Remarks of John E. Bowman, Acting Director
Office of Thrift Supervision
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Good morning. Thank you very much for that introduction, Jim, and congratulations on your installation as the new ICBA chairman. We look forward to working with you and your organization in the coming year. I would like to thank Cam Fine for the gracious invitation to speak today. I'd also like to recognize Wayne Cottle of Dean Bank in Massachusetts, who is ICBA Secretary and a member of OTS's Mutual Savings Association Advisory Committee. And last, but certainly not least, I'd like to recognize former OTS Director John Reich, who is here with us today.

I am very pleased to be with all of you at your national convention, chiefly because community bankers like you represent the essence of the consumer-and-community lending at the heart of the U.S. thrift industry.

I must also admit that I am very happy to be with you here in the warmth of Orlando after digging out of five feet of snow in Washington this winter. Although you might argue that Washingtonians have become tougher this year in dealing with the harsh weather, I have never been so glad to see spring.

It's been almost a year since I became Acting Director of the OTS. I won't ever forget that day – just a few days after your national convention last year in Phoenix – when the Treasury Secretary informed me that I would be leading the agency. I haven't had much time to dwell on those events, or to look back, because the whirlwind financial crisis was already well under way and only now begins to show signs of waning.

A great deal has occurred during that time. There have been many challenges for the OTS, for the other federal banking regulators, for the financial services industry, for the global economy, and for consumers in this nation and across the world. I am happy to report to you that, despite these challenges, the OTS continues to be a healthy, vibrant organization that is hiring new employees and planning for the future.

However, as you well know, financial institutions of all types continue to feel tremendous strain from problem assets – a strain that a growing number of institutions will not survive. And too many families are struggling to pick up the pieces of their lives after job losses, foreclosures and other personal calamities.

Understandably, after a crisis like this, there is an eagerness to fix what went wrong, so such a crisis cannot happen again. Members of Congress hear the voices of their constituents calling for reform. Something meaningful must be done.

I can tell you honestly that we at the OTS agree with the calls for reform. It is not acceptable for companies to be too big and too interconnected to fail, that have through sheer size and complexity been awarded an invaluable, implicit government guarantee that grants them an unfair advantage over their competitors. The too-big-to-fail syndrome warps the system of proper risks, rewards and consequences that underpins our financial system and our economy. It is critical that this nation have an orderly process to wind down large, interconnected financial firms that are failing.

Nor is it acceptable for some people who offer home mortgages and other financial products to American families to escape the reach of nationwide consumer protection rules that apply to others who offer the same products. The same rules must apply to everyone offering financial services products. Otherwise, competitive forces exploit the holes in the system and consumers suffer.

Nor is it acceptable for financial institutions to engage in the trading of opaque and complex derivatives outside the scope of federal regulation. The consequences of these gaps have become all too clear.

I have no illusion that my views on financial regulatory reform might be taken with one or more grains of salt. After all, we at the OTS are not disinterested observers in this debate. Critics are fond of saying that the OTS and the other regulators are looking out for themselves and protecting their own turf. That's a fair point. I have testified before Congressional committees five times in the past year and I can assure you that not once have I advocated the elimination of the Office of Thrift Supervision. The Bush Administration and the Obama Administration have advocated it. Lawmakers on Capitol Hill have advocated it and a bill that would close the OTS passed the House of Representatives. Another bill is pending in the Senate.

Yet, as you know, prospects for final passage appear no more certain now than in the past and I continue to believe that the consumer-and-community lending embodied in the thrift charter is a model that should be nurtured, not discarded.

Boards of Directors and financial institution managers should continue to make their plans for the future based on their business models and business plans, not based on fear of the unknown and the uncertain outcome of events on Capitol Hill or elsewhere.

Community banks and thrifts have, for the most part, weathered this recent economic storm quite well, as long as they closely adhered to the model of making loans to their local consumers and communities – and keeping those loans on their books. I don't need to point out to you that this model is embraced by most of the people in this room.

For many Americans, the classic 1940s movie, "It's a Wonderful Life" captured the image of a typical savings institution, the Bailey Building and Loan Society. Thrifts have traditionally engaged in relationship banking, where bank executives – like George Bailey in the movie – frequently know their customers by name and extend credit based on personal knowledge of the borrower's character, integrity and ability to repay.

That may seem like an old-fashioned view of the banking business in modern times, but if this recent financial crisis has taught us anything, it is that traditional banking principles possess real staying power and value. To the extent that the financial services industry has moved away from those principles, we have moved into territory fraught with risk.

So, yes, I continue to believe in the thrift charter, I continue to believe in the thrift industry and I continue to believe in the Office of Thrift Supervision. We are seeing some encouraging signs of renewed vigor in the thrift industry. In fact, in the fourth quarter of 2009, the thrift industry posted a profit of $505 million. For all insured depository institutions, the profit for the quarter was $914 million. So thrifts, which constitute about one-tenth of all insured institutions, were responsible for more than half of the profits.

I have a sense of optimism as we at the OTS look toward the future – accepting new charter applications, sustaining our expert workforce and tackling the continued challenges to the industry from bad assets.

As I have said more than once in Congressional testimony and elsewhere, in the rush to fix what caused this financial crisis, we must ensure that changes to the financial regulatory system address real problems. Neither the bill that passed the House, nor the proposal pending in the Senate, pass that test. For true regulatory reform, it is time to start over – with a clean slate – and get it right.

It is crystal clear to me that a super regulator like the one in Great Britain, as envisioned in the original Senate bill, is not the way to go. With more than 8,000 federally insured depository institutions that range from a handful of megabanks to thousands of community banks like yours, the United States has a vastly larger and more complex financial service sector than any of the nations with a single regulator. Those nations fared no better than the U.S. during this financial crisis. Years from now, we don't want to be looking back and saying that a U.S. super regulator helped cause another financial crisis. So, I am glad that the model of a single bank regulator has – thus far – been rejected.

I strongly believe that one basic principle should form the foundation of prudential regulation of financial services in America. It is a principle that has largely been overlooked during this long debate about regulatory reform and it is a principle that no major bill under consideration in Congress has embraced. However, it is a principle that I think everyone in this room will understand and appreciate.

The principle is that the thousands of community banks like yours in cities, towns and rural areas around this country have almost nothing in common with megabanks like Bank of America, JPMorgan, Wells Fargo and Citigroup. Nor do they have anything in common with the large, complex commercial banks that have not yet grown to megabank proportions. The vast differences involve not only scale, but also complexity, risk management, lines of business and daily operations. At a community bank, concerns often focus on interest rate risk – not on derivatives or complex computer models. The OTS shares that focus on interest rate risk and closely tracks it through our unique interest rate risk model.

Whether a community bank holds a state charter, a national bank charter or a federal thrift charter, that institution should not be supervised by the same agency that oversees complex commercial banks. The one-size-fits-all regulator, by necessity, will pay the greatest attention to the complex commercial banks, because they pose the greatest potential risks to the financial system. As a result, the community banks and thrifts that – by far – make up the largest number of institutions will receive "afterthought" supervision, rather than a regulatory approach tailored to their unique business model.

It is ironic that none of the bills pending in Congress would provide community banks with their own dedicated regulator. Take a close look at the practices that have caused problems during this crisis, such as weak loan underwriting – especially for loans sold into the secondary market; lending in hot real estate markets outside the institution's geographic service area; and extending credit to borrowers based on the value of the collateral, rather than the borrower's ability to repay.

Those are not the practices of traditional community banks and thrifts. In fact, as I pointed out, community banks and thrifts that stuck with their conservative principles have fared much better than most institutions during this crisis. Mutual institutions, which have rightly been called the quintessential community banks, are perhaps the greatest embodiment of those principles.

The federal government should be promoting the community bank model, not taking actions that threaten to foster and accelerate the consolidation that has fed the rise of the megabanks. The community bank business model is unique enough – and community banks are numerous enough – to warrant separate treatment.

Our proposal is simple: instead of four federal banking regulators – the Federal Reserve, the FDIC, the Office of the Comptroller of the Currency and the OTS – there should be two: one for community-based banks and thrifts, and one for complex commercial banks.

In addition, holding companies would be supervised on a consolidated basis by the primary federal functional regulator of the underlying financial institution.

This model would ensure that the community bank regulator would be free to focus on what is best for community banks, for the communities served by those banks and for consumers.

There should be no competing or conflicting interests. That's why I don't favor the idea of making the FDIC the federal regulator of all state chartered banks. Administration of the nation's deposit insurance fund creates an inherent conflict with prudential bank supervision. As the administrator of the deposit insurance fund, the FDIC's interest lies in minimizing losses to the fund from bank failures. A bank regulator's mission is to ensure the safe and sound operation of the institutions it regulates.

Those competing interests, which can sometimes collide, are best managed through discussions and negotiations between the FDIC and the prudential regulator – not through internal discussions within the FDIC. Combining supervision of all state-chartered banks under the deposit insurer would be returning to the FSLIC-Federal Home Loan Bank Board model that was correctly rejected two decades ago.

I also believe the Federal Reserve is not the logical federal regulator for community banks. The Fed's chief focus is on monetary policy. Prudential supervision of community banks would always be relegated to a lesser level of concern. Although the Fed's monetary policy decisions benefit from observations of global economic conditions, Wall Street trades and the dealings of complex, systemically important financial institutions, supervision of community banks provides nothing beyond the insights that could be gleaned from information provided by other bank regulators.

I believe community bank supervision would best be managed by a new independent agency that would have the sole mission of supervising community banks and thrifts, supervising their holding companies and protecting consumers. For the first time, the health and welfare of this nation's community banking sector and its consumers would be the top priority of a federal agency. This priority would not negate all of the forces that have led to the industry consolidation of recent decades, but it would ensure that regulatory perspectives and decisions for community banks would not be colored by the competing interests of large, complex banks.

Because this new agency would be dedicated to consumers and communities, the agency would also be the best location for a consumer protection division, led by a presidential appointee, with input from an interagency council of regulators. The consumer division would write rules that applied across the financial services landscape and would enforce those rules for nonbank businesses. For banks and thrifts, the primary federal regulator would enforce consumer laws and regulations, with input from the interagency council of regulators.

This proposal is a broad outline, not an intricate blueprint planned out to the last detail. There are questions that would need to be answered and fine points that would need to be spelled out. For example, the new agency would have to be funded by assessments without imposing an unnecessary burden on state-chartered banks that now pay for deposit insurance, but not a federal assessment for supervision.

There are other key details, such as where to draw the line between community banks and complex commercial banks and, if institutions' business models evolved, how they would make the transition from one to another.

Because of important questions such as these, I am presenting this proposal to you today as a starting point for a renewed discussion. My hope is that, as the legislative calendar moves on, Congress will decide to take up this debate anew, without the distraction and emotion of legislating in the middle of a crisis.

In the meantime, we believe the current system is far superior to the system envisioned by current Congressional proposals. We also believe that the thrift charter and its regulatory framework hold intrinsic value for our nation and provide a highly attractive model for financial institutions such as yours that focus on consumer and community lending.

I ask each and every one of you to think about these issues and discuss them. What do you think is the best approach to reform? What would be best for your business, your industry, your customers and your nation?

Community banks and community bankers have a great deal of credibility right now. Although the average American might think all bankers are at least partly to blame for the crisis, insiders and experts in the financial services industry, government and elsewhere recognize that community banks and thrifts did not cause this problem – and they know that community bankers could light the way toward reshaping the system for the future.

Community banks should have a separate, dedicated regulator, no matter what type of charter the community bank might have. An industry with a specialized regulator is more likely to survive, to thrive and to effectively serve its customers than an industry regulated as an afterthought. It's that simple – and it's not too late.

Thank you again for having me here today. I'd be glad to answer any questions.