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The Honorable Donald W. Riegle, Chair
Senate Committee on Banking, Housing,
and Urban Affairs
SD-105, Dirksen
Washington, D.C. 20515

Dear Senator Riegle:

As the House and Senate Banking Committees and Congress debate proposed legislation to reform the federal deposit insurance system, the financial industry and the bank regulatory structure, issues are being raised that greatly affect our states. Of greatest concern are issues raised by the Department of Treasury Study, <u>Modernizing the Financial System</u>, now contained within the Treasury Bill, "The Financial Institutions Safety and Consumer Choice Act of 1991," S. 713 and H.R. 1505. Several of these concerns have also been incorporated within other bills being introduced.

DOUGLAS AMENDMENT AND MCFADDEN ACT

The Treasury Bill proposes to repeal the Douglas Amendment to the Bank Holding Company Act, and the McFadden Act, thereby providing full nationwide interstate banking and breaching. The Douglas Amendment provides authority for individual states to set appropriate restrictions or conditions in allowing out-of-state holding companies to acquire banks within their respective state. This should not change. An individual state can best determine its own needs. In fact, all states with the exception of two have already adopted some form of interstate banking. The majority of the states have elected full nationwide banking. Other states currently prefer regional banking arrangements. Montana and Hawaii have not, as of yet, adopted interstate banking and have determined their states' needs are best met by not allowing out-of-state acquisitions. The Douglas Amendment should not be repealed.

Likewise, the McFadden Act should not be repealed. The consequences of a repeal of the McFadden Act include: (1) a substantial reduction in the bank tax bases of approximately 27 states who currently tax income from federal obligations; (2) competitive inequity as large banks will locate in states that do not tax income on federal obligations; (3) a lack of local control by states to ensure community banking needs are being met by an out-of-state bank with only a branch located in their state; and (4) elimination of intrastate branching restrictions still maintained by ten states.

As an alternative to full repeal of the McFadden Act, the "Wilmarth" proposal being advocated by the Conference of State Bank Supervisors will preserve a state's determination of what best meets its needs. The Wilmarth proposal recommends amending the McFadden Act to grant states the authority to permit out-of-state banks to establish branches within their borders. Interstate branching by state or national banks would not be allowed in states that have not passed permissive legislation. Therefore, the proposal allows each state to set appropriate controls, terms and conditions, and to address state taxation issues.

Determination of bank structure has been granted to the individual states pursuant to the Douglas Amendment and McFadden Act. To take away that authority now would be a grave mistake. States must be allowed to continue to address their own interests, including state franchise tax revenues.

TOO-BIG-TO-FAIL

The too-big-to-fail doctrine that has been practiced by the Federal Deposit Insurance Corporation (FDIC) should be eliminated. Unfortunately, it is unlikely the doctrine will be fully eliminated since protection of the very largest banks may be necessary to prevent systemic failures. The problems, therefore, have been of fairness between large and small banks and of who should bear the financial burden of protecting uninsured depositors where the doctrine is used. As long as the too-big-to-fail doctrine is used, deposits will tend to flow from small institutions to the large institutions where depositors know they will be fully protected. If uninsured deposits and creditors are protected, the FDIC Bank Insurance Fund (BIF) should not absorb the financial burden of invoking the too-big-to-fail doctrine. Funding for the doctrine should then come from some other source, such as a standby fund at the Treasury.

DEPOSIT INSURANCE REFORM

Several areas suggested in the Treasury Study for deposit insurance reform are worthy of comment. These include: (1) elimination of insurance on multiple accounts; and (2) assessment of foreign deposits for deposit insurance.

Elimination of Insurance on Multiple Accounts

The elimination of insurance on multiple accounts is related to the too-big-to-fail doctrine. Unless the too-big-to-fail doctrine is satisfactorily addressed, any reduction in insurance coverage on multiple accounts for deposit customers will be an additional catalyst for depositors to move accounts from small to large institutions. Eliminating the insurance on multiple accounts will have little effect upon institutions known to be too large to fail when their depositors and creditors are fully protected.

Assessment of Foreign Deposits

Although there are a number of reasons not to assess foreign deposits for deposit insurance, one strong and compelling reason to do so is fairness. Large institutions with foreign offices have the ability to attract deposits which may comprise a significant portion of their deposit accounts without being assessed a FDIC insurance premium. This has resulted in the inequitable treatment for those institutions that do not have foreign offices as opposed to those institutions which have foreign office deposits that have been protected by the FDIC. Certainly, faced with the problem of determining funding sources for recapitalization of the BIF, the fund can ill afford protecting foreign deposits without the related premium income. If foreign deposits are not assessed insurance premiums, the clear alternative is for the FDIC not to protect them. The Federal Deposit Insurance Act already provides that deposits in foreign branches of U.S. banks are not insured. If the too-big-to-fail doctrine is eliminated, the current inequitable treatment existing between uninsured foreign deposit protection and small institutions is alleviated. Despite the Department of Treasury's recommendation not to assess foreign deposits, the issue is worthy of your Committees' attention.

REGULATORY RESTRUCTURING

The Treasury Bill recommends significant changes to bank regulatory structure. Obviously, any recommendation to remove state's oversight responsibility for state-chartered banks causes great concern. The present duel-chartering system providing for national and state charters has served the country well. States have not abused the powers granted to them, but rather have developed a strong framework enhancing the overall banking system. The individual state must remain the primary supervisor for state-chartered banks.

Thank you for the opportunity to provide comments. I urge careful consideration be given to the implications of reforming the financial system. We must not allow individual states' rights to be compromised in the final legislation.

Note that this has broad bipartisan support; and we believe that most Governors in the United States support this position.

Sincerely,

George A. Sinner
Governor

Tommy G. Thompson
Governor

GAS:dlb