ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA

Testimony of
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On behalf of the
Independent Community Bankers of America

Before the

Congress of the United States
House of Representatives
Committee on Financial Services

Hearing on

"Promoting Bank Liquidity and Lending Through Deposit Insurance,
Hope for Homeowners, and other Enhancements"

February 3, 2009
Washington, DC

Chairman Frank, Ranking Member Bachus, Members of the Committee, my name is Michael Menzies, and I am the President and CEO of Easton Bank and Trust Company, Easton, MD, and the Chairman-Elect of the Independent Community Bankers of America[1]. Easton Bank is a state-chartered community bank with $150 million in assets. I am pleased to represent community bankers and ICBA's 5,000 members at this important hearing on "Promoting Bank Liquidity and Lending Through Deposit Insurance, Hope for Homeowners, and other Enhancements" and H.R. 703.

Introduction & Summary

Today's hearing is focused on improving bank liquidity, promote lending and address the foreclosure crisis through improvements in deposit insurance, the Hope for Homeowners Program and other enhancements. We will focus our comments on the Chairman's bill, H.R. 703, which address many of these issues. My testimony addresses the following issues:

- Deposit insurance issues related to the current economic crisis
- Community bank access to the TARP's Capital Purchase Program
- Foreclosure mitigation and improvements to FHA programs

We believe each of these issues will have a direct impact on the prospects for a strong recovery. We applaud the Chairman for addressing many of these issues by introducing H.R. 703. We understand that the Committee will mark up some of the provisions in H.R. 703 in separate bills tomorrow, and ICBA urges swift passage of those provisions.

ICBA applauds the Chairman for including a provision to give the banking industry more time to recapitalize the FDIC Deposit Insurance Fund – an idea the ICBA has strongly advocated. The bill makes permanent the increase in deposit insurance coverage from $100,000 to $250,000. And, as the ICBA recently advocated in a comment letter to the FDIC, the bill makes clear bank holding

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[1] *The Independent Community Bankers of America represents nearly 5,000 community banks of all sizes and charter types throughout the United States and is dedicated exclusively to representing the interests of the community banking industry and the communities and customers we serve. ICBA aggregates the power of its members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.*

With nearly 5,000 members, representing more than 18,000 locations nationwide and employing over 268,000 Americans, ICBA members hold more than $1 trillion in assets, $800 billion in deposits, and more than $700 billion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

companies with significant non-bank subsidiaries will pay their fair share of any deficit in the FDIC Temporary Liquidity Guarantee Program (TLGP).

As part of the FDIC's efforts to promote stability and liquidity in banks, the agency established an optional guarantee of all amounts above $250,000 in non-interest and very-low interest bearing transaction accounts in FDIC-insured institutions under its TLGP. The program has been a useful tool for community banks that face stiff competition for deposits, the main source of community bank liquidity. ICBA urges the Committee to include a two-year extension of the transaction account guarantee program in the deposit insurance provisions.

ICBA is pleased that H.R. 703 addresses community bank access to the CPP by requiring the Secretary of the Treasury to promptly allow access to the CPP by small financial institutions, and to do so on terms comparable to those applicable to the largest banks that have already received capital infusions under the TARP.

Deposit Insurance Issues

The Emergency Economic Stabilization Act temporarily increased deposit insurance coverage from $100,000 to $250,000. The additional coverage has helped community banks be a part of solution to the credit crisis caused in large part by the activities of larger financial institutions. We are pleased that the Chairman's bill would make this increase permanent.

The FDIC has proposed increases in deposit insurance assessments that double existing premium rates because the FDIC's Deposit Insurance Fund reserves are significantly below required levels due to recent bank failures. Community banks are prepared to do their part to maintain a strong and well-capitalized deposit insurance system. However, the nation is currently faced with the most severe economic crisis it has faced in many generations. Holding down deposit insurance premiums at this time would be consistent with the government's efforts to restore stability to the markets and the financial sector. We commend the Chairman's approach to this issue by increasing the period for recapitalization of the DIF from five years to eight years. A longer period for recapitalization would allow the FDIC to reduce proposed assessment rates. Lower rates would keep additional funds in local communities for lending to small businesses and consumers at this critical time.

H.R. 703 addresses another issue that the ICBA has raised with respect to the FDIC's Temporary Liquidity Guarantee Program (TLGP). The FDIC used its systemic risk authority to establish the TLGP. The net costs of any activity under the systemic risk authority must eventually be borne by all FDIC-insured banks and thrifts through an assessment based on the institutions' assets minus equity. The statute does not expressly authorize the FDIC to assess non-bank and non-thrift affiliates, including holding companies. The Debt Guarantee Program has been extended to holding companies because much of the bank debt is issued at the holding company level. However, should a special assessment be needed to make up for any deficit in the TLGP, the FDIC cannot levy an assessment against the non-bank assets of a holding company. We applaud the Chairman and the FDIC for their support of a provision in the bill that would allow the FDIC to ensure holding companies with significant non-bank assets pay their fair share of any deficit in the TLGP.

ICBA also supports a provision in the bill increasing the FDIC's standby line of credit with Treasury. Although the FDIC has never used the line of credit, an increase in the amount will insure that the FDIC will have adequate resources to meet future challenges in the banking sector.

Extension of the FDIC's Transaction Account Guarantee Program

As part of the FDIC's efforts to promote stability and liquidity in banks, the agency established an optional guarantee of all amounts above $250,000 in transaction accounts in FDIC-insured institutions under its TLGP. More than 6,000 banks, including thousands of community banks have chosen to participate in this program.

Community banks in many markets face stiff competition for deposits, the primary source of liquidity for community banks. The program has been a useful tool for community banks competing with larger banks, including the too-big-too-fail banks, for commercial deposits.

Participation in the program also frees up capital and resources used by community banks to purchase Treasuries and other securities for repurchase agreements that secure commercial and public deposits. Community banks can use the freed up resources to promote lending in their communities.

Taxpayers have no liability for the program, and the program does not reduce the FDIC reserve ratio. Participants are assessed a 10 basis points fee for the guarantee, and any deficit in the program would be made up by a special industry assessment under the FDI Act's systemic risk provision.

Unfortunately, the transaction action account guarantee program will expire at the end of the year. We strongly urge Congress to preserve this important support of community bank liquidity during the current economic crisis. We propose that the Committee include a two-year extension of the program in H.R. 703.

Limited Availability of Community Banks to TARP/CPP

It is vital to note that community banks had no role in creating the current problems we face. They did not engage in irresponsible subprime lending and have remained strongly capitalized. There are more than 8,000 community banks nationwide, and they are well positioned to extend lending to their communities using capital from the Capital Purchase Program. Including interested community banks in the Capital Purchase Program will stimulate additional lending in local communities throughout the country.

ICBA has had significant concerns with the pace of implementation of the Troubled Asset Relief Program's CPP. We are pleased that Treasury released a term sheet for Subchapter S banks last month. ICBA is also pleased to see Treasury's latest round of TARP CPP capital purchase transactions include a good number of community banks.

However, mutual savings banks and thrifts still do not have a term sheet available. These institutions play critical roles in their communities, particularly in small towns and in the New England states where they are the predominant local and small business lenders.

H.R. 703 directly addresses this concern. It explicitly directs the Treasury "to promptly make funds available for smaller community institutions." It is entirely feasible to craft workable terms for mutual banks so they can access CPP funds under similar economic terms as the big publicly traded banks. We urge Treasury to act quickly to include all mutual institutions in the CPP.

ICBA members are growing increasingly concerned with the lack of information on pending CPP applications. While some community banks have begun to receive funds under the CPP, many other banks are having difficulty determining the status of their applications, which are reviewed by their primary federal regulators and then sent to Treasury. ICBA is pleased that Treasury has announced plans to make the CPP process more transparent. We urge Treasury and the regulators to make available application status information to individual banks.

We are pleased that H.R. 703 would ensure that most new conditions in the CPP would not apply to community banks with pending applications and institutions, such as Subchapter S and mutual banks, which, through no fault of their own, have been unable to apply for the CPP. H.R. 703 recognizes that applying such conditions retroactively would place an unfair burden on community banks.

Allowing all community banks to participate in the TARP CPP will help boost lending to families and small businesses. For every dollar in new capital a community bank can raise it will help facilitate an additional seven to ten dollars of lending in their communities. The cost of this CPP capital is not inexpensive for community banks, at some 7.5% tax effective rate in the first five years with additional warrant-related costs on top. So community banks participating in the program will put the capital to good use by doing what they do best – lend on Main Street.

Foreclosure Mitigation Steps

Community banks are truly invested in long-term relationships with their customers and their communities. When community banks service mortgages, often mortgages they have kept on their books, they have a strong interest in maintaining those relationships, and not just guarding the interests of investors. They know their community will be hurt too by empty homes. Community banks' involvement in finding solutions for consumers extends beyond their own customers as community banks have offered refinancing to troubled borrowers with loans from other institutions as well.

Since community banks, by and large, did not engage in the subprime lending practices at the heart of the current crisis, they are not currently experiencing unusual levels of mortgage defaults. And, ICBA members are still making mortgage loans. Community bank mortgage originations remained steady throughout 2008. ICBA Mortgage Corporation helped 1,000 community banks write approximately 40,000 mortgages totaling $6.2 billion. Assuming ICBA Mortgage Corporation's share of the community bank market is five percent, we estimate community banks have originated approximately 800,000 mortgage loans for an aggregate principal amount of approximately $125 billion in 2008.

We agree minimizing foreclosures is an important part of the effort to stabilize the U.S. economy. Foreclosure is often a very lengthy, costly and destructive process that puts downward pressure on the price of nearby homes and has a devastating impact on families and communities.

Community banks that service their own mortgages monitor payment activity for changes that might signal a borrower could have difficulty paying the mortgage. If default occurs, they contact the borrower quickly to avoid potential problems. Community banks do not rush to foreclosure.

Community banks will continue to work with individual borrowers to find the best solution to keep borrowers in their homes, including through a loan modification under the Hope for Homeowners Program or under any new government programs that would support mortgage modification. ICBA supports the revisions to the Hope for Homeowners Program included in HR 703 and makes the following suggestions to improve the prospects of any mortgage modification program:

1) Loan-to-Value Determination —-Any program depends on a credible valuation of the property. The federal banking agencies currently have interagency appraisal guidelines and have proposed additional guidance for federally related transactions. The agencies in charge of loan modification support programs should ensure that their valuation procedures are the same or consistent with the appraisal guidelines and once the value of a property is properly determined, there should be an agreement by the banking regulators that they won't second guess the value of the collateral in a subsequent bank examination, at least for a reasonable period of time.

2) Regulatory and Accounting Forbearance – When a lender modifies a mortgage, it must recognize a loss on the original loan. There should be a relaxation of accounting standards for the recognition of the losses, and the banking regulators should relax regulatory capital standards vis-à-vis these losses.

Unleash FHA Potential

ICBA supports increasing capacity for the Federal Housing Administration to serve homebuyers, homeowners and lenders. As credit for home purchases and refinancing has seriously contracted, FHA insurance has taken on an expanded role. FHA is vital to the provision of affordable housing and the recovery of the housing market. Increasing capacity, by hiring more personnel at FHA and Ginnie Mae will allow the agencies to carry out their mission and assist homebuyers, lenders and communities. Due to FHA's resurgence in the marketplace, FHA lender approval can take as much as 180 days. Additional resources for FHA would help speed up the approval process.

In reports on FHA modernization, the GAO has stated that subpar technology is impeding the FHA's effectiveness. FHA told GAO its systems are poorly integrated, expensive to maintain, and do not fully support the agency's operations and business requirements. We urge Congress to address these critical concerns. FHA has an important role to play in the market in saving homes and assisting the underserved.

Conclusion

ICBA appreciates this opportunity to testify on these critical issues. We look forward to working with this Committee and Congress on these and other steps that will help us emerge from this current crisis and improve our financial system for the long run.