Remarks by
FDIC Acting Chairman Martin J. Gruenberg
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I want to thank Rob Blackwell and the American Banker for inviting me to take part in this regulatory symposium. The opportunity for an exchange of information and views provided by an event such as this is extremely valuable.

In my remarks today, I will comment briefly on the condition of the banking system and then outline some of the FDIC's priorities going forward.

Condition of the Banking Industry

The FDIC and the banking industry are only now emerging from the most severe financial crisis since the 1930s. The latest data, released by the FDIC in its Quarterly Banking Profile last month, indicate that banks have continued to make gradual but steady progress in recovering from the financial market turmoil and severe recession that unfolded from 2007 through 2009.

The economic recovery, now entering its third year, has been marked by continued distress in real estate markets and a slow, painful process of balance-sheet repair by households, financial institutions, small businesses, and, now, governments at all levels. The result has not only been sub-par growth compared with previous recoveries, but also a persistent uncertainty about the future prospects for the economy, for jobs, and for the banking industry.

All of these trends are, of course, of concern to policymakers and to the public. The FDIC remains alert to these challenges going forward.

There is also positive news in the financial services industry. FDIC data show an overall improvement in the condition of insured financial institutions in the second quarter. Industry earnings have grown over the past eight quarters. The percent of noncurrent loans on the books of FDIC-insured institutions has declined for five consecutive quarters, reflecting improved credit quality. The growth in the problem bank list declined in the second quarter for the first time in nearly five years. The Deposit Insurance Fund returned to positive territory as of June 30. The FDIC is forecasting fewer failing banks this year than last year.

FDIC-insured institutions are generally well positioned to continue working through this difficult episode. Industry capital ratios have been restored to record-high levels. This capital cushion represents not only the wherewithal to absorb additional loan losses, if needed, but also to back new lending as the demand for credit recovers.

However, reductions in loan-loss provisions -- the money banks set aside against expected loan losses -- account for most of the improvement in industry earnings. As the levels of loan-loss provisions approach their historic norms, the prospects of earnings improvement from further reductions diminish. Increased lending will be essential for future revenue growth.

FDIC Priorities

In addition to its basic responsibilities for deposit insurance, bank supervision and bank resolution, the FDIC has three main priorities going forward that I would like to discuss today:

- the implementation of the FDIC's systemic resolution responsibilities under the Dodd-Frank Act;
- the future of community banks; and
- economic inclusion and access to mainstream banking services.

Implementing Systemic Resolution Responsibilities Under the Dodd-Frank Act

The FDIC has been given significant new responsibilities under the Dodd-Frank Act to resolve systemically important financial institutions (SIFIs). Specifically, these include an Orderly Liquidation Authority to resolve bank holding companies and non-bank financial institutions, if necessary, and a requirement for resolution plans that will give regulators additional tools with which to manage the failure of large, complex enterprises.

The FDIC has taken a number of steps over the past year to carry out these responsibilities.

First, the FDIC established a new Office of Complex Financial Institutions to carry out three core functions:

- monitor risk within and across these large, complex firms from the standpoint of resolution;
- conduct resolution planning and the development of strategies to respond to potential crisis situations; and
- coordinate with regulators overseas regarding the significant challenges associated with cross-border resolution.

For the past year, this office has been developing its own resolution plans in order to be ready to resolve a failing systemic financial company. These internal FDIC resolution

plans -- developed pursuant to the Orderly Liquidation Authority, provided under Title II of Dodd-Frank -- apply many of the same powers that the FDIC has long used to manage failed-bank receiverships to a failing systemically important financial institution. If the FDIC is appointed as receiver of such an institution, it will be required to carry out an orderly liquidation in a manner that maximizes the value of the company's assets and ensures that creditors and shareholders appropriately bear any losses. The goal is to close the institution without putting the financial system at risk.

This internal resolution planning work is the foundation of the FDIC's implementation of its new responsibilities under Dodd-Frank.

In addition, the FDIC has largely completed the related rulemaking necessary to carry out its responsibilities under Dodd-Frank.

In July, the FDIC Board approved a final rule implementing the Orderly Liquidation Authority. This rulemaking addressed, among other things, the treatment of similarly situated creditors, protection for employees of covered financial companies that continue to work for the company following failure, and protection for policyholders of insurance companies under the orderly liquidation process.

Last week, the FDIC Board adopted two rules regarding resolution plans that systemically important financial institutions themselves will be required to prepare – the so-called "living wills."

The first resolution plan rule, jointly issued with the Federal Reserve, implements the requirements of Section 165(d) of the Dodd-Frank Act. This section requires bank holding companies with total consolidated assets of $50 billion or more and certain nonbank financial companies that the Financial Stability Oversight Council designates as systemic, to develop, maintain and periodically submit resolution plans to regulators. The plans will detail how the top-tier legal entity in the enterprise – as well as any subsidiary that conducts core business lines or critical operations – would be resolved under the U.S. Bankruptcy Code.

Complementing this joint rulemaking, the FDIC also issued an Interim Final Rule requiring any FDIC-insured depository institution with assets over $50 billion to develop, maintain and periodically submit plans outlining how the FDIC would resolve it through the FDIC's traditional resolution powers under the Federal Deposit Insurance Act.

These two resolution plan rulemakings are designed to work in tandem and complement each other by covering the full range of business lines, legal entities and capital-structure combinations within a large financial firm. Both of these resolution plan requirements will improve efficiencies, risk management and contingency planning at the institutions themselves. They will supplement the FDIC's own resolution planning work with information that would help facilitate an orderly resolution in the event of failure.

We expect that the process of developing these plans – or "living wills" -- will be a dialogue between the regulators and the firm. It is not a simple "check-the-box" exercise, and it must take into account each firm's unique characteristics. The planning process must also be iterative, especially for the largest and most complicated firms.

Together, these efforts will ensure comprehensive and coordinated resolution planning for both the insured depository and its holding company and affiliates in the event that an orderly liquidation is required.

The Future of Community Banks

The FDIC is the primary federal supervisor for the majority of community banks in the United States. These institutions, with assets under $1 billion, comprise nearly 7,000 of the approximately 7,500 insured financial institutions in the country.

In the aftermath of the recent crisis, considerable concern has been expressed about the future of community banks.

It is important to recognize that community banks play a critical role not only in the financial system, but also in the U.S. economy as a whole. While community banks with assets under $1 billion represent less than 11 percent of banking assets, they provide nearly 40 percent of the loans the banking industry makes to small businesses, extending credit that is crucial to job creation. Throughout the crisis and ensuing recession, we saw community banks maintain and even modestly grow their loan balances.

At the same time, the financial crisis and ensuing recession have taken a serious toll on community banks. Of the 395 FDIC-insured institutions that have failed during the crisis, more than 300 have been community banks. Still, the large majority have come through this crisis in good shape. They remain viable and provide a wide range of critical services for their communities. As such, they have a unique role to play in our financial system.

The FDIC is going to undertake a number of initiatives to further our understanding of the challenges and opportunities for community banks going forward. We plan to hold a conference early next year on the future of community banking. We have asked our research division to trace the evolution of community banks over the past 20 years, including changes in business models and cost structures, and suggest lessons to be learned. The FDIC is also reviewing key challenges facing community banks such as raising capital, keeping up with technology, attracting qualified personnel, and meeting regulatory obligations.

Additionally, we are looking at our own risk-management and compliance supervision practices to see if there are ways to make the process more efficient.

Importantly, we will continue to have direct outreach and an open dialogue with community bankers. I plan to hold a series of regional roundtables with community bankers across the country to get their input. This dialogue will continue to include our Advisory Committee on Community Banking, a forum where we hear firsthand from a broad cross-section of community bankers about both the challenges and the opportunities they see in their markets, as well as some of the concerns they have about the regulatory environment.

This overall effort in regard to community banks will be a major priority for the FDIC over the coming year.

Economic Inclusion and Access to Mainstream Banking Services

The core responsibilities of the FDIC in regard to deposit insurance and the supervision of community banks relate directly to the third priority I want to discuss – expanding access to insured financial institutions to all Americans.

Deposit insurance is essentially about making people feel secure putting their money into financial institutions. In many parts of the country, both urban and rural, a community bank may be the only source of mainstream financial services. However, accessing such services has proven elusive for millions of people in our country.

In 2009, pursuant to a statutory provision, the FDIC partnered with the Census Bureau to conduct the first national survey ever undertaken of who is unbanked and underbanked in the United States. It found that 7 percent of U.S. households do not have bank accounts, and that another nearly 18 percent who may have an account still utilize non-bank financial services such as check cashers and payday lenders, which are frequently more expensive. Taken together, this means that nearly a quarter of American households are underserved by the mainstream banking system, and the proportions are significantly higher for low-income and minority populations. The Census Bureau will now conduct this survey on behalf of the FDIC every two years. The second survey was conducted a few months ago, and we plan to release the findings next year.

In response to this issue, the FDIC has undertaken initiatives at both the local and national level.

At the local level, the FDIC's Alliance for Economic Inclusion (AEI) has organized coalitions of financial institutions, community organizations, local government officials, and other partners in communities across the country to bring unbanked and underserved households into the financial mainstream by expanding access to basic retail financial services, including savings accounts, affordable remittance products, small-dollar loan programs, targeted financial education programs, and asset-building programs. These partnerships are currently operating in 14 communities nationwide, and the FDIC plans to expand the program in the coming months.

At the national policy level, the FDIC's Advisory Committee on Economic Inclusion – composed of bankers, community and consumer organizations, and academics – also explores ways to bring the unbanked into the financial mainstream. The Committee has pursued a number of initiatives since it was formed in 2007. One of the initial projects it recommended – the Small-Dollar Loan Pilot Program – demonstrated that banks can offer safe, affordable small-dollar loans as an alternative to high-priced sources of emergency credit, such as payday loans or fee-based overdrafts.

The Advisory Committee is now undertaking a pilot program called Model Safe Accounts to evaluate how banks can offer safe, low-cost transactional and savings accounts that are responsive to the needs of underserved consumers. Participating banks are in the process of testing the model accounts, which feature electronic debit-card based accounts with low fees and low minimum balance requirements. We are hopeful that the results of the testing will encourage more banks to offer such products.

The Advisory Committee will meet again later this year. A focus of the Committee and the FDIC going forward will be the potential role that technology and innovation can play in expanding access to mainstream financial services.

Conclusion

In conclusion, I would note that these are challenging times for the FDIC and the banking system. There are, of course, many other issues that will occupy our attention. The three I discussed today, however, go directly to our core mission and will be a particular focus of attention.

Thank you.

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