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U P D A T E

News of Developments in the Financial Sector and Related Areas

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New Bank Formations

The Federal Deposit Insurance Corporation ("FDIC") is seeking comment on a new handbook developed to facilitate the process of establishing new banks entitled *Applying for Deposit Insurance – A Handbook for Organizers of De Novo Institutions.* The handbook provides an overview of the business considerations and statutory requirements that de novo organizers will face as they work to establish a new depository institution and apply for deposit insurance. It offers guidance for navigating three phases of establishing an insured institution: pre-filing activities, the application process, and pre-opening activities.

The handbook is the latest in a series of steps that the FDIC has taken to support the establishment of de novo institutions. The goal of the FDIC is to increase transparency about the application approval process and resources available to assist potential organizers. The FDIC developed the handbook as a practical and plain language guide to help organizers navigate the application review process.

The handbook seeks to address the informational needs of organizers, as well as feedback from organizers and other interested parties during recent FDIC outreach events. Future outreach events are planned for Dallas, Chicago, and Kansas City in 2017.

The handbook does not establish new policy or guidance, or modify existing policy or guidance. The handbook, however, provides organizers and the public with transparency and clarity about the FDIC's process for reviewing and approving applications for deposit insurance.

To ensure that the handbook will be useful to organizers, the FDIC is seeking comment on the following questions:

- Does the handbook provide an organizer with sufficient clarity, transparency, and understanding with respect to the requirements, procedures, and processes for establishing an insured depository institution?

- Does the handbook adequately address the requirements, procedures, and processes for establishing an insured depository institution during the primary phases: pre-filing activities, the application process, and pre-opening activities?

- Does the handbook appropriately

address the information needs of organizers who are experienced bankers, as well as the information needs of other organizers, such as certain proposed investors or directors, who may not have experience in banking?

- Is the inclusion of comments from successful bank Chief Executive Officers regarding de novo formation helpful and, if so, should the discussion be expanded?

The 60-day comment period ends on February 20, 2017. Comments should be submitted to handbookcomments@fdic.gov.

A number of articles has been written in recent years regarding the scarcity in the formation of new banks in the United States. A study by the Federal Reserve Bank of Richmond published in 2015 noted that the financial crisis that began in 2007 significantly altered the banking land scape. The study found that from 2007 through 2013 that the number of commercial banks in the United States fell by more than 800 representing a 14 percent decline. The drop was highly concentrated among small community banks with less than $50 million in assets representing a 41% decline.

The study noted that although many banks failed during the financial crisis beginning in 2007 that this decline was driven largely by the lack of new bank formations. The study found that the formation of new banks has fallen sharply since 2010. For instance, in 2012, there were no new banks formed in the United States, and in 2013 there was only one bank formation which was formed to serve the Amish community in Lancaster County, Pennsylvania. From 2011 through 2013, there were only four new banks formed in the United States compared to a yearly average of more than 100 from 2002 through 2008.

Some commentators take the position that the decline in the formation of new banks is due in large part to low bank profitability. An important factor in bank profitability is the net interest margin meaning the spread between deposit rates and lending rates. The Federal Reserve Board's policy of keeping the federal funds rate near zero since 2008 has pushed lending rates down resulting in the net interest margin being relatively low.

Other commentators are of the position that the following the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act compliance costs are a driving force for the lack of new bank formations. Other factors in the lack of new bank formations in the United States include, but are limited to, higher capital requirements, more frequent examinations by bank regulatory agencies and the lengthy application process to form a new bank.

The FDIC published an article in August 2016 entitled *De Novo Banks: Economic Trends and Supervisory Framework*. The article provides an overview of trends in de novo formation, the process by which the FDIC reviews applications for deposit insurance, the supervisory process for de novo institutions, and steps the FDIC is taking to support de novo formations. The information provided in the article reflects the FDIC's ongoing efforts to work with, and provide support to, groups interested in organizing a de novo institution. The article points out that of the more than 1,000 new banks formed between 2000 and 2008, there were 634 were still operating as of September 2015, but also noted that the failure rate of banks established between 2000 and 2008 was more than twice that of small established banks, this being consistent with previous research that found de novo banks to be susceptible to failure under adverse economic conditions. The article concluded by noting that the current economic environment with narrow net interest rate margins and modest overall economic growth remains challenging for the establishment of de novo institutions.

Our firm is experienced and available to answer questions regarding new bank formations and the consolidation of banks.