



August 20, 2021

**VIA E-MAIL AND FEDERAL EXPRESS:**

The Honorable Representative Jacob D. Auchincloss  
House Committee on Financial Services  
United States House of Representatives  
1524 Longworth House Office Building  
Washington, DC, 20515

**Re: H.R. 4590 Promoting New and Diverse Depository Institutions Act**

Dear Congressman Auchincloss:

America's Mutual Banks (AMB) congratulates you on the Committee's passage of your Bill, H.R. 4590. If it becomes law, it will do much to focus the federal bank regulators on the formation of minority depository institutions (MDIs); and the important role diversity in banking plays in the overall health of the United States economy. We strongly support H.R. 4590, however we seek inclusion of express references in H.R. 4590 to promote the formation of de novo MDI mutual institutions. The addition of clear chartering provisions and guidelines would significantly aid in the formation of de novo MDI mutual institutions.

**America's Mutual Banks**

AMB is an unincorporated association whose membership consists of mutually chartered FDIC insured institutions and mutual holding companies. AMB's membership consists entirely of community based institutions dedicated to serving their communities and fostering the economic growth of those communities. Community based, mutual form institutions and holding companies are historically a vital part of the fabric of many communities and their future viability must be protected and enhanced.

**Importance of the mutual bank and MDI model**

Mutual MDIs, and community development financial institutions (CDFIs) are central to the strength of the U.S. economy, and to the local communities they serve. Rural and minority communities have been for the most part neglected even by regional depository institutions. Creation of mutual depository institutions, which have historically served rural and minority communities, has ceased. **No new mutual has been chartered for over a half a century.** Data on de novo formation and mutual banks leaves no doubt as to the neglect of the banking agencies of their statutory responsibilities. Effectively, the federal government has abandoned its statutory mandate to charter and insure the deposits of de novo mutuals. This has left a void in banking services in many of the communities that need them the most.

Legislative changes, combined with the indifferent attitude of the OCC, the FDIC and state banking regulators towards mutuals, has led to an overall decline in the diversity and number of these institutions. Indeed, since the late 1960s, no de novo mutual has been insured by the

FDIC or its predecessor FSLIC. During the period from 1984 to 1994, mutual institutions' asset share of the total banking industry fell from 16% to 4%; while the number of chartered mutuals also declined from 2400 to 1076. Today the number of mutual banks is approximately 500. Mutual MDIs have suffered an even greater decline. Despite this, mutual banks remain resilient, with only approximately twelve relatively small mutuals failing as a result of the Great Recession. Moreover, as the FDIC notes, "mutuals were an unexpected source of stability within the banking system", providing higher quality loans, before, during, and after the financial crisis.<sup>1</sup> This is significant given that as of 2015, 78% of mutual institutions specialized in mortgage lending.

### **The Mutual Form is tailored for MDIs**

The history of mutual depository institutions in the U.S. is a proud one. During the first half of the twentieth century mutual savings associations, building and loan associations and savings banks flourished. They provided financial services to immigrant, minority and low income groups that commercial banks simply ignored. Indeed, these institutions were formed by community groups, for the community and were managed and staffed by community members. (See Mehrsa Baradara's *How the Other Half Banks: Exclusion, Exploitation and the Threat to Democracy*, for a detailed account of the role mutual banks played in serving the unbanked). Indeed, the mutual culture was idealized by Frank Capra's classic movie, *It's a Wonderful Life* as a tribute to the role mutual institutions played in fostering the prosperity of the average American.

While the necessity for profitability levels that will achieve viability and also provide attractive stockholder returns is a critical factor in the lack of interest by organizing groups in forming de novos in low income communities, the absence of stockholders in a mutual eliminates this factor. A mutual MDI is chartered for altruistic reasons, not for the profit of its founders but as in the Capra movie the prosperity of its community. It by definition is mission driven. It need not achieve profitability levels that will tempt riskier business strategies. It is not compelled to "swing for the fences" because of stockholder demands for short term profit. Ironically, a stock MDI that succeeds is more likely to monetize that success for its stockholders by selling itself and merging out of existence. Thus, a stock owned MDI provides little long term benefit to the community. If it fails, it leaves the community without the financial services it was chartered to provide; if it succeeds, it produces the same result by merging out of existence. On the other hand a mutual MDI becomes a trusted educator for financial literacy of its customers, an incubator for developing financial skills for community members who will staff the institution and source of trust to the community as its leaders and founders will be trusted members of the community. Most importantly, it cannot be bought and sold or merged out of existence for the benefit of its founders and owners. It is in it for the long haul. It is regrettable that the many positive attributes of the mutual format have been almost forgotten by those in the best position to support the underbanked and unbanked in the community.

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<sup>1</sup> FDIC. (2016). Mutual Institutions: Owned by the communities they serve. *FDIC Quarterly*, 10, 47-59.

## **Statutory changes**

Despite the best intentions of Congress and federal regulators, the chartering and deposit insurance processes have evolved in a manner detrimental if not exclusionary to the formation of mutual MDIs. While the OCC and the states are the only chartering authorities, current banking law require federal or state chartered de novo institutions to acquire FDIC deposit insurance.

Until the passage of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Congress required deference to the OCC's chartering decisions by the deposit insurers (the FDIC and FSLIC) in insuring the deposits of national banks and federal savings associations. Essentially, they were required to defer their decision on a deposit insurance application to the primary federal chartering authority. Prior to FIRREA, the deposit insuring agencies, the FDIC and the FSLIC, had a duty to insure de novo national banks and federal associations. Under FIRREA, the FSLIC was eliminated and its duties were transferred to the FDIC. The duty to insure was also eliminated under FIRREA.

While FIRREA mandates agency support for MDIs, the statutory changes have created a significant obstacle to the formation of any mutual de novo, and especially mutual MDI de novos.

## **Existing capital requirements are incompatible for community banks**

As highlighted above, the elimination of deference to the OCC, means the FDIC can determine the viability of a de novo institution based solely on its assessment of the deposit insurance application. For MDI mutuals, this is particularly burdensome because the capitalization requirements, and overall application process is tailored towards commercial banks with aggressive, oftentimes national growth business plans, and not towards firms operating in lower-income communities. Insurance risk is the predominant factor, not community need and success. Effectively the FDIC has superseded the prerogative of the OCC the chartering agency. Without an applicant's compliance with the FDIC's insurance of accounts requirements, the exercise of the OCC's authority is purely symbolic. Effectively, Congress has given the FDIC veto power over all OCC chartering decisions. This power has been used to create unreasonable, and often insurmountable initial capitalization requirements. Any suggestion that this is an exaggeration is rebuffed by a simple inquiry into the number of de novo mutuals insured since the 1960s.

On one hand, the FDIC's Handbook for Organizers of De Novo Institutions states that "the FDIC does not prescribe a minimum dollar level of capital for any given proposal", but rather requires a tier 1 capital to assets leverage ratio of 8% through the first three years of a de novo institution's operation.<sup>2</sup> However, many groups who have attempted to form de novo institutions have stated they believe the FDIC implicitly expects a minimum capitalization of

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<sup>2</sup> Federal Deposit Insurance Corporation. (2019). *Applying For Deposit Insurance: A Handbook for Organizers of De Novo Institutions*.

\$20-\$25 million.<sup>3</sup> While these guidelines are unclear, the fact remains that the capital to assets leverage ratio of 8% for the first three years of operation, is burdensome for community banks.

These unclear and burdensome capital requirements create a significant entry barrier for prospective de novo mutual MDIs. In cases where an application for deposit insurance is granted, these high capital expectations can lead management to seek riskier investments, and often outside of the communities their bank serves. Overly burdensome capitalization requirements, are antithetical to the mission of MDIs and inhibit their ability to serve their communities. For a mutual MDI, these capital requirements are the equivalent of hanging a sign at the FDIC's doorstep saying "Mutual MDIs need not apply."

### **Recommendations**

AMB proposes explicitly addressing the chartering process for MDIs, and CDFIs, in the mutual form in H.R. 4590. In its current form, H.R. 4590 addresses implicitly, but not expressly, the issues raised by the dearth of mutual de novo formation. The absence of an approach which seeks answers to the lack of formation of de novo mutual MDIs, will not encourage a reversal of the low de novo formation rate.

As such, AMB recommends reinstating the deference principle for MDIs, to streamline and clarify the de novo formation process. While deposit insurance remains a condition for the formation of de novo institutions, decisions regarding the business potential of the institution should stay within the domain of the federal chartering authority, the OCC, and not the FDIC (a naturally risk-averse institution). Reinstating the deference principle is fully within Congressional purview, and would be a significant step in remedying one of the major barriers to de novo mutual formation. Moreover, it would give the OCC additional authority to implement the Congressional mandate to promote MDIs.

Secondly, AMB proposes modifying capital requirements specifically for mutual MDIs. There is no distinction in Tier 1 capital requirements between commercial and community institutions, creating a significant barrier to entry for institutions serving the most vulnerable communities. Although ultimately guidelines should be set by the FDIC, AMB recommends inserting language into H.R. 4590 that calls for an evaluation existing capital requirements for de novo mutuals. Language could suggest the phasing in of capital requirements on an annual basis, rather than a static 8% Tier 1 capital to assets ratio for the first three years of operation. More importantly, the FDIC's capital interpretations must be harmonized with federal and state law regarding the capitalization of de novo mutuals. Historically, mutuals have relied on pledged deposits and mutual capital certificates to raise capital. Those methods have been effectively repealed by agency interpretations of the Basel capital requirements which apply to systemically significant institutions. This was done by agency fiat not Congressional action. Ironically, these interpretations failed to recognize the various

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<sup>3</sup> American Bankers Association. (2019). *Comment Letter on the FDIC's Deposit Insurance Application Process* (FDIC: RIN 3064-ZA03),

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exceptions adopted by European regulators for their cooperative and mutual financial institutions leaving US mutuals at a severe disadvantage.

Thank you for your continued support for seeking solutions to the dearth of de novo MDIs especially de novo MDI mutual institutions. We look forward to working with you, and the full Financial Services Committee to explore new pathways to MDI mutual bank formation. If you have any questions concerning our recommendations, please contact the undersigned at [dfaucette@lockelord.com](mailto:dfaucette@lockelord.com) or (202) 220-6961.

Sincerely,

A handwritten signature in black ink, appearing to read "Douglas P. Faucette". The signature is fluid and cursive, with a large initial "D" and "F".

Douglas P. Faucette  
DC Director  
America's Mutual Banks

cc: Senator Sherrod Brown, Chair, Senate Banking, Housing, and Urban Affairs Committee  
Senator Patrick J. Toomey, Ranking Member, Senate Banking, Housing and Urban Affairs Committee  
Congresswoman Maxine Waters, Chair, House Committee on Financial Services  
Congressman Patrick McHenry, Ranking Member, Bill Co-Sponsor, House Committee on Financial Services  
Congressman Al Green, Bill Co-Sponsor, House Committee on Financial Services  
Congressman Van Taylor, Bill Co-Sponsor, House Committee on Financial Services  
Congresswoman Joyce Beatty, House Committee on Financial Services  
Len Stekol, Chairman, America's Mutual Banks