

The Meeting of the Advisory Committee on Community Banking

of the

Federal Deposit Insurance Corporation

Held in the Board Room

Federal Deposit Insurance Corporation Building

Washington, D.C.

Open to Public Observation

June 5, 2012 - 8:32 A.M.

The meeting of the Federal Deposit Insurance Corporation (“FDIC”) Advisory Committee on Community Banking (“Committee”) was called to order by Martin J. Gruenberg, Acting Chairman, FDIC Board of Directors.

The members of the Committee present at the meeting were: Robert F. Baronner, Jr., President and Chief Executive Officer (“CEO”), Bank of Charles Town, Charles Town, West Virginia; R. Daniel Blanton, President and CEO, Southeastern Bank Financial Corporation and Georgia Bank and Trust Company of Augusta, Augusta, Georgia; Charles G. Brown, III, Chairman and CEO, Insignia Bank, Sarasota, Florida; Deborah A. Cole, President and CEO, Citizens Savings Bank and Trust Company, Nashville, Tennessee; Carolyn “Betsy” Flynn, President and CEO, Community Financial Services Bank, Benton, Kentucky; Walter E. Grady, President and CEO, Seaway Bank and Trust Company, Chicago, Illinois; James H. Gray, Chairman, Beach Business Bank, Manhattan Beach, California; Jack E. Hopkins, President and CEO, CorTrust Bank, National Association, Sioux Falls, South Dakota; Ann Marie Mehlum, President and CEO, Summit Bank, Eugene, Oregon; Joseph G. Pierce, President and CEO, Farmers State Bank, Lagrange, Indiana; Rebecca Romero Rainey, Chairman and CEO, Centinel Bank, Taos, New Mexico; Dorothy A. Savarese, President and CEO, Cape Code Five Cents Savings Bank, Orleans, Massachusetts; Alan Thian, President and CEO, Royal Business Bank, Los Angeles, California; and Ignacio Urrabazo, Jr., President, Commerce Bank, Laredo, Texas.

Matthew Williams, Chairman and President, Gothenburg State Bank and Trust Company, Gothenburg, Nebraska was absent from the meeting.

Members of the FDIC Board of Directors present at the meeting were: Martin J. Gruenberg, Acting Chairman, Thomas M. Hoenig and Jeremiah O. Norton.

FDIC staff who attended the meeting included: Ruth R. Amberg, Steven O. App, Stephen Beard, Richard A. Brown, William F. Cole, Kymberly K. Copa, Carolyn D. Curran, Christine M. Davis, Patricia B. Devoti, Dianne E. Dixon, Bret D. Edwards, Diane Ellis, Robert

E. Feldman, George French, Marshall E. Gentry, Alice C. Goodman, Shannon N. Greco, Craig R. Jarvill, Sally Kearney, Ellen W. Lazar, Jill A. Lennox, Alan W. Levy, Marianne Lloyd, Christopher Lucas, Roberta K. McNerney, Robert W. Mooney, Charles Morris, Arthur J. Murton, Christopher J. Newbury, Thomas E. Nixon, Richard Osterman, Mark Pearce, Sylvia H. Plunkett, Claude A. Rollin, Barbara A. Ryan, Maureen E. Sweeney, Sandra L. Thompson, James C. Watkins, Cottrell L. Webster, John D. Weier, Mindy West and Katherine G. Wyatt.

William A. Rowe, III, Deputy to the Director (Comptroller of the Currency) was also present at the meeting.

Acting Chairman Gruenberg welcomed the Committee members and gave an overview of the day's agenda, which included: an update on the FDIC's Community Bank Initiatives; a discussion of capital and other supervisory issues; community bank compliance issues; the FDIC's plan to review regulations for burden reduction; the impact of the use of shared loss agreements in resolving failed banks; and a roundtable discussion. He also noted the luncheon speaker would be Mary Miller, Undersecretary of the Treasury for Domestic Finance.

Acting Chairman Gruenberg introduced Barbara Ryan, Chief of Staff, who moderated the day's proceedings and introduced the first panel, "Update on the FDIC's Community Bank Initiatives," and its panelists: John Weier, Advisor to the Acting Chairman, Sylvia Plunkett, Senior Deputy Director, Division of Depositor and Consumer Protection ("DCP"), James Watkins, Deputy Director, Division of Risk Management Supervision ("RMS") and Diane Ellis, Deputy Director, Division of Insurance and Research ("DIR").

Ms. Ellis reported that the FDIC continued work on the 14 community banking issues she outlined at the previous Committee meeting. She said that researchers had gathered and organized the data that is readily available and are currently analyzing it; staff would begin drafting working papers on different subjects during the summer. Ms. Ellis noted that, while the research continues to compare community banks to non-community banks, researchers were also performing life cycle analyses of the structure and performance of different groups of community banks to gain a more in-depth understanding of what characteristics and business models had been successful (and unsuccessful) during the past 25 years and the last two banking crises. For example, she said, they would explore how community banks that have been in existence for the past 25 years compare with the 11 percent that failed, and the 50 percent that merged or consolidated in the period; and further, among the merged or consolidated banks, how many did so because they were struggling or because they were successful.

Mr. Watkins spoke about RMS's and DCP's internal reviews aimed at enhancing their examination processes. In RMS, working groups were reviewing over 3,300 suggestions provided by 700 examiners which had identified five fundamental areas for improvement. The first area related to pre-examination planning. Occasionally, he said, information was requested from banks which was not fully utilized and the FDIC would attempt to streamline these requests. A second area, Mr. Watkins said, was improving communications throughout the exam process. In some instances, for example, information requested from banks was used in the exam but examiners had not effectively communicated why it was needed. Mr. Watkins said a third area for which examiners had provided recommendations was the better use of technology

that the FDIC has available. A fourth area, Mr. Watkins described, was the better use of outreach events and technical assistance by the FDIC to more fully explain complicated regulations or the calculations of certain ratios the FDIC uses. Finally, he said the post-examination process could be improved to ensure banks understand and are addressing the issues raised during examinations.

Ms. Plunkett said DCP followed a process similar to RMS to get information from examiners and it was comparing that input with feedback the FDIC was receiving at the regional community banking roundtables; she noted that the issues identified by the two groups were quite consistent. Ms. Plunkett then addressed for DCP, the same five areas that Mr. Watkins had discussed for RMS. In the pre-examination process, she said DCP was also looking to ensure that examiners had adequate preparation time before going on site so that the entry discussion was meaningful and moved the examination forward faster. Regarding communications about compliance exams, especially where consultation with Washington and the FDIC Legal Division was required, she said it was important that examiners keep banks informed about where they are in the process. She said such ongoing communications occurred in some locations, but it was important to make this a uniform practice in all exams. Regarding the use of technology, Ms. Plunkett said some information currently requested from banks in the pre-exam planning process could be obtained through automated systems, thus reducing the impact on banks.

Ms. Plunkett said the fourth area, outreach and technical assistance, was particularly important where regulations had changed and banks needed to know what was expected of them. She said the FDIC offers a series of bankers' calls on new or "hot" topics (such as the one occurring that afternoon on third-party compliance management oversight). Ms. Plunkett also said the FDIC was working on technical assistance items to be shared with banks and it aimed to encourage continuous back-and-forth communications about regulatory expectations, so questions would not be raised only on a three-year exam cycle. Regarding the post-examination process, Ms. Plunkett recognized that many bankers felt it took too long to receive their examination results. She said prompt reports were also in the interest of consumers and the FDIC because they would allow quicker corrective actions and that DCP was looking for ways to improve timeliness. Finally, Ms. Plunkett said the FDIC was developing a regulatory calendar for its website where bankers could see what regulation changes were in the pipeline and their effective dates.

Mr. Weier spoke about the FDIC Community Banking Initiative roundtables which had occurred in Dallas, Atlanta and Chicago (with three remaining), noting they generally involved FDIC leadership and 50 to 60 bankers, trade representatives and state supervisors. Each meeting consisted of two panel discussions with additional time for questions and answers. One panel, which focuses on financial and operational challenges, has raised issues such as soft loan demand, the high competition for making loans, interest rate risk, implementing new technologies in a safe and secure way, and, the possible extension of the Transaction Account Guarantee ("TAG") program. Mr. Weier described the second panel discussion in the roundtable meetings as focusing on regulatory interaction, which includes topics such as bankers' concerns about the increasing complexity and cost of regulations, the need for technical assistance to comply with them, and the desire for examinations to take into account the bank's size and complexity, and a preference for using experienced exam teams. Mr. Weier said bankers want

assurance that the information they provide to examiners is used and that the bankers understand how it is used. In addition, he said the roundtables provide bankers with feedback forms they can use to raise additional issues.

The Committee provided the FDIC leadership with feedback on a variety of subjects. The subjects included: the FDIC Community Banking Initiative; the examination process, including pre-examination information requests; FDIC communications in general and in specific situations; the development of banking best practices, their relationship to examination standards and banker responses to examination recommendations; the cost of regulatory compliance and how to measure it; weak loan demand and competition in banking; and the continuation of the TAG program. For ease of understanding, the Committee feedback is summarized by subject.

Member Brown said the Community Banking Initiative roundtable meetings reassured bankers who attended them that the FDIC was “hearing” the problems bankers were experiencing on various issues, including the inefficient use of pre-examination information requests. Member Urrabazo said that the Committee and the roundtables had generated many good suggestions, but added it was important that tangible outcomes resulted. Specifically, he suggested the FDIC publish white papers or other analyses to summarize its findings and provide insight into the future of community banking, and for these to include action items and strategic timetables to implement the particular recommendations. Member Urrabazo further said the analyses and action items should be disseminated to the FDIC’s regional offices to ensure implementation.

Member Savarese reported she had received positive feedback about the Community Banking Conference and roundtables. She said the attendance by the Acting Chairman and FDIC leadership to hear bankers’ concerns was important, but agreed that bankers often feel that there is a disconnect between what headquarters says and its translation in the field. Member Savarese said there was enthusiasm that the FDIC was taking the effort and risk to focus on the situation of community banks during this period of significant change in the economy, which could be viewed either as a crisis or a tremendous opportunity. Member Savarese observed the Community Banking Initiative needed to have short, intermediate and long-term goals as well as an overarching objective. She suggested various methods to help maintain the project’s momentum, including: allowing the project plan to evolve, maintaining project transparency, encouraging feedback from the regions, and showing that hearing and learning are occurring throughout the process. She agreed that action plans were key. Member Savarese complimented the FDIC for engaging as a partner with community banks and for providing a forum where ideas could be worked on collaboratively and experimentation encouraged. Mr. Weier later agreed with members about the importance of action plans and said that he would be sure to share them with the Committee.

Member Brown spoke about the information banks provide examiners before an examination. He said the concept of providing information that could be reviewed before examiners were on site was good, but it was clear examiners were arriving without having thoroughly reviewed what had been sent. Member Brown recommended examiners be given more time to prepare before an exam or reduce the amount of information the bank is required to

provide. Member Blanton said his bank had experienced similar issues and, in response, created a short write-up about the bank's current status and its progress since the last examination. Member Pierce later said on-site examiners had requested documents or information the bank had already provided, thus requiring bank employees to duplicate work they had already done.

Member Brown said bankers had told him that FDIC communications were generally improved and, although there was still some disconnect in communications from Washington and the regions, those differences were dramatically improved. Other members, however, reported instances of less successful communications. Member Pierce said he appreciated DCP's offer of technical assistance in meeting compliance obligations because there had been occasions when the regional office had communicated that their job was to protect the consumer, not to assist banks in complying with the law. He noted such comments were inconsistent with the relationship his bank had enjoyed with FDIC examiners over time. Member Urrabazo related an experience of compliance examiners not conducting an exit meeting that would have revealed the examiners had reviewed outdated bank materials. When the examination report issued six weeks later and the examiners' mistakes were pointed out to them, he said he was surprised they declined to revise their findings. Mr. Weier said he would follow up on the issue after the meeting. Member Thian said, although examiners were generally experienced and knowledgeable, he occasionally found some were too subjective and unresponsive to the bank's explanation. He inquired about how the FDIC received and evaluated feedback about their examiners. Mr. Watkins said FDIC field office supervisors and other management officials welcome discussions with bankers about examiner performance and experiences during an examination. He also noted FDIC examiners must meet rigorous training standards and are evaluated on a full balance of their quantitative and qualitative skills as well as their ability to communicate effectively.

Member Savarese spoke about the development of "best practices" and their relationship to examination standards. She said the FDIC, as insurer and regulator, can helpfully alert banks to emerging trends it identifies and provide appropriate guidance. She said, however, FDIC best practices guidance is sometimes developed without enough transparency or industry input and is issued in a way that bank directors see it as a requirement rather than as a subject calling for discussion. Member Savarese also indicated it sometimes appears examinations are measured against a best practices standard rather than regulation or guidance. She said some fields, such as information technology, move so quickly it is important that banks are part of the development of best practices before guidance on a matter is issued. Member Gray observed examinations also include examiner suggestions, which his bank views as a positive learning opportunity. He noted, however, not every suggestion is appropriate for his institution and his bank writes a letter to the region covering each of the suggestions, including an explanation of why the bank was not implementing any of the suggestions. Member Gray said these letters prompt useful exchanges with the region. Member Urrabazo said his bank received best practices recommendations from examiners at its last examination and ultimately the bank and examiners "agreed to disagree." He added, however, his bank was afraid to disagree with its examiners and thought long and hard before writing the region to explain why its recommendation would not work for his bank. Member Urrabazo said banks should not be afraid of articulating their disagreement and examiners occasionally try to force best practices and guidance where it does not fit.

At various times during the first panel, the Committee discussed the cost of regulatory compliance. Member Urrabazo suggested the FDIC should make an effort to understand the costs of compliance for community banks, although he recognized it would be a difficult analysis. He said he was concerned about the issue because his bank's cost for compliance kept escalating while its revenues were going down, capital requirements were going up and investors were not attracted to his bank's returns. Member Urrabazo indicated FDIC regional staff was focused on compliance, which his bank was maintaining, but failed to appreciate the increasing costs it imposed. Ms. Ellis agreed the issue was critically important and is on the FDIC's research agenda but noted it was a challenging issue, in part, because banks account for the costs in different ways and there is not much data available to estimate the costs associated with regulatory burden. Mr. Watkins said most banks do not have cost accounting systems that would fully describe or easily segregate the cost of regulatory compliance. Member Urrabazo suggested changing the Call Report to oblige banks to understand their regulatory compliance costs. Member Savarese suggested the FDIC could drill deeply into some specific regulatory compliance costs and then extrapolate those detailed numbers for making public policy decisions and promulgating best practices.

Member Grady observed another cost of regulatory compliance can be the loss of customers; he related an example of a customer feeling harassed by his bank's efforts to comply with the Bank Secrecy Act and anti-money laundering regulations. He also noted, although his bank did not have a cost accounting system that could provide precise compliance cost numbers, he could report how many people worked on compliance matters. Member Pierce observed that it is comparatively easy to measure, for example, how much taxes cost on a particular piece of Other Real Estate Owned ("OREO"), but it was harder to track the cost of employee time spent on compliance because community bank employees perform such a variety of functions. He also said his bank had spent hundreds of hours preparing for its last compliance examination. Regarding helping banks efficiently achieve regulatory compliance, Member Blanton recommended that regulators, when drafting regulations, include examples of how a bank could comply with them. Member Blanton also noted that banks in his area were seeing weak loan demand and noted that regional banks were trying to take customers by offering a ten-year fixed rate loan product with which community banks found it hard to compete. Member Pierce later agreed with these observations and added that regional and large banks first competed on interest rates and then lowered underwriting standards, which he was now seeing occur.

The Committee also discussed the possible extension of the TAG program at various times. Member Blanton said he now felt the program should be extended for another year so consumers would have no reason to question if their deposits were insured. He said an extension would benefit smaller and weaker banks. Member Brown said it would be helpful if the FDIC shared information about the cost to banks of extending the TAG program and he and Ms. Ellis discussed measuring the costs. Ms. Ellis said FDIC staff has determined the estimated losses associated with the TAG program, which insures non-interest bearing transaction accounts on an unlimited basis (compared to the limited insurance for other accounts), accounted for about three percent of the estimated total cost of bank failures. She noted this estimate is based upon the failure of smaller institutions, and the loss rate could differ significantly in the event of a failure of a larger institution since, on average, these deposits constitute a greater share of insured

deposits in larger institutions. Ms. Ellis also noted the FDIC needed to meet the statutory goal of a 1.35 percent reserve ratio for the Deposit Insurance Fund (“DIF”) by September 30, 2020. Current projections indicated the existing assessment rate schedule would achieve that goal, with or without a short-term extension of the TAG program. She added, however, that an extension might delay, by a quarter or two, when the FDIC could lower the insurance assessment schedule. Member Flynn said her bank was experiencing such strong loan demand from small businesses that it needed deposits to fund those loans but had to turn away substantial municipal deposits because it did not have available securities to pledge for those deposits. She said it was extremely important the TAG program be extended, for her bank and for the economic recovery generally. Members Mehlum and Cole also supported a TAG extension because it would remove an element of instability and help the community banking industry overall, especially smaller banks.

Director Norton inquired how regulators should view the TAG program’s guarantee of bank liabilities for small banks, where the market has few opportunities to price the banks’ risk because their equity and debt is not traded. Member Mehlum responded that the question was correct but it could not be quantified; she said depositors perceive a risk in small institutions which they do not in the largest banks. Members Flynn and Blanton agreed there was a difference in the perceived security of deposits in small and very large banks. In response to a question from Director Norton about how many members’ banks had more loans than deposits, Member Hopkins responded that his bank’s loan-to-deposit ratio was about 110 percent before the recession, but was lower now. He added, during the crisis, big banks encouraged depositors to move their deposits to them because they were too big to fail, and depositors did so. Member Flynn agreed and added that big banks were not allowed to fail; she said, although the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) was supposed to end that perception, she was skeptical it would occur.

Ms. Ryan then invited George French, Deputy Director, RMS, to join Mr. Watkins in moderating the next panel, “Capital and Other Supervisory Issues.” Mr. French began by noting the FDIC Board of Directors would soon consider four regulatory capital rules. Two of them, a market risk final rule and an advanced approaches proposed rule, would generally not affect community banks, he said. The third, the Basel III General Approaches Rule (a notice of proposed rulemaking), would affect community banks if the FDIC Board approved the staff recommendation. Mr. French said the proposed rule would implement the Basel III agreement in the U.S.; it would strengthen the definition of regulatory capital and increase the level of minimum capital requirements for the various risk-based capital ratios. He said the FDIC’s analysis indicated most community banks already meet the proposed requirements. The other proposed rule, the Standardized Approaches Rule, Mr. French continued, included a variety of proposed enhancements to the risk weighting of assets. He observed the documents were large and would challenge community banks to identify the parts which were relevant to them but said the FDIC was committed to assisting understanding. Acting Chairman Gruenberg noted both proposed rules had appendices community banks could use as a concise guide to complying with the rules. Member Gray indicated that such an appendix was the type of compliance guidance the Committee had discussed and requested.

Mr. Watkins then compared capital levels maintained by community banks (using \$1 billion or less of assets as the threshold) and non-community banks. He said community banks consistently maintained higher levels of capital, noting, for example, at the end of the first quarter of 2012, they had a leverage capital ratio of nearly 10.25 percent while non-community banks had just over nine percent. Mr. Watkins also said about half of community banks had tried to raise capital in the last three years and many had been successful in doing so; he added that a significant part of the capital increase came from positive performance in retained earnings. He said the capital increase showed considerable support from existing shareholders and management. Mr. Watkins noted, however, that many community bankers indicated they were having difficulty sustaining strong earnings, especially in some areas of the country. In response to a question from Member Mehlum, Mr. Watkins said the capital level difference between community and non-community banks had historically been greater, but some of the large banks had recently raised capital.

Member Brown expressed concern that higher capital requirements would make it difficult for community banks to produce an adequate return on equity ("ROE") which, he said was important to their ability to "survive, thrive and raise capital." He strongly encouraged the FDIC to consider ROE as well as return on assets ("ROA") in its decision making. Member Brown recognized capital was an important aspect of banks surviving in a crisis, but said that the community bank capital ratios Mr. Watkins discussed indicated an unacceptable return for shareholders and, over time, they would move their investments away from community banks. In response to Director Norton's inquiry about what specific type of ROE he was speaking about, Member Brown indicated that it was whatever ROE that draws investors to community banks. Mr. French said, not disputing the point about ROE, it was surprising how many community banks had been able to raise capital during the crisis and that quite a few had been able to raise capital externally or from their holding company. He also agreed with Member Blanton's observation that most of the capital was raised by members of banks' boards of directors or existing shareholders. Member Gray added that the dilutive effect of a capital raise on existing shareholders was a significant concern in community banks and made it difficult to raise capital.

Member Blanton said his bank's shareholders appeared to be different than those described by Member Brown; they came from a banking family that is part of their community and expected a reasonable return, not the maximum return a regional bank might offer. He added he viewed this position -- not having to compete with the best yield an alternative investment might make -- as a community banking strength. Member Brown agreed publicly traded banks may have different perspectives than one that has a small number of shareholders in a single community, but said it was important for the overall industry to understand the relationship to ROE because, ultimately, investors expected a return on their investment.

Director Hoenig asked the Committee what they judged to be the "right" amount of capital, noting the judgment has to be made and there is no formula. He observed, without deposit insurance, capital requirements would probably be dramatically higher, as they were historically, and that deposit insurance serves, in a sense, as a substitute for capital. Director Hoenig noted he had to be concerned about the deposit insurance fund while Member Brown had to be concerned with investors, thus creating different perspectives. He said he understood the issue of ROE, but said risk-adjusted return on equity was really the issue. Member Brown said



ROE is important to both the FDIC and community bankers because it reflects the future of the industry. He said investors see community banks that failed and may conclude community banks are a relatively high-risk, illiquid investment, ultimately resulting in bank boards being hyper-focused on ROE. Member Brown recommended the FDIC monitor ROEs and consider the effect of proposed capital requirements on community banks' ROEs. He said his bank had considered raising capital but, when they considered the dilutive effect of it, chose to "flatline" the bank or to shrink banks in some cases. Member Urrabazo indicated more investors were focused on return and were relatively unconcerned about risk; he added most of his bank's capital growth was from retained earnings. Mr. French agreed that how banks raise capital is an important issue but emphasized, for the most part, the FDIC did not expect the proposed rules would require community banks to raise capital externally.

In response to Director Hoenig's question regarding what are the correct capital requirements, Member Mehlum said the FDIC now had a great deal of data from failed banks and suggested the information be analyzed to determine how much capital they had needed. Member Hopkins observed some failed banks had 25 percent capital levels and a high level of capital could not protect a bank against bad management or bad concentrations.

Mr. Watkins said the new issue of the FDIC's *Supervisory Insights* journal would contain articles that touched on issues raised previously in Committee meetings, including an article on improving communications throughout examinations, and an article clarifying troubled debt restructurings ("TDR") which also provides illustrative examples.

Member Cole asked if the FDIC would consider its written communications about exam results. She noted the FDIC's letters can be more focused on deficiencies and violations than the examination itself and cause confusion for the bank's board. Mr. Watkins said the FDIC was aware of inconsistencies between closeout meetings with examiners and subsequent written reports. He said it was an issue the FDIC had struggled with and guidance had been issued to examiners and discussed in conference calls and other venues. Member Savarese complimented efforts in the FDIC's northeast region to employ an experienced individual to provide coaching for examiners on effective communications.

The Committee stood in recess at 10:16 a.m. and reconvened at 10:32 a.m. that same day.

Ms. Ryan then introduced the moderators for the third panel, "Compliance Issues," Mark Pearce, Director, DCP, Sylvia Plunkett, and Jonathan Miller, Deputy Director, DCP. Mr. Pearce said, in addition to the RMS and DCP examination *process* review Mr. Watkins and Ms. Plunkett had discussed earlier, DCP was also undertaking a parallel review of its compliance examination and supervisory program to ensure it effectively identified, addressed and prevented risks of consumer harm. He explained, in light of significant changes in consumer protection laws in the last five years, DCP was now supervising more detailed and complex consumer regulations than ever before and it was not practicable for the FDIC to merely add these new regulations on top of the existing compliance examination procedures. Thus, Mr. Pearce said, DCP had assembled a working group comprised of field, regional and headquarters staff that, starting from first principles, was considering what is meant by consumer harm – including economic loss and noneconomic losses such as the discouragement of certain sets of applicants. The working group

is cataloguing the risks to consumers addressed in the 40-plus regulations that the FDIC enforces, he said, with the aim of creating a set of recommendations and action items to help focus compliance examinations. The goal is to focus examinations on consumer harm, and the intent and spirit of the laws, not merely technical compliance, he said, while simultaneously taking into consideration differences in bank size, complexity, location, and business model. Mr. Pearce said DCP wanted the process to be open and transparent and was a reason he was discussing it with the Committee today.

Member Mehlum praised the effort, noting community bankers are outraged by blatant consumer harm but are concerned the regulations are impacting banks even if they do not make consumer loans or have issues involving consumer fairness or harm. Members Cole and Urrabazo also supported the project but noted the requirements of some laws themselves can have harmful consumer impacts by raising costs to consumers or causing banks to decline to make loans due to compliance concerns. Member Savarese later said the FDIC has a role in coordinating various regulations that involve several agencies and suggested those cross-jurisdictional regulations should also be examined for their costs and benefits. She also observed that some regulations, such as the Home Mortgage Disclosure Act (“HMDA”), have burdensome collection methods needing interagency review, and regulations have to be reassessed on a continuous basis.

Member Rainey supported reviewing regulations for consumer risks but felt regulator communications and transparency were also important elements. She said, for example, bankers were concerned about fair lending referrals to the Department of Justice (“DOJ”) and, absent feedback from the FDIC about what it is specifically looking at in such cases, banks become paranoid about violations and may stop making some loans to avoid violations. Member Rainey suggested the FDIC could provide banks with feedback on what its examiners are finding and how the FDIC is responding so that banks can ensure their programs are in-line with expectations. Member Brown later agreed that community banks were very concerned about fair lending compliance. He said some banks avoided risk-based pricing of their loans because it was perceived as a safe way to avoid a fair lending violation even though, he said, it did not make economic sense to not use risk-based pricing. Other banks, he said, documented their loans using various matrices of factors (such as loan-to-value, debt-to-income and credit scores) but there was a concern using such matrices increased the probability of a violation being found. Member Brown said many banks use a third approach of making every loan decision on a case-by-case basis, which also had a high risk of being found to be a violation. He observed that bankers’ fears of violating the law made their decision-making inefficient and negatively impacted earnings; he recommended the FDIC provide more guidance on fair lending enforcement.

Member Brown inquired about consultations between the FDIC and the Consumer Financial Protection Bureau (“CFPB”). Mr. Miller said the CFPB consults with the FDIC about rulemakings as required by law, but also informally consults on a variety of topics. Mr. Miller said the FDIC is eager for the CFPB to understand the unique characteristics of small banks as it drafts new consumer regulations. Member Brown said he was happy that the law required the CFPB to have hearings related to their rulemakings and he had recently participated in a CFPB rulemaking consultation. On one hand, he said, he was pleased the CFPB was considering various exceptions and exemptions to rules in development. On the other hand, Member Brown was concerned that the CFPB was considering various pricing and product mandates which he said would cause

consumer harm by interfering with the operation of the market. He was also concerned that the CFPB was considering imposing the same testing and licensing standards on bank mortgage loan originators as on mortgage brokers. Member Brown indicated the subject matter tested for was often unrelated to work that loan originators actually performed, and that CFPB requirements may duplicate those imposed by bank regulators, ultimately causing banks to withdraw from that line of business. Mr. Miller said he would make a point of speaking to the CFPB about the issue; he also said that the CFPB was a data driven organization and encouraged Committee members to share relevant data with them. Mr. Pearce also commented that the CFPB had been receptive to the FDIC's data and its insights about community banks.

Members Hopkins and Urrabazo discussed concerns about fair lending violations based on disparate impact analysis and the lack of clarity about what regulators and the DOJ look at in such decisions. At Mr. Pearce's invitation, Ms. Plunkett described the FDIC's supervisory approach. She noted fair lending examinations are risk focused and often start where discretion is exercised, either in pricing or underwriting. Ms. Plunkett said the FDIC does not discourage the use of discretion but said management needs to monitor its results; for example, whether loans made in one area are priced higher than in others, or if loans are denied more frequently in one area or denied based on a prohibited basis. She said a monitoring system needs to be in place so a bank can explain the business reason for its disparities in pricing loans and other exceptions from the norm. Ms. Plunkett noted the FDIC regional offices have examination specialists who review the most difficult cases and provide training to bankers through various outreach events.

Ms. Plunkett also described the HMDA Outlier Review which involves statistical analysis to identify those banks (usually 20 – 40 per year) which demonstrate the highest risk of pricing disparities. If a bank is identified as an outlier, a targeted fair lending review is conducted. She said, when evidence of a potential violation is found, the FDIC sends a "15-day" letter which explains the finding and gives the bank an opportunity to respond in writing. Upon request, examination staff will hold a conference call with the bank. Speaking about the Equal Credit Opportunity Act, Ms. Plunkett said cases involving a pattern or practice violation must be referred to DOJ, but, based on years of agency interaction, DOJ refers most cases back to the FDIC for administrative handling. DCP is exploring ways to make the process more efficient, Ms. Plunkett said. It also tasked a team of experts to review fair lending examinations from across the country to assure similar issues were handled consistently and to identify ways to be more effective and efficient.

Member Brown said his bank was trying to analyze its HMDA data but noted it would be helpful if banks could use the same analytical tools as the FDIC. Member Mehlum said she appreciated the focus on outliers and tying compliance reviews to consumer harm; she discussed additional methods of learning about harm from consumers themselves, for example, asking bank customers about their opinions during an examination, or correlating consumer complaints with information solicited by the CFPB. Member Mehlum also cautioned against the FDIC's apparent view of a banker's use of discretion as a red flag during a fair lending review. In her view, more broad-based consumer harm has been caused by giant, automated systems than has been caused by the exercise of discretion. Members Cole and Savarese expressed the view that examiners too often focus on technical violations where no actual consumer harm resulted. Member Savarese suggested it may be better framework for lenders to aim for compliance *excellence* rather than to

aim for *perfection* based on a fear of making technical violations. Mr. Pearce agreed the emphasis should be on consumer harm and it should infuse the entire examination and enforcement process; although mistakes cannot be ignored, the FDIC can communicate better about the relative seriousness of problems that it finds.

Ms. Ryan then introduced the day's fourth panel, "The FDIC's Preliminary EGRPRA Plan," and its moderators, Roberta McInerney, Deputy General Counsel, and Mindy West, Acting Associate Director, RMS ("EGRPRA" refers to the Economic Growth and Regulatory Paperwork Reduction Act of 1996). Ms. McInerney explained that the EGRPRA review was a periodic review of regulations aimed at eliminating outdated and unnecessary ones. She noted the EGRPRA review complemented other FDIC efforts to be efficient and effective and, because of the importance of reducing regulatory burden and previous banker requests for more time to provide comments, Acting Chairman Gruenberg had asked staff to begin the EGRPRA review a year early (the previous one was completed in 2006). Ms. McInerney noted the EGRPRA review requirement applied to all the agencies that belong to the Federal Financial Institutions Examination Council ("FFIEC"), including the Office of the Comptroller of the Currency and the Federal Reserve Board of Governors, but not the CFPB.

Ms. McInerney gave the Committee an overview of the EGRPRA review's process which, consistent with the law, begins by establishing categories of regulations by type (such as safety and soundness, or consumer protection) and assigning each agency regulation to a category. Then, the agencies publish the categories of regulations at regular intervals for public and banker comment on ways to reduce burden. Once public input is received and reviewed, Ms. McInerney said the agencies identify significant issues raised, eliminate regulatory burdens where they can, and publish a report for the Congress. If regulations had been issued with other agencies, any changes to them would be done on an interagency basis, she said. The report to Congress identifies and analyzes areas of burden reduction that require legislative rather than regulatory action. Ms. McInerney said the FDIC recently published on its website a preliminary discussion of the EGRPRA process, a list of the previous categories, and a request to bankers and the public to make recommendations about categories and the placement of regulations in them (including how to treat Dodd-Frank Act regulations).

Ms. West made several observations about how earlier Committee member recommendations would tie to the EGRPRA review. She also noted the EGRPRA process was transparent; every comment received will be reviewed by staff and shared with the public. Ms. West noted the previous EGRPRA review placed 131 regulations into 12 categories, and the categorization of regulations was, itself, an attempt to minimize burden on banks in analyzing regulations and providing comments. She also noted the FDIC would soon request further input on the categorization of regulations and the frequency of EGRPRA requests for comment; the FDIC would also ask for input on how to treat the Capital rules now being promulgated. Ms. West also said, in the previous EGRPRA review, bankers had said that mere "tweaking" of regulations is often not helpful because any change to a regulatory requirement requires bank resources to respond.

In response to a question from Member Gray, Ms. West said about 14 statutory changes had resulted from the previous EGRPRA review; among the more significant ones were changes

to the frequency of bank examinations and changes to Regulation O requirements. In response to a question from Member Mehlum, Ms. West said, in the previous EGRPRA review, agency leaders met with industry representatives several times in roundtable discussions. Member Baronner said such gatherings would help avoid misunderstandings and unintended consequences of the comment process. In response to inquiries from Members Mehlum and Savarese, Ms. West said, in the previous EGRPRA review, the burden reduction recommendations that required statutory changes had been sent to Congress as a single package.

Member Brown suggested that the EGRPRA review of the Regulation B spousal signature requirements would be productive; he said the current requirements were complex and created negative outcomes in actual application. Member Hopkins recommended that mortgage documentation requirements be reviewed from the ground up, he commented that the large numbers of papers requiring signatures obscured important information from borrowers and the revisions currently under review by the CFPB were too limited. Member Brown later suggested that HMDA reporting requirements could also be productively reviewed.

Ms. McInerney noted the CFPB was now responsible for a variety of consumer protection regulations for which the Federal Reserve was previously responsible and the CFPB had requested public input on those rules. She also observed that the CFPB is required to consult with the FDIC about many regulatory changes it makes and the CFPB had begun doing so. Ms. McInerney later noted the CFPB was not formally subject to the EGRPRA review requirements (although the CFPB must review its regulations on a five year cycle compared to the EGRPRA ten year cycle). Member Urrabazo suggested the CFPB and EGRPRA reviews could be joined. Member Savarese noted the FDIC often must examine banks for compliance with rules it does not write. She suggested it would be useful to include DOJ and the Department of Housing and Urban Development in the EGRPRA burden conversations to help keep them from drafting requirements that have unintended consequences on banks and consumers. Member Urrabazo suggested bankers and agencies identify members of Congress who could act as advocates for any EGRPRA burden reduction recommendation that required statutory change.

Ms. McInerney said, in light of the interest expressed, FDIC may consider providing an EGRPRA update to the Committee. Ms. Ryan also suggested the FDIC EGRPRA staff could consider the earlier review's practice of engaging with the banking industry and with other agencies, including the CFPB.

The Committee stood in recess at 11:46 a.m. and reconvened at 1:30 p.m. that same day.

Ms. Ryan introduced Bret Edwards, Director, Division of Resolutions and Receiverships ("DRR") and Marshall Gentry, Assistant Inspector General for Evaluations, Office of the Inspector General ("OIG") who moderated the discussion of "Impact of the FDIC's Shared Loss Agreements." Ms. Ryan noted that pursuant to a recently signed law, Public Law 112-88, referred to as House Resolution ("H.R.") 2056, the FDIC OIG is required to conduct a comprehensive study of the impact of the failure of insured institutions. The study requires the OIG to consider the impact of shared loss agreements ("SLAs") on loan modifications, credit availability, and participation loans; the study will also consider the FDIC's plans for terminating SLAs.

Mr. Edwards said the FDIC first used SLAs in selected purchase and assumption agreements of failed institutions in 1991. Under an SLA, the FDIC divides assets of a failed institution into commercial and single-family loan groups and sells the assets to Acquiring Institutions (“AI”) after competitive bidding, with the FDIC agreeing to absorb a portion of certain losses according to the SLAs. Mr. Edwards later explained the FDIC’s initial approach was to absorb 80 percent of the loss with the AI absorbing 20 percent, up to a certain dollar threshold of loss after which the FDIC absorbed 95 percent of the loss. He added, as the market for failed bank assets has improved, the FDIC now accepts AI bids that propose sharing loss at any percentage up to a maximum FDIC loss of 80 percent. Mr. Edwards said the FDIC had determined loss share reduces the FDIC’s immediate cash needs at the time of failure, is operationally simpler, more seamless to failed bank customers than other forms of resolution, and moves assets quickly into the private sector.

Mr. Gentry invited the Committee to provide feedback on whether the FDIC’s use of SLAs has an impact on the rate at which AIs modify loans. Member Brown said his bank was not an AI, and he had heard many consumer complaints about the difficulty borrowers experience in his area of Florida when they request loan renewals or modifications. He continued that his bank experienced more difficulty selling assets on which it had foreclosed in condominium developments, for example, where an SLA was a big presence compared to selling similar foreclosed assets where there was not a large SLA presence. Members Brown and Blanton said the real estate markets in their respective areas of Florida and Georgia were significantly negatively affected. Member Blanton added his concern as SLA agreements neared the end of their five-year coverage period, SLAs would return a large block of assets to real estate markets which had not recovered. Member Hopkins said his bank is an AI, and it was a misconception that an AI would merely dump properties onto the market explaining that an AI still shares in any loss. Director Hoenig asked whether the real estate impact discussed was the effect of excess supply or whether SLAs contributed to the negative effect. Member Brown said the negative effect was a result of both issues; he said, where an SLA was a large presence in a development, there was a significant negative impact on the value of condominiums. Member Blanton said that he saw a similar effect; he attributed it to the fact that an AI only had to experience 20 percent of a loss whereas a bank which had a similar property in OREO would have to experience a 100 percent loss and declined to sell. He thought that open banks would pursue different liquidation strategies for their OREO than SLAs do.

Member Grady said his bank was also an AI and it had developed a loan modification program the FDIC had approved. He said, as an AI, his bank had to market properties and document a market price before the FDIC would accept payment obligations under the loss share program. Members Hopkins and Grady agreed that FDIC representatives ensure that AIs properly justify decisions to dispose of an asset at the time they make the decision and a failure to adequately justify would endanger the loss share coverage. Mr. Edwards observed that SLA agreements require AIs to treat the SLA assets in the same way they treat their similar non-SLA assets. He agreed an AI’s disposition strategy could be affected by the fact it would experience a 20 percent loss. Mr. Edwards noted, when the FDIC resumed the SLA program in 2008, there was little market appetite for failing institutions and their assets without loss share and the alternatives to using SLAs (e.g., selling assets immediately into a depressed market, taking assets

into the FDIC to manage, including structured transactions) all had negative impacts compared to the use of SLAs. Mr. Edwards pointed out prospective AIs are now able to submit flexible bids, up to 80 percent, and as competition has increased recently, some winning bids have been at 50 percent. In response to Mr. Gentry's inquiry, Member Hopkins said, as an AI, his bank had the same incentive to work with customers on modifications. He said, if a customer had a problem and provided information, the bank would try to work with them, but it was more difficult if the customer was perceived as trying to take advantage of the AI.

Mr. Gentry then inquired about a second area of the OIG report, whether and how the FDIC's use of SLAs impacts credit availability. Member Hopkins said his bank became an AI so it could gain entry into a new market; because his bank had good capital ratios and the ability to expand, it found the SLA a useful way to enter an underserved market. Member Blanton indicated this was the right reason to enter an SLA, in contrast with AIs that enter an SLA just to liquidate assets and move on, without an intention to remain in the community. Mr. Edwards said there was some concern, as expressed by H.R. 2056, that the FDIC's loss sharing program provided disincentives for credit extension but he thought the opposite was true. He said SLAs keep assets in community banks and, although some borrowers were in difficult circumstances when an SLA is signed, there was a potential they would obtain credit extensions. He noted, in a failed bank situation, the FDIC generally does not have an interest in developing a long-term relationship with the failed institution's borrowers. SLAs have the benefit of transferring the customer to another banker who may have an interest in cultivating a long-term relationship.

Member Brown inquired if, as an SLA neared its five year termination, there was an incentive for an AI to dispose of assets (instead of keeping the credit) because there was a risk of losing the SLA's loss share coverage. Member Blanton also inquired whether SLAs had provisions that gave AIs more flexibility in disposing assets near the end of the agreements. Mr. Edwards said AIs can propose bulk selling some assets at a point in the last year of a five-year contract. He also said that, previously, the SLA would not permit an AI to modify a commercial loan's term past the SLA's fifth-year because five years was viewed as a lengthy period for commercial loans and there was an expectation that there would be significant economic recovery by five years. Mr. Edwards added, however, in recognition of economic conditions, AIs may now modify a commercial loan's term beyond five years although loss share coverage ends within the five years. He also questioned why an AI would be motivated to dispose of a performing loan just because its SLA coverage was lapsing. Mr. Edwards said commercial SLAs emphasize that AIs use the same work-out strategies for SLA assets as non-SLA assets; if an AI fails to do that, it risks having its loss claims rejected by the FDIC, which monitors them closely. In fact, Mr. Edwards stated that AIs have lost coverage on assets for not complying with the SLAs. In response to a question from Member Grady, Mr. Edwards reported that three early terminations of SLAs have occurred. Members Gray, Blanton and Brown also discussed with Mr. Edwards the treatment of loan modifications in comparison with TDRs. Member Hopkins suggested adding a new line to the Call Report entitled, "TDR covered under loss share," which he said would help clarify problems associated with performing loans still labeled as TDRs. In response to Mr. Gentry's inquiry, Member Blanton said he did not think that SLAs have any negative impact on banks' ability to extend or modify credit.

Mr. Gentry then inquired whether SLAs have an impact on participation loans, especially in situations where an AI has a lead role in a participation loan and non-AI community banks have a downstream role. Member Blanton said community banks had been significantly damaged being in small, downstream positions in participation loans and he doubted there would be as many participation loans as there had been in the past. Member Brown agreed and said lead banks perceived to be weak would have trouble engaging junior partners in participation agreements because of community bank concerns about future developments; he said his bank developed an approach of buying 100 percent of the participation if the lead bank was viewed as high risk. Member Brown also said his bank was concerned about community bank repudiation rights as part of the participation agreements. Members Brown and Blanton said the problem was an SLA issue because, when an AI assumes the lead position in a participation at a discount, it creates an unequal situation for the downstream participants who are still involved at 100 cents on the dollar. Member Blanton described a situation where the downstream participants were obligated under accounting rules to write down the value of the participation and the AI lead participant could then buy the community banks' downstream interests.

Mr. Edwards observed that an AI is not able to change a participation agreement; his understanding was that some AIs may have enforced their rights and responsibilities more seriously than the failed bank that drafted the agreements. He said there had been an instance of inadequate information sharing by an AI in one situation but that had been resolved. Member Blanton agreed some downstream participants had not adequately understood participation agreements had been drafted to greatly favor the lead participant. Member Grady described a situation where his bank became a lead participant as an AI and a downstream participant experienced a complete loss; he said he understood their loss but there was little that could be done since the credit was essentially unsecured. Member Hopkins also spoke about becoming a lead participant as an AI and having a strong disagreement with a participant bank that was avoiding writing down its credit.

In response to Mr. Gentry's inquiry about the general impact of SLAs, Member Blanton said SLAs were a necessary thing to clean up banking issues. He said some communities had been hard hit because all their banks were in loss share and there were no strong community banks left to do business. Mr. Gentry then invited Committee feedback on the termination of SLAs. He inquired how the FDIC can make terminations orderly and avoid negative impacts on the DIF and on lending to the real estate industry. Mr. Edwards commented that most of the discussion had been about commercial SLAs, which had the bulk of SLA assets, and which generally had loss share for five years. He noted that single family SLAs generally involved a ten-year agreement. Member Blanton suggested the FDIC consider extending five-year SLAs an additional two years rather than allowing those assets to flow back onto the market at deeply discounted prices, especially in hard hit areas. Member Hopkins said his bank would be interested in exploring a "clean-up call" of assets remaining in an SLA, referring to Mr. Edwards' earlier comment on early terminations. Mr. Edwards said the FDIC would be willing to discuss such issues and was considering various proposals. He said the FDIC had a pilot program in which SLAs with \$1.5 million of single family assets left in a portfolio would receive an offer from the FDIC to close out the SLA. Mr. Edwards said the FDIC shared Member Blanton's concern about releasing assets into areas with significant related asset concentrations and had not recovered as quickly as expected; he said the FDIC was considering strategies



recognizing the interests of AIs, non-AI banks and the FDIC. Mr. Edwards and Mr. Gentry noted that H.R. 2056 required the OIG to submit a report to Congress by January 3, 2013 and that Congressional testimony would accompany the report.

Ms. Ryan then invited the Committee to share any additional observations or concerns during the last panel, which was entitled, "Roundtable Discussion." Member Mehlum said she had two concerns about the viability of community banking: first was the rate of return to shareholders and what it needed to be; second was the cost of compliance, which she agreed was growing into a very important issue. Member Blanton repeated the recommendation that a way to reduce the cost of regulatory compliance would be for regulators to provide compliance guidance when they issue new regulations. Members Pierce and Rainey agreed that such guidance would need to be more specific than current guidance which tends to be too generic. Member Rainey provided an example concerning guidance on the oversight of third-party payment processors. She said, upon reading the guidance, she concluded her bank did not have significant risk based on its operations. Member Rainey was later surprised when the bank received a pre-exam request letter which appeared to indicate her bank should be taking a variety of compliance steps (despite the lack of risk exposure). Member Rainey indicated it would be helpful if the published guidance better predicted the examination standards that would be applied. At Ms. Ryan's invitation, Ms. Thompson addressed the issue, noting that if a risk is not present at a particular institution, examiners should not be asking for information addressing that risk. Pre-examination planning should identify what issues need to be examined and which do not.

Member Brown complimented the FDIC for being alert to the emerging risk of interest rate risk; he encouraged the FDIC to share specific information about problems it is seeing. Mr. Brown also said banks in his area are experiencing a problem with rules prohibiting mortgage originators from reimbursing clients when a mistake had been made; for example, reimbursing a client for the cost of a second appraisal when the first was faulty. He said the issue had been raised at a CFPB hearing and appeared to be shared broadly among mortgage originators. Mr. Pearce said he would gather more details and take appropriate action.

Member Savarese said the rapid pace of change in technology is a significant concern. She said technology helps level the playing field between community banks and large institutions, but also imposes a cost structure community banks have trouble maintaining. She suggested FDIC guidance on emerging technological changes would be helpful. Ms. Thompson agreed specific technologies change rapidly, and it is difficult for banks to remain current. She emphasized the FDIC takes a principles-based approach; for any delivery mechanism a bank considers, the bank should assess the risks the new technology raises, such as security and privacy as well as cost, and respond to those risks. Ms. Thompson said each of the FFIEC agencies have information technology examiners who meet regularly and consider different technologies and their risks, as well as institutions' unique risk profiles.

Member Savarese said a second broad issue of concern is the regulatory oversight of the core systems providers many community banks rely on to provide data processing services. She said there appears to be some inconsistency in regulators' communications about any problems found with the core systems providers. Ms. Thompson said the FFIEC works to conduct

interagency examinations of technology service providers. She said when supervisory issues or enforcement actions emerge, the agencies communicate to the processor who then communicates with its customers. Ms. Thompson said the heads of supervision of each FFIEC agency meet monthly to discuss issues, including information technology, to help ensure supervisory oversight is consistent.

Member Urrabazo described a situation in which an examiner informed his bank it needed to develop a policy about the Volcker Rule which explained why the rule did not apply to his bank. He also said he was advised his bank's sales associates who provided financial advice to a local county – including something as minor as telling the county representative what the renewal rate for a certificate of deposit would be – would require the bank employee to register with the Securities and Exchange Commission (SEC) to ensure compliance with the Volcker Rule. Acting Chairman Gruenberg noted the Volcker Rule was only a proposed rule, not a final one, so there should not be any compliance requirements. Mr. Watkins said RMS does not impose a requirement for a bank to take any special action regarding the Volcker Rule, and very few community banks would engage in any activity that would be considered a trading operation covered by the proposed rule. He said banks need to have policies on the types of investments suitable for their investment portfolios, and banks need to have systems to evaluate their asset-and-liability matches, but nothing such as Member Urrabazo described. Ms. Thompson and Mr. Watkins offered to discuss the matter further with Member Urrabazo. Member Urrabazo also recommended the FDIC represent community banks in the deliberations of other agencies, such as the SEC, whose rules on topics such as defining who is a financial advisor, would impact community banks. Mr. French said FDIC staff had discussions with SEC staff on the issues Member Urrabazo raised and he would make further inquiries about the results of them.

In response to an inquiry from Member Brown about the status of guidance on mobile banking, Ms. Thompson said the FDIC published an article on mobile banking in the *Supervisory Insights* journal, but no checklist had been assembled. Member Pierce inquired as to how FDIC management communicates emerging trend information to examiners. Ms. Thompson responded that the FDIC uses a variety of channels, including interactive video meetings where a presentation is made on a specific topic, examples are discussed, and examiners can raise questions. She also said examiners and bankers participate in industry calls, during which new policy or guidance being prepared for issuance is discussed. She noted that *Supervisory Insights* helps communicate supervisory information to bankers.

Member Savarese suggested the FDIC try to speed up the dissemination of information on the development of best practices; she noted there was some perception banks were being examined to the standards of best practices. Mr. Watkins clarified examinations are conducted looking at the traditional CAMELS factors, risk analysis, laws and regulations. To the extent best practices have developed, he said examiners share them as a useful piece of information for the bank's consideration. Member Savarese said although examiners do not indicate failure to follow a best practice will impact an examination rating, the examination reports imply there is a deficiency if the bank is not complying with them. She noted bank directors often do not fully understand how to evaluate examination discussions of best practices and said that, due to the relative power of examiners over community banks, bankers are hesitant to inform the examiner that certain best practices are not appropriate for their institution. Member Savarese indicated

what should be a dialogue between examiner and banker becomes a one way communication. Mr. Watkins said the FDIC will continue to work on improving examination communications.

Member Flynn expressed a concern, with new developments in technology, a substantial portion of the payments system had migrated to unregulated businesses. She said the payment system was the future of banking, and community banks were losing their place in it. Member Baronner noted because of the recent passage of the Jumpstart Our Business Startups Act, his bank had been able to deregister with the SEC, which would save the bank a great deal of work. He also observed accountants and regulators appear to work at cross purposes concerning the allowance for loan loss reserves and recommended they work together to develop a consistent methodology.

Acting Chairman Gruenberg said that he found the Committee's meetings to be very productive learning experiences. He said that FDIC hopes to issue its action plan concerning the Community Banking Initiative toward the end of the year.

There being no further business, the meeting was adjourned at 2:35 p.m.



Robert E. Feldman  
Executive Secretary  
Federal Deposit Insurance Corporation  
And Committee Management Officer  
FDIC Advisory Committee on Community Banking

Minutes  
of the  
Meeting of the FDIC Advisory Committee on Community Banking  
of the  
Federal Deposit Insurance Corporation  
Held in the Board Room  
Federal Deposit Insurance Corporation Building  
Washington, D. C.  
Open to Public Observation  
June 5, 2012 - 8:32 A. M.

I hereby certify that, to the best of my knowledge, the attached minutes are accurate and complete.



Martin J. Gruenberg  
Acting Chairman  
Board of Directors  
Federal Deposit Insurance Corporation

Dated: August 21, 2012