Las Vegas Business Press
April 24, 2016

FDIC loosens rules, encourages community banks

By Buck Wargo
Special to the Las Vegas Business Press

The FDIC has rescinded a 2009 order for heightened regulatory scrutiny of new banking institutions in a bid to increase the number of community banks.

The order issued in the midst of the financial crisis in 2009 extended the regulatory oversight from three years to seven years for examinations, capital maintenance and other requirements. That proved to be an added burden to lending institutions, and now the period of extra scrutiny for newly organized institutions returns to three years.

The move's been applauded by community bank executives in Nevada and across the country who say more institutions will be launched because of the rule change.

"I would say that this statement signals confidence from the FDIC in the overall condition of the banking industry," said James York, president and chief executive officer of Valley Bank of Nevada. "The fact that they're willing to shorten the oversight of de novo banks from seven years back to three years demonstrates that they're confident in the management and oversight of even the smallest community bank."

York said it will be interesting to see how many de novo applications are approved in the next couple of years.

Camden Fine, president and chief executive officer of the Independent Community Bankers of America, said the rule change will make a difference. Fine, who talked about FDIC announcement while attending a retail banking conference in Las Vegas this month, said that up to 2008 about 125 institutions a year were created. There were two created nationwide in the past five years.

"I think we're going to have maybe 10 or 11 or as much as 15 banks a year now," Fine said. "When the regulatory agencies expanded, that was seven years of dividend restrictions, examinations and holding of super capital."

The FDIC said it issued the rule change in 2009 against the backdrop of an elevated number of newly insured institutions that had either failed or had been identified as problem banks during the financial crisis. State and federal agencies charter banks, while the FDIC's role in the establishment of new banks is in the approval of deposit insurance.

"The entry of new banks has helped to preserve the vitality of the community banking sector over time," said FDIC Chairman Martin Gruenberg who made the announcement at a conference hosted by the FDIC. "De novo institutions fill important gaps in our local banking markets, providing credit and services to communities that may be overlooked by larger institutions."

Arvind Menon, president and chief executive officer of Meadows Bank in Las Vegas, attended the community banking conference in Washington, D.C. where Gruenberg made the announcement. He said bankers thought it would happen over time but were surprised to hear the change now. The industry believes it's a step in the right direction, he said.

"I am happy to hear that," Menon said. "That might spur small groups to try and put banks together, which in our town we could use a few more. Clearly the FDIC is trying to drum up more applicants. Community banking is an extremely important niche in the business world here."

Meadows opened in 2008 expecting a three-year enhanced supervision period only to find it extended to seven. Under the rules in 2008, banks were required to file a business plan for the first three years. That meant any deviation from the plan had to get prior approval by the FDIC, in Washington, D.C. rather than San Francisco in some cases. Meadows had to file another plan after three years and adhere to it closely and seek out approval for offering a new product or getting into a different line of business, Menon said.

"I can tell you from personal experience that anytime you're closely supervised by the FDIC during that de novo period, it's a tremendous part of oversight and difficult," Menon said. "The gloves come off after the de novo period so to speak. You are able to operate like a regular business at that point in time."

Valley Bank of Nevada opened in 2005 and was out of its three-year mode when the rule changes brought them back under enhanced scrutiny, York said. He didn't think that was fair because it meant a return to heightened regulations and more frequent visits that take time and add expense to community banks.

"When you're a de novo bank, you have to have permission before you can do anything and it's 'mother may I,'" York said. "After the de novo status, you just inform them of any changes of either new products, business lines, or locations or even changing out board members. When you're de novo, you have to get pre-approval to do all of those things."

Both bank executives said there institutions are doing well.

Menon said he doesn't want to boast, but cited a research report rating the bank as rated No. 5 in the country for top performing banks with less than $1 billion in assets. Meadows has a $500 million loan portfolio.

"We went from zero assets when we started to more than $500 million and change now," Menon said.

York said his institution "flat lined for five years" but started growing again in 2013 and is doing great. He added that 2015 was its biggest year of growth when it did $25 million in new small business loans, more than double what it had done prior to that.

"The economy is improving and coming back and the timing is good, and that's why you see the FDIC saying we will take some new bank charter applications now," York said. "(Businesses) weren't borrowing for a while, and now they're back borrowing again. The quality of loans are getting better and better, and I'm seeing improvement across the board."

York said he thought launching a de novo bank in 2005 was a brilliant idea but not so much in 2008. In the end, however, he said it turned out to be a "pretty good idea because there's few of us left." He said his charter and business is more valuable because of it.

As for whether he would do it again, Menon said it’s a tough question to answer but said he would not go through it if the regulatory period would be for seven years instead of three.

“Three years, I would have never had a problem,” Menon said. “But in the last few years with Dodd-Frank and all of those kinds of things, the regulatory environment has changed significantly and the amount of regulation has increased where small banks like us have tremendous overhead to keep on top of regulations and make sure we’re complying.”

Menon said he doesn’t know how many banks will be launched with the rule change. There are likely some who are giving it thought but nothing will happen quickly, he said. There are still regulatory hurdles and a high amount of oversight and capital requirements

“That might still give reason for people to pause and not jump into it,” Menon said. “Certainly the reduction of the timeframe will be a positive. It’s a good idea. Definitely a good idea.”