Testimony
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On behalf of

Independent Community Bankers of America
Washington, DC

"Oversight of the Office of Thrift Supervision"

United States House of Representatives
Financial Services Committee, Subcommittee on
Oversight and Investigations

May 25, 2006

Mr. Chairman, Ranking Member Gutierrez and members of the Subcommittee, my name is Ted Gurzynski and I am Vice President and Chief Credit Officer of PyraMax Bank, FSB, located in Greendale, Wisconsin. It is my pleasure to speak to you about today about the Office of Thrift Supervision (OTS) on behalf of the Independent Community Bankers of America, which represents approximately 5,000 community banks across the nation, many of whom like PyraMax Bank are federal or state savings associations or thrifts regulated by the OTS.[1]

Summary of ICBA Views

ICBA believes that the excellent health of the thrift industry and its remarkable recovery since the enactment of FIRREA can be attributed to the supervision and regulation of the OTS as well as to the vitality of the thrift charter. OTS has fulfilled its mission well as the nation's primary regulator of thrift institutions and has expertise in supervising institutions whose business focus is housing finance. ICBA opposes eliminating the OTS and merging or shifting its duties to another agency. As long as the institutions it regulates prefer a separate regulator and support the agency through assessments, the OTS should remain a separate regulator.

ICBA commends OTS Director John Reich for his efforts to reduce unnecessary regulatory burden on banks and thrifts and the leadership that he has assumed under the Economic Growth and Regulatory Paperwork Reduction Act ("EGRPRA") project. The support of the OTS and the other banking agencies has been critical for the successful passage of H.R. 3505, the Financial Services Regulatory Relief Act of 2005, in the House and will be critical for passage of S.2856, the Financial Service Regulatory Relief Act of 2006, in the Senate. ICBA generally supports the savings association provisions in H.R. 3505 and S. 2856.

In its role as an advocate for all community banks, ICBA promotes mutuality as a viable charter alternative that should be accorded parity in all respects with other charter forms. We agree with the OTS that regulators should be neutral when it comes to charter choice and charter conversions. The National Credit Union Administration attempts to thwart the conversions of credit unions to mutual savings banks violate this principle.

Mission of the Office of Thrift Supervision

Established by Congress as a bureau of the Department of Treasury on August 9, 1989, OTS charters, examines, supervises, and regulates federal savings associations (thrifts) insured by the Federal Deposit Insurance Corporation (FDIC). OTS's primary statutory authority is the Home Owner's Loan Act or HOLA originally enacted in 1933. OTS also examines, supervises and regulates state-chartered thrifts insured by the FDIC and provides for the registration, examination, and regulation of savings and loan holding companies and other affiliates.

[1] Throughout this statement, the terms "thrifts" or "savings associations" will be used interchangeably.

With a skilled staff of 900 employees most of whom work in four regional offices, OTS has done an excellent job of supervising and examining thrifts under HOLA. ICBA notes that just recently the OTS announced plans to hire 60 new examiners, bolstering its exam staff by 11.5 percent. In addition, OTS has stated that it will re-establish at its Washington headquarters a centralized direction for compliance, Community Reinvestment Act and consumer protection—a function that was formerly delegated to the regional offices. ICBA commends the OTS for taking these actions to improve its ability to supervise the nation's savings associations.

Health of the Thrift Industry

Today's thrift industry has never been healthier. For 2005, assets for institutions regulated by OTS were up 12 percent from the prior year to a record $1.46 trillion. In the past five years, industry assets grew 57.7 percent, representing a robust average annual five-year growth rate of 9.5 percent.

Earnings, too, were strong last year, and have been very strong for the past five years. For 2005, earnings were up 17.6 percent from 2004, and industry earnings more than doubled in the last five years, climbing from $8.0 billion in 2000 to a record $16.4 billion in 2005.

The industry equity capital ratio improved to a record 9.45 percent at the end of 2005—well in excess of minimum requirements—and the amount of equity capital held by thrifts reached a new record. Over 99 percent of the industry currently exceeds well-capitalized standards and no thrift was less than adequately capitalized at year-end. Of the 863 savings associations regulated by the OTS, over 94 percent achieved an overall composite CAMELS rating of 1 or 2 last year.

ICBA believes that the excellent health of the thrift industry and its remarkable recovery since the enactment of FIRREA can be attributed to the supervision and regulation of OTS as well as to the vitality of the thrift charter. OTS has provided effective regulation that has allowed this industry to both thrive and operate in a safe and sound manner. With its ability to operate nationally under uniform standards and its flexibility to engage in a wide variety of activities, many view the federal thrift charter as the preeminent retail banking charter.

ICBA opposes eliminating the OTS and merging or shifting its duties to another agency. The OTS has done an excellent job in supervising the thrift industry and assisting it through some very troubled times. As long as the institutions it regulates prefer a separate regulator and support the OTS through assessments, the OTS should remain a separate regulator.

Furthermore, having a separate regulator for thrifts can help focus that industry on the nation's housing market and housing finance. Housing is one of the principal drivers of the American economy, accounting for more than 20 percent of the annual gross domestic product (GDP). Thrifts are major players in this arena and therefore make a significant contribution to the nation's GDP. Total thrift mortgage originations for

2005 were $744.1 billion and accounted for 26 percent of total 1-4 family originations in the fourth quarter.

The business focus for most thrifts remains residential mortgages and supporting the nation's housing market. Thrift investments related to residential mortgages still account for more than 65 percent of total industry assets. Although thrifts have been expanding into consumer and commercial lending, single-family mortgage loans account for nearly half of thrift assets. The OTS has demonstrated that it has the expertise and competence to regulate all aspects of this important industry.

Reducing Regulatory Burden

ICBA commends Director Reich for his efforts to reduce unnecessary regulatory burden on banks and thrifts and for the leadership that he has assumed under the EGRPRA[2] project. Through the public comment process, banker outreach meetings and the EGRPRA website, the project has generated a large number of recommendations for reducing the regulatory burden on banks. Changes to the Community Reinvestment Act regulations to extend eligibility for streamlined CRA exams to more community banks, and the amendments by the FDIC to the Annual Audit and Reporting Requirements (Part 363) to eliminate costly internal control attestations for privately held banks with up to $1 billion in assets, are examples of burden reduction measures recently adopted by the banking agencies that were due, in whole or in part, to the efforts of the EGRPRA project.

However, Director Reich's competent leadership of the project, and his passionate belief that unnecessary regulation must be reduced, were critical to achieving the goals of the EGRPRA project of identifying outdated, unnecessary, or unduly burdensome regulatory requirements. The universal message from the EGRPRA banker outreach meetings is that community banks are struggling under the burden and costs of regulatory compliance. This burden is eroding the ability of community banks to compete effectively. Even though the last three years have been very profitable for the banking industry as a whole, there is a gap between community banks' profitability and the rest of the industry, in part due to the disproportionate impact of regulations on community banks, causing many community banks to consider selling or merging. As Director Reich stated in Congressional testimony, "I believe that in looking to the future, regulatory burden will play an increasingly significant role in shaping the industry and the number and viability of community banks….if we do not do something to stem the tide of ever increasing regulation, America's community banks will disappear from many of the communities that need them most." [3]

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[2] Mandated by Congress in the Economic Growth and Regulatory Paperwork Reduction Act of 1996, the EGRPRA project is an overall review of agency rules to identify outdated, unnecessary, or unduly burdensome regulatory requirements.

[3] Statement of John M. Reich, Vice Chairman, Federal Deposit Insurance Corporation on Consideration of Regulatory Reform Proposals before the Committee on Banking, Housing and Urban Affairs, United States Senate, June 22, 2004

ICBA commends the OTS and the other banking agencies for their support of a comprehensive regulatory relief bill in Congress. Agency support for H.R. 3505, the Financial Services Regulatory Relief Act of 2005, introduced by Reps. Jeb Hensarling (R-Texas) and Dennis Moore (D-Kansas) was critical to successful passage of that legislation in the House by an overwhelming margin. Similarly, agency support for the Financial Service Regulatory Relief Act of 2006 (S. 2856) authored by Senator Mike Crapo (R-Idaho) will be critical for the success of that bill in the Senate.

Both bills include provisions from the ICBA-backed Communities Banks Serving Their Communities First Act or "Communities First Act" (H.R. 2061 and S.1568) introduced by Rep. Jim Ryun (R-Kansas) and co-sponsored by more than eighty members of the House, and introduced by Sen. Sam Brownback (R-Kansas) and co-sponsored by four members of the Senate. These provisions include: (1) directing the federal banking agencies to review the call report every five years to delete items that are no longer needed; (2) increasing the asset-size eligibility for an 18-month exam cycle for well-rated, well-capitalized banks from $250 million to $1 billion (S. 2856 would raise eligibility to $500 million); and (3) increasing the $20 million in assets limitation for exemption from the management interlocks restriction (H.R. 3505 would raise it to $100 million, S.2856 would raise it to $50 million).

In addition, H.R. 3505 includes two additional provisions from the Communities First Act: allowing well-managed, well-capitalized banks under $250 million to submit short form quarterly call reports in two out of four quarters each year; and eliminating annual Gramm-Leach-Bliley Act customer privacy notices for banks that have not changed their privacy policies and do not share information with third parties.

ICBA also supports the savings association provisions in the regulatory relief bills (Title II in H.R. 3505 and Title IV in S. 2856). These include (1) updating the statutory limits on the ability of federal savings associations to make small business and other commercial loans, and (2) providing parity for thrifts with banks under the Securities Exchange Act of 1934 and the Investment Advisors Act. All of these provisions would provide thrifts with greater flexibility to promote safety and soundness through diversification, more opportunities to counter the cyclical nature of the mortgage market, and additional resources to manage their operations safely and soundly.

ICBA commends the leadership role taken by the OTS in helping to reduce examination burden under the Community Reinvestment Act rules. Prior to OTS taking action on CRA rules, extended discussions among the agencies about increasing the asset size limit for eligibility for streamlined small bank CRA examinations did not result in consensus. Believing that the increased asset limit would both reduce burden and help thrifts serve their communities, the OTS acted unilaterally in August 2004 to increase the asset limit for the streamlined exam from $250 million to $1 billion. In part due to the OTS's definitive action, the other federal banking agencies were able to reach consensus and also increased the asset limit for a streamlined examination.

In addition, OTS is the only agency that has considered increased flexibility for assessing the CRA compliance of larger institutions with more than $1 billion in assets. Larger thrifts are assessed on a combination of their community lending, services and investments. Generally, a bank's rating is based 50% on lending and 25% each on investments and services. However, in November 2004, the OTS proposed reducing burden by granting larger thrifts the option to realign these weightings to allow them to offers loans, investments and services in a way that best meets the needs of the thrift's community and the thrift's own strategic goals and strengths.

Mutual Holding Companies

Recently, OTS has been asked to opine on and support a proposal to amend the statutory and regulatory requirements applicable to mutual holding companies or MHCs. ICBA understands that a request was made that OTS alter the corporate governance rules for MHCs in order to permit the minority shareholders of a savings association to override the interest of a controlling, majority MHC shareholder. This would provide the minority shareholders in a MHC structure greater control over the underlying depository institution than a majority and controlling MHC, contrary to prevailing law regarding the rights of minority shareholders vis-à-vis majority shareholders in public companies.

ICBA agrees with the OTS that this proposal is inconsistent with U.S. corporate governance standards and would undermine the interests of the underlying institution's depositors who are represented by the majority or the controlling MHC. Furthermore, the proposal poses significant safety and soundness risks in the operation of MHCs, and also risks the retention and future use of the MHC structure. Furthermore, ICBA opposes its inclusion in any of the regulatory relief bills being considered by Congress and commends the OTS for also taking that stand.

In its role as an advocate for all community banks, ICBA promotes mutuality as a viable charter alternative that should be accorded parity in all respects with other charter forms. The banking agencies should not favor one form of ownership—stock or mutual—over another form. The OTS is correct in its position that supporting the minority shareholders in a MHC structure would not only pose safety and soundness risks but would indirectly favor one form of ownership over another. With approximately 340 mutual institutions and 80 MHCs under its supervision, the OTS should maintain its neutrality on this issue. **The mutual charter remains a vigorous, competitive, and innovative option for hundreds of banks in the United States who are very content with their choice of charter and have no desire to change it.**

Credit Union Conversions and the NCUA

ICBA also applauds the OTS for its recent testimony before the House Subcommittee on Financial Institutions concerning credit union conversions and H.R. 3206, Credit Union Charter Choice Act. We agree with the Deputy Director of OTS who testified that it should be the regulator's role to "minimize regulatory

obstacles, reduce burden and facilitate legitimate business decisions regarding charter choice made by the institutions we regulate.” [4]

When it comes to credit union conversions, the National Credit Union Administration (NCUA) has not followed that advice. Instead, the NCUA has attempted to obstruct the right of a credit union to convert to a mutual savings bank rather than supporting the right of a financial institution to choose the type of charter under which it operates.

ICBA believes that the NCUA should follow the lead of the OTS and other banking agencies and cease thwarting credit union conversions. As the Deputy Director of OTS testified, “charter flips” are a normal course of business at the OTS and among the banking agencies.” The ability of financial institutions to choose their charter is one of the key strengths of our nation’s diverse economy. Unlike other countries, we do not have a one-size-fits-all financial system. Our depository institutions have the ability to choose a national or state charter, as well as the ability to choose the type of charter. Each of these charters has their advantages and limitations, though all must meet safety and soundness and consumer protection standards.

We also agree that for the NCUA to require converting credit unions to provide detailed descriptions of potential future business plans serves no meaningful purpose. Requiring detailed information on the downsides of converting and barring any information of the upsides as the NCUA requires with its “boxed” disclosures is misleading to the members of the credit union. The NCUA should revise its conversion regulations so that they are consistent with those of the other banking agencies.

Conclusion

ICBA very much appreciates the opportunity to testify at this oversight hearing regarding the OTS. The OTS is successfully fulfilling its mission as the primary regulator of thrift institutions. Today’s thrift industry is healthier than ever and the OTS has done an excellent job in supervising the industry, including through some troubled times. As long as the institutions the OTS regulates prefer a separate regulator and support the OTS through assessments, the OTS should remain a separate. Having a separate regulator for thrifts can help focus that industry on the nation’s housing market and housing finance, and the OTS has demonstrated that it has the expertise and competence to regulate all aspects of this important industry.

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[4] See the testimony of Scott Polakoff, Deputy Director of OTS, before the House Subcommittee on Financial Institutions and Consumer Credit dated May 11, 2006.