Remarks of John M. Reich, Director
Office of Thrift Supervision
to the Florida Bankers Association's Regulator Town Hall Meeting
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Good morning, and thank you for inviting me to join you in beautiful Tampa, Florida. I particularly want to thank my good friend, Alex Sanchez, for the invitation to be here today.

We are not far today from where I spent a significant portion of my career as a community banker – in Sarasota, and prior to that in Fort Myers, Florida. I look back on those years with many great memories.

My experience as a community banker was tremendously fulfilling from both a professional and personal standpoint. Community banking is a career choice in which you become what you do. It is as much a lifestyle choice as a career choice. As community bankers, you are typically among the most involved citizens in your communities. You know your customers and, through them, you know your communities.

You know many of your customers personally. You know their families, their challenges, their activities, and the organizations they belong to. You live with them. You know what is important to them at the most basic level – the price of milk, the cost of gasoline, the cost of a lot on which to build a home, who the best builders are in your community, the best doctors, lawyers, CPAs, schools and schoolteachers, the best service clubs.

Many of you are members of Kiwanis, Lions, Rotary, Civitan, Optimists, or various other local service and community clubs. When I was a community banker, I was involved with several of these community-based organizations, first in Champaign-Urbana, Illinois, where I began my career, and later in Fort Myers and Sarasota, Florida, for over 20 years.

As a community banker, I served as Treasurer of a Boy Scout Council, Chairman of a public hospital board, and Chairman of a YMCA Board. I was also active in the United Way, served on the Board of a Drug Abuse Program for teenagers, a Symphony Orchestra Board, and a Little League Baseball Board. For 7 years, I was the coach of a Babe Ruth Baseball team for 13 year olds while I was the CEO of my bank in Sarasota.

And I know that most of you have very similar credentials. I believe I understand the pressures under which you live and work every day of the week. Community banking is about service, belonging, and doing something to make a difference in people's lives. What you and your banks do in your communities matters, perhaps more than you realize.

Community banking matters because of the opportunities you have every day to make a personal and significant difference in the lives of your customers, their families, and your community.

One of my top priorities as Director of the OTS is to preserve and promote community banking across this country. While it has a national and statewide voice in organizations such as the Florida Bankers Association, community banking is an industry that is distinctly local.

You have had great opportunity and experience for many years here in Florida to witness community banks selling out to larger regional and national banking organizations that often seem to establish little presence in local communities beyond their branch offices. This is not the case for all larger institutions, but it is a perception backed by the experiences in many communities.

Mergers and acquisitions involving community banks are typically motivated by real market pressures, including regulatory burden and unfair competition that is squeezing community banks. Among the issues that we in Washington need to address is unfair competition for deposits and loans in local markets from organizations that have artificial, government-sponsored economic advantages, including credit unions and the Farm Credit Administration. These unfair public policies ought to be changed. My colleagues and I at the OTS are sensitive to these issues and will continue to work to reduce unfair competition and regulatory burden on community banks.

Of course, you community bank CEOs can do your part to protect and preserve community banking. In your own institution this includes providing greater assurance for the future of community banking in your community by planning for succession and continuity of management when you are ready to retire. If you have not already done so, I encourage you and your Board members to address this issue. My fear is that the exit plan for many community bank CEOs is simply to sell out. Most of your customers, I believe I can say with a high degree of confidence, believe this is rarely a desirable outcome for your community and your customers you now serve.

I would like to move now to share with you the observations of a former community banker on the thrift charter, and then some current issues with subprime lending. I will conclude my remarks with an issue of critical importance to you and virtually all of the communities you serve in Florida and the Gulf Coast states – hazard insurance.

The Thrift Charter

The OTS and the charter we oversee have unique and inherent strengths that, I believe, continue to reap rewards for the industry we regulate. Since I joined the agency less than two years ago we have increased our overall staff by more than 15 percent. By September 30, 2007, we will have a professional staff of just over 1,000 people who are dedicated to the mission of maintaining the safety and soundness of the thrift industry, and improving our application processing, and the regulation, oversight and flexibility of the charter.

We have a skilled staff with experience in virtually every sector of banking. With the addition of 100 new examiners – 60 last year and approximately 40 this year - and additional training and hiring in certain critical areas, including capital markets, economic analysis, and compliance management, we are further improving and upgrading our supervisory structure to make it more effective and efficient.

Our priorities include greater emphasis on outreach and visibility for the OTS at state and national conferences and conventions, such as yours. As the retail community banking sector grows, I believe the thrift charter is well positioned to provide a structural and regulatory alternative both to established financial services businesses and to new entrants that are working to grow market share in this area. The combination of nationwide branching, strong preemption authority, and seamless consolidated supervision in a holding company / subsidiary banking structure, ensures savings institutions are able to follow their customer base and the growth of their business from one end of the country to the other – all with minimal regulatory burden.

Currently, there are 845 OTS-regulated thrifts, holding assets of $1.4 trillion. We also oversee 475 thrift holding company structures with consolidated assets of approximately $8.0 trillion. While financial services consolidation has reduced the overall number of savings institutions, industry asset growth remains strong. In fact, in the past five years, industry assets grew 53.4 percent, representing a healthy average annual growth rate of 7 percent, due to growth within existing thrifts and the fact that various financial institutions continue to choose the thrift charter for the reasons I just mentioned.

The thrift charter is deployed in neighborhood community banks all across America. It is used by leading nationwide lenders, by investment banks offering a full array of financial services, and by global conglomerates involved in a wide array of diverse businesses – to name just a few. These organizations have all come to the thrift charter at different times and for reasons as diverse as their underlying businesses and the markets they serve. And the facts seem to show that it has been a profitable decision.

The more I learn and the more I know about the institutions we regulate, the more I am convinced the charter is a unique and outstanding structure for conducting community-based retail banking activities offering sound opportunities for community banks. I note no small irony in the fact that, after many years as a community commercial banker, I now understand that there is an alternative model for community retail banking that may be – depending on the institution – preferable from a business standpoint. The thrift charter offers a viable business model for *de novo* institutions, and a number of groups in the process of organizing new banks are giving it consideration, as well as the fact that some existing institutions have chosen to convert to the thrift charter.

Current Issues with Subprime Lending

I am certain you are all aware of the fact that subprime lending has risen to the top of the issues of concern in Washington, D.C., to Congress, the regulators, and more recently, the Treasury Department.

Sometimes people confuse subprime lending with predatory lending. There are a number of options available for addressing these issues. In considering options to curb predatory lending, the issue always comes down to enforceability. By contrast, solutions to address troubled subprime loans require the participation of mortgage bankers, servicers and investors in connection with foreclosure avoidance. It is challenging to figure out what we can do to make this happen and, more importantly, how much should we really be doing – or not doing – to assist or avoid interfering in this process.

Clearly, some of the numbers regarding existing problems in the subprime and Alt-A markets are daunting. By some estimates, more than 20 percent of the $567 billion of subprime hybrid mortgages that are scheduled to reset this year will involve a serious delinquency that could lead to foreclosure. There have been many high level meetings the past several months among regulators, industry participants, legislators and administration officials about how to address this problem and the potential fallout on the mortgage markets. Generally, the consistent theme that has come out of all of these discussions is that a foreclosure is in no one's interest. Rather, all agree that we collectively need to identify solutions and options to avoid, whenever possible, foreclosing on borrowers who are struggling to stay in their homes.

I intend to work with our regulated institutions to provide the supervisory flexibility and regulatory encouragement to address problems in the subprime market. However, as I and my colleagues at the other federal banking agencies have noted, the bulk of the problem lies outside insured institutions. While federal standards and guidelines may be helpful, we need the structure or process to ensure the net we cast includes all participants in the mortgage process.

The intersection of preserving sound subprime lending and shutting down predatory lending abuses in the subprime markets is particularly troubling. It goes to the very heart of affordable housing. We need to weed out predatory lending, and particularly the potentially predatory features of certain lending products in the subprime market, without cutting off the availability of credit to subprime borrowers.

We also need to address the problem of key participants in the mortgage process escaping accountability. One obvious solution is imposing regulation where it is needed; but it is equally important not to interfere when market solutions can be more effective and efficient – and without imposing regulatory burdens that run counter to the efficient allocation of credit in the housing markets. Again, too much government can create inefficiencies that run counter to the best interests of the mortgage market, including the subprime market. It can also shut down credit. We have witnessed this phenomenon several times within the last several decades.

As you aware, the federal banking agencies issued proposed guidance on subprime lending. The comment period for that proposal closed a few days ago, on May 7. I hope you had an opportunity to share your thoughts with us on the proposal, particularly with respect to your views on the appropriate underwriting standards that should apply in the subprime markets.

An area of particular interest to me is the application of subprime lending standards to state-licensed mortgage brokers and other state-regulated and/or unregulated mortgage bankers and lenders. It is estimated that 70 to 80 percent of subprime loans are originated through mortgage brokers. Thus, oversight of this segment of the mortgage pipeline is critical to the success of preserving and promoting sound subprime underwriting and lending activities.

Unfortunately, there are wide variations in estimating the number of <u>licensed</u> mortgage brokers in the U.S. The scope of regulation, oversight, and supervision of mortgage bankers and lenders in various states is also uncertain. While some states license mortgage brokers with respect to the activities involved in originating a loan, the entity that funds the loan, i.e., a mortgage banker or lender, may not be regulated.

I understand that the Conference of State Banking Supervisors (CSBS) and the American Association of Residential Mortgage Regulators (AARMR) are currently coordinating on a nationwide residential mortgage licensing program to address part of the problem with state mortgage brokers and bankers. However, this is only part of what is required to address the existing problem with the activities of state regulated mortgage brokers and lenders. More rigorous oversight and enforcement of the mortgage origination process may be the best prescription for addressing predatory lending abuses and poor underwriting practices that have created problems in the subprime market.

The OTS will continue to be an active participant in many aspects of subprime mortgage market issues as they unfold over the next several months. We are partnering with community groups and industry participants on a host of housing-related issues involving affordable housing and addressing predatory lending. We will continue to explore the appropriate use of various industry, community and regulatory forums to increase awareness and discuss solutions for the subprime market and address predatory lending abuses.

The Availability of Homeowner's Insurance

Lending institutions and their customers in Florida and other Gulf Coast states are confronting significant obstacles in obtaining affordable homeowner's insurance. As a result of the many hurricanes and the significant damage they caused, adjustments in the offering and underwriting of homeowner's insurance have the potential to disrupt the lending business in these states. In Florida, there are 37 OTS-regulated thrifts that rely to a significant extent on real estate collateral.

The issue of affordable homeowner's insurance includes a number of problems that manifest themselves in various ways. For instance, homeowners and business owners in coastal areas often cannot find affordable hazard and windstorm insurance. When they find affordable insurance coverage, they often find that the insurance is offered by lesser-rated or unrated companies, and that deductibles are high and coverage is reduced. When disasters hit, they also find there may be questions as to whether damage was caused by wind or water, and hence whether they had adequate coverage for both hazard and windstorm damage.

Financial institutions are concerned about the adequacy of insurance coverage of their residential and commercial loan customers' collateral properties. They also worry whether borrowers can afford heightened escrow payments to cover the cost of insurance, and they worry whether their customers can afford to rebuild given the immediate and potential long-term costs of doing so. Institutions also worry about having to force place insurance coverage for their customers who cannot afford insurance, or who rely on the institution to provide force placed coverage when they cannot find it themselves. Institutions sometimes even have to scramble to find insurance coverage on their own offices.

Coastal state insurance regulators are working hard to have affordable insurance coverage available in their states. State insurance regulators are encouraging well capitalized insurance companies to continue offering insurance in the states, but there are serious issues with exposure to coastal areas. Potential insurance payouts from a direct hit by a significant hurricane are further exacerbated by coastal property values that have mushroomed. Not only have the number of people moving to the coast skyrocketed, but the square footage of residences has ballooned, and the density of waterfront living has jumped due to the prevalence of multi-story condominiums. Reinsurance costs have also exploded since the 2004 and 2005 hurricanes that hit the southeast and gulf states. Some reinsurers stopped offering coverage in the most exposed states.

But you already know all these things. In fact, the Florida Bankers Association was perhaps the first banking trade group in the country that proactively addressed the hazard insurance problem. Your 45-member Property Insurance Task Force did groundbreaking work in responding to the region's insurance challenges. In addition to holding a summit on these issues last fall, you adopted a detailed 11-point insurance agenda that you issued on September 28, 2006, and also forwarded to Governor Bush.

Your agenda addresses important insurance issues facing Florida, such as bringing in new insurance carriers, the lack of hurricane mitigation on older homes, the Florida Building Code, and state catastrophic fund reinsurance programs. It is my understanding that thrifts have been prominent in attempting to deal with these issues. Your FBA chair, Gwynn Cochran Virostec, a WAMU executive, has provided leadership in raising insurance issues with legislators and other parties. And thrift executives serve on the insurance committee responsible for your hazard insurance agenda.

Thrift executives in various Gulf Coast states continue to offer advice and counsel to legislators and others as they deal with the daunting issues raised by the escalating cost, affordability and/or unavailability of hazard insurance coverage. We are monitoring our affected institutions, and attending meetings with insurance commissioners and other regulators on the subject. While a number of avenues are being explored, and remedies are being put into place or considered, there is still a lot of hope pinned on 2007 being like 2006, which was relatively free of major hurricanes. However, I think we all recognize that this is not a good approach.

I share your concern about the stress these problems are causing to the banking industry, the region's economy and its people. At the OTS, we would like to be part of the solution. It is with this backdrop that I am announcing today that the OTS will be sponsoring our second national housing forum this fall, which will include two very important aspects of the fallout of natural disasters – future hazard insurance coverage and recovering and restoring affordable housing to disaster affected communities. I hope all of you will be able to attend or listen in on this important event.

Conclusion

Thank you for the opportunity to meet with you this morning. The Florida Bankers Association is one of the premier banking advocacy voices in the U.S., at both the state and federal level. It is always a pleasure to be here. I am happy to answer your questions as time permits.