of why we delisted should illustrate to you several policies that should be corrected.

We went public via merger with an existing NASDAQ firm that had a poor business plan and management savvy enough to realize this fact before it was too late, and who then liquidated the business. Essentially the firm we merged our bank into was a cash shell with $400,000 of cash. At that time, a NASDAQ Small Cap Stock Exchange listing cost $4,000 a year. The cost of a public company audit was about $25,000 more than a private company audit. Bank Call Reports filed with their banking regulators were about 10 pages in length.

Since NASDAQ's fees were not effectively regulated by anyone and because after the AMEX was acquired by the NYSE and the regional stock exchanges (e.g. Chicago, Philadelphia and Boston) all went out of the stock listing business, there was no real competition, and NASDAQ was able to raise our annual fees in stages up to $40,000 a year.

Today we are listed on the OTCQB Stock Exchange and our annual listing fee is $10,000. The OTCQB Stock Exchange has market making comparable or better to what the NASDAQ Small Cap used to be, and it has information disclosure requirements better than what the NASDAQ used to require. For example, as a bank, we are required to post our quarterly Bank Call Reports within 60 days of quarter-end. These Bank Call Reports are now about 100 pages long and contain an incredible quantity of data. We are also required to attest and update a long list of information about our firm and its principals and outside key vendors every six months. All this information is available online to investors. OTCQB is a superior stock exchange to the old NASDAQ Small Cap. This leads me to my first recommendation:

> **1) Make the OTCQB and OTCQX a "National Exchange" for the purposes of all regulation, including IRS regulations and Blue Sky Regulations.**

To illustrate, the IRS regulation around ESOPs requires an annual appraisal of the company, which costs us $4,500 a year, if the stock is not traded on a National Exchange, which is currently defined as only the NYSE, AMEX and NASDAQ. The ESOP also then cannot buy or sell shares except at this annual appraised value or less during the year unless the stock is traded on a National

Exchange. It's just another hassle that doesn't protect anyone except the NYSE, AMEX and NASDAQ business model.

The General Counsel of OTC Markets, which manages the OTCQB & OTCQX Stock Exchanges, provided to me a three page list of 14 points of regulatory changes that they have requested of the SEC to eliminate the disadvantages that current regulation puts their exchanges under. The companies that list on them are also therefore placed at a disadvantage[7]. Since 900 of the 5,600 banks are listed on either the OTCQB or OTCQX stock exchanges this issues is of critical importance to the FDIC and the banking industry in general. In addition, most de novos would initially find it most cost effective to be listed on these exchanges and not be SEC registered but subject to the FDIC's jurisdiction for purposes of their publicly issued capital securities. Therefore we believe that:

> **2) The FDIC should talk to OTC Markets, the parent of the OTCQB and OTCQX stock exchanges, and find out additional ways to put them on a level playing field with the NYSE and NASDAQ. The FDIC should examine the 14 point list of securities law and regulation changes advocated by the General Counsel of OTC Markets and adopt for banks any of the recommendations that apply to banks.**

Because the accounting profession controls their regulator, the PCAOB, whose board is staffed with accountants, and the FASB is staffed nearly entirely by accountants, each year the FASB was able to add new and more complicated accounting principles to the GAAP audit requirements. Each year there is guaranteed to be changes to GAAP, because this is how the accountants assure that their billings get amped up. If GAAP didn't change, the cost of an annual audit would drop 10-20%. The cumulative cost of these changes adds materially to the cost of an audit over time. By 2009 the cost of our annual audit had risen from $50,000 a year to $250,000 a year even though our bank had only doubled in size.

Then came the Sarbanes–Oxley Act (SOX) and its requirements around audit attestation around internal controls (section 404). Implementation was delayed several years for small companies until finally it was required for annual audits for all years ending after December 15, 2008. Our auditor informed us that the cost of the annual audit would rise from $250,000 to $500,000 and that is why we delisted. As noted by research:

> The cost of complying with SOX 404 impacts smaller companies disproportionately, as there is a significant fixed cost involved in completing the assessment. For example, during 2004 U.S. companies with revenues exceeding $5 billion spent 0.06% of revenue on SOX compliance, while companies with less than $100 million in revenue spent 2.55%.[8]

SOX is very misguided because it was an expensive solution when a simple solution would have sufficed. SOX was passed in response to the frauds at Enron and WorldCom. These firms engaged in complicated self-dealing transactions. A simple reform would have prevented future similar frauds from occurring:

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[7] This three page list is appended as the second endnote to this letter.
[8] "Final Report: Advisory Committee on Smaller Public Companies", https://www.sec.gov/info/smallbus/acspc/acspc-finalreport.pdf.

3) Disclose in Footnote 1 of the Financial Statements the level of materiality of the audit. In the case of Enron, it was $100 million. This means that the audit was allowed to pass on errors of up to $100 million. If investors knew this, they would never have bought the stock.

4) Disclose in the annual proxy statement the complete text of all insider related agreements. In the case of Enron and WorldCom, if the shareholders had received a proxy in the mail the size of the New York City Yellow Pages, they would have rushed out and sold the stock. They didn't even need to read the document to know the corporate culture was rotten to the core.

Recommendation #3 above is not even permitted under GAAP, because the accountants don't allow it. I asked my outside audit firm one year to include the level of materiality of our audit in Footnote 1 and they flat out refused to allow it. The solution here is to reform FASB and the PCAOB, so that the boards are by statute required to have board members who meet the following criteria:

5) 1/3 of Board Members should be accountants with a CPA degree;
1/3 of Board Members should be CFOs of publicly traded companies;
1/3 of Board Members should be institutional investors who use & analyze financial reports.

I assure you if the FASB and PCAOB boards were constituted this way, the number of future changes in accounting standards would decline precipitously and stupid rules, such as mark to market[9] and various detailed disclosures that add little to no value, but tremendous cost to an audit, would be pared back over time.

However in the meantime:

6) The FDIC could apply their own principles to banks that opted into a Regulatory Accounting Principles (RAP) based regime with these superior rules. This would enable small and midsize banks to access a lower cost regulatory regime.

Ironically, the FDIC holds our bank to a higher standard when it comes to the accuracy of our financial disclosures. When we file our Bank Call Report, each field of the 100+ pages of data we submit quarterly must be accurate to within $1,000. Our auditor told our audit committee informally that our level of materiality for our audit is somewhere in the $100,000 to $150,000 range depending upon the item. This leads to my fifth recommendation:

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[9] For an overview of the history of how mark to market accounting nearly destroyed the U.S. banking system during the Great Depression, see: https://seekingalpha.com/article/125914-mark-to-market-the-bogeyman-of-the-1930s-is-back

7) Allow heavily regulated firms[10] to file the quarterly or semi-annual financial reports that they file with their primary regulator to serve in lieu of SEC required reports if those reports are filed timely with an exchange that provides access to that information on demand to investors.[11]

Firms that are heavily regulated are already under great scrutiny and the detailed SEC disclosures serve little value added, yet increase materially the cost of being public. If the Call Report is sufficient for the FDIC to monitor the condition of banks, it should be sufficient to serve the needs of investors for periodic reporting on the condition of publicly traded banks.

8) The FDIC should unilaterally adopt via rules these reforms outlined in recommendations #3, #4, #5, #5, #6 and #7 for all banks that have publicly traded securities, even if the SEC does not agree to do so.

Because Congress since 1990 has imposed banking regulations that severely restrict the ability of banks to provide credit to start-up and growth stage firms that do not have a demonstrated track record of profits, and because Wall Street won't fund them as discussed below, angel capital and venture capital provide assistance to entrepreneurs to get their businesses the capital they need that is unavailable elsewhere. Without access to capital, these firms would never get off the ground or would struggle for years and never achieve much until they die from lack of capital or entrepreneurial fatigue. Good and viable business concepts would not be translated into reality, many jobs would not be created and the growth rate of our local, Michigan and national economy would be lower. Social ills would all therefore be higher.

Over the past few years over a half dozen of Ann Arbor's most rapidly growing and successful venture capital backed firms have been sold and relocated out of Michigan. This is a natural consequence of an inherent flaw in the venture capital model. As a former venture capitalist (our fund, Michigan Business Development Company backed 27 firms in Michigan and those firms raised over $270 million of capital and created over 700 "base" economic jobs and had a 35% annual return for the seven years it was in business), I believe that while VCs overall are a very positive force for good, however it is not all positive. The problems with firms being primarily venture capital backed are:

A. VCs want to buy control of a firm. They start with over 50% ownership. Two rounds of capital raising later and the founder and original angel investors usually own well under 25% of the VC backed firm.
B. VC funds usually have a seven year life on investments and any portfolio investments that cannot be liquidated within seven years becomes a problem "zombie" investment. If a VC generates too many zombie investments, it can destroy the fund's entire track record and prevent the VC fund sponsors being able to successfully raise new VC funds to continue in business as a venture capitalist.

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[10] Firms that file detailed financial statements quarterly or semi-annually include: Banks, Bank Holding Companies, Insurance Companies, Public Utilities, Mortgage Banking Firms, SBICs and BIDCOs, to name a few.

[11] Exchanges that require this include the NYSE, AMEX, NASDAQ, OTCQX and OTCXB Stock Exchanges.

C. VC backed and controlled firms no longer have access to the financial markets to do initial public offerings. There used to be a path to the stock market through regional broker dealers for growing firms with a $25 million to $50 million market capitalization such as Roney & Co or First of Michigan in Michigan and other regional brokerage firms elsewhere, but Wall Street gamed and manipulated the rules at the SEC, undermining this regional broker business model, and Wall Street gobbled them all up. Now Wall Street focuses on large initial public offerings over $500 million. As a result, when seven years are up, management cannot raise the capital to buy out the VCs and the only viable exit for VC backed firms is to sell the firm to the highest bidder, often an established competitor located out of state.

The impact for Ann Arbor, is that our most promising growth firms aren't growing up to create 1,000 job firms, or more, like what happens in Silicon Valley. Hopefully, recent innovations such as Crowdfunding and SEC rule changes mandated in the JOBS Act will help change this negative dynamic and allow our area to fully reap the benefit of being the 5th highest VC activity cluster in the U.S.

A similar dynamic as described above for start-up and entrepreneurial growth companies also exists for start-up de novo banks. The impact on banks is that many de novos are sold quickly once they achieve substantial profitability or reach the seven year anniversary of their foundation. However this does lead to my next recommendation:

9) Examine the SEC's rules to find out why and how regional brokerage firms died out. Repeal the rules that caused this and foster their renaissance.

Why are these regional investment banking and broker firms desirable merger or acquisition candidates? Each regulation has costs that are relatively fixed. For example, if a regulation costs $100,000 a year for a broker to comply and that broker has 1,000,000 transactions, the cost comes to $0.10 per transaction. If a broker has 1,000 transactions, the cost is $100 per transaction. The larger broker can buy the business of the smaller broker, take out the second set of regulatory costs and substantially increase the profit per transaction of the combined brokerage firm. To be able to succeed in such an environment brokers must seek ever larger volumes of business and achieve economies of scale.

Under this scenario, any regulation is good for the business model of large or acquisition-focused brokers. The current regulatory policy and philosophy drives the growth of ever-larger, harder-to-manage and harder-to-regulate megabrokers, while regional brokers have been left to be picked up by acquirers. Unless those policies change, that trend will persist for President Trump's entire term in office.

Access to growth capital for entrepreneurs and existing and de novo banks from a diverse array of sources at the grassroots level is a strong positive social good and key to the success of the American economy. Centralizing capital access among a few powerful megabrokers is not just risky. It's bad for our economy and slows economic growth rates. It also threatens our democracy over the long term, since money can translate into power and trillion-dollar pools of money can easily warp the political process.

However if we want to foster access to growth capital for entrepreneurs and more public companies and also for more banks in the U.S., the SEC and FDIC need to change many of their policies and radically rethink their regulatory approach to increase economic growth, innovation and high quality jobs. Many of the problems that need to be solved are long standing (for nearly three decades now) and in my opinion, impossible for the private sector to fix on their own within the current regulatory framework. This regulatory framework must change or the numbers of banks and publicly traded firms will continue their relentless decline.

Isn't this goal of fostering better access to growth capital for entrepreneurs and more public companies and also for more banks in the U.S. a laudable goal that the SEC and FDIC should back? With a new FDIC chair, you have the ability to change the SEC's long standing policies and obtain for our country and its citizens the many benefits I've outlined above.

If you have any questions about the material presented in this comment letter, I am available to assist you in any way as follows:

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Sincerely,

Stephen Lange Ranzini
President & CEO
University Bank*[+] & University Bancorp, Inc.
Ann Arbor, MI USA

* University Bank is a Member FDIC and an Equal Housing Lender. University Bank is a wholly-owned subsidiary of University Bancorp, which is listed on the OTCQB stock market under symbol UNIB. We are proud to be noted by American Banker newspaper as the:

- #3 top performing publicly traded bank in the U.S. in 2017 based on Average ROE;
- #1 top performing publicly traded bank in the U.S. in 2016 & 2015, based on Average ROE;
- #2 top performing publicly traded bank in the U.S. based over the period 2014 to 2012, based on Average ROE.

University Bank's five year average Return on Equity is 19.1% and our Return on Equity in 2017 was 28.3%. University Bank's ten year annual average revenue growth was 32.5%.

[+]The American Bankers Association, through its Corporation for American Banking subsidiary, has endorsed University Bank's subsidiary, Midwest Loan Services Inc., to provide residential mortgage subservicing services to member banks and their borrowers nationwide. Midwest is known for friendly, responsive service and industry-leading technology that help lenders retain customers, reduce costs and ensure regulatory and operational compliance. Midwest's mortgage customers have 14x fewer complaints than the industry average according to the Consumer Financial Protection Bureau's complaint database.

American Banker

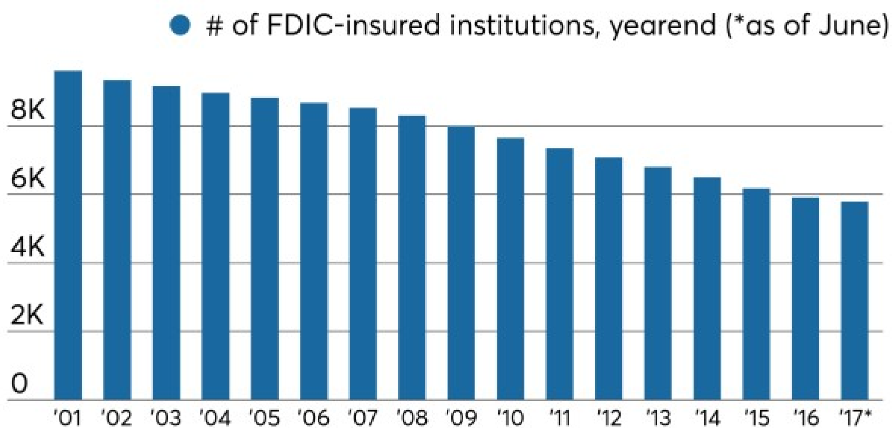
Don’t let community banking go from endangered to extinct

By Stephen Lange Ranzini
Published October 17 2017, 12:00pm EDT

When I entered community banking 29 years ago, bank regulation was focused on two things: The accuracy of financial reports in the bank’s call report, and the bank’s ability to detect and guard against insiders stealing money from the institution.

Back in 1988, the banking industry was still expanding. The number of banks and savings and loans, as well as that for credit unions, was each around 20,000 — and growing every year. The call reports in July 1988 were about 10 pages long versus the over 100 pages our community bank must file today. Some community banks now get to use a “short” form, which runs 80 pages.

The focus of bank regulation today is completely different. Its goal is to ensure that banks don't fail. To achieve this objective, banks must establish committees and follow best practices and complete a lot of documentation of their every move. I met with a customer the other day. It was only the fourth such meeting I have had within the past 12 months. Bank executives have become desk-bound, engaged in constant box-checking and “administrivia.” As expected, this new reality has raised regulatory costs.



Another key factor driving regulatory costs higher is a philosophy that detailed legal disclosures are beneficial to consumers — as best exemplified by mortgage disclosures that now stack six to nine inches high — yet these documents are expensive to create and in the real world consumers don’t actually read them. Yet, to comply and produce all these complicated disclosures, institutions must establish and maintain very expensive systems, much of which have fixed costs and only some are variable in cost.

Because of these rising regulatory and compliance disclosure costs, the median return on equity for FDIC-insured banks in the U.S. has fallen to 9%; there are many banks under $100 million in assets with an ROE below 4%. Since the financial markets require a 9% ROE for investment in bank equity, half the banks in the U.S. are now worth more dead than alive, making them ripe for merger. On average, both one credit union and one bank are sold each business day. The peak of roughly 20,000 banks has fallen to below 5,800.

Why are these low-profit banks and credit unions desirable merger or acquisition candidates? Each regulation has costs that are relatively fixed. For example, if a regulation costs $100,000 a year for a bank to comply and that bank has 1,000,000 transactions, the cost comes to $0.10 per transaction. If a bank has 1,000 transactions, the cost is $100 per transaction. The larger bank can buy the business of the smaller bank, take out the second set of regulatory costs and substantially increase the profit per transaction of the combined bank. To be able to succeed in such an environment banks must seek ever larger volumes of business and achieve economies of scale.

Under this scenario, any regulation is good for the business model of large or acquisition-focused banks and credit unions. To be clear, the number of institutions in the industry was on the decline before the passage of the Dodd-Frank Act in 2010, but that trend continued following implementation of the regulatory reform law. The law supposedly targeted the biggest financial firms, which had brought the economy to its knees with their risky activities, but just look at the response by Goldman Sachs CEO Lloyd Blankfein when he was questioned about the effect the then-still-pending legislation: “We will be among the biggest beneficiaries of reform.”

The current regulatory policy and philosophy drives the growth of ever-larger, harder-to-manage and harder-to-regulate megabanks, while community banks have been left to be picked up by acquirers. Unless those policies change, that trend will persist for President Trump’s entire term in office. Assuming President Trump wins reelection, by the time he would leave office in 2025, there would be only 2,000 banks and 2,000 credit unions left. By then it would be too late to rescue the community banking industry in the U.S.

A policy designed to ensure that banks don’t fail which actually just helps along the failure of 75% of banks and credit unions, is obviously not successful and therefore must be changed.

While it is a laudatory goal to want banks to be so well-run and able to control risks that none fail, in the real world this is a clear policy failure. The system that encouraged the growth of the industry for decades also fostered growth in the number of banks and credit unions. Access to credit from a diverse array of sources at the grassroots level is a strong positive social good and key to the success of the American economy.

Centralizing credit among a few powerful megabanks is not just risky. It’s bad for our economy and slows economic growth rates. It also threatens our democracy over the long term, since money can translate into power and trillion-dollar pools of money can easily warp the political process. While banks and credit unions routinely failed under the old system, more new ones always sprung up and took their place. This cycle of creative destruction was healthy for a dynamic economy.

For large systemically important institutions, preventing failure perhaps makes more sense, and the full scale of current regulation and best practices for the biggest companies is appropriate. However

if we want to foster a community banking and community credit union industry in the U.S., we need to radically rethink our regulatory approach.

Stephen Lange Ranzini the CEO & president of University Bancorp in Ann Arbor, Mich.
www.americanbanker.com/opinion/dont-let-community-banking-go-from-endangered-to-extinct