United States General Accounting Office

GAO

Report to Congressional Committees

March 1997

BANK DATA

Material Loss of Oversight Information From Interstate Banking Is Unlikely

GAO/GGD-97-49

GAO

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General Government Division

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March 26, 1997

The Honorable Alfonse M. D'Amato
Chairman
The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking, Housing, and
Urban Affairs
United States Senate

The Honorable James Leach
Chairman
The Honorable Henry B. Gonzalez
Ranking Minority Member
Committee on Banking and Financial Services
House of Representatives

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal) authorizes interstate mergers between banks beginning June 1, 1997, regardless of whether the transaction would be prohibited by state law.[1] In addition, Riegle-Neal also provided that banks may branch across state lines if the host state has a law permitting the establishment or acquisition of branches by out-of-state banks. Interstate mergers between banks and the establishment of interstate branches are allowed before June 1, 1997, in states having laws that expressly allow such mergers. Previously, most banks that wanted to operate across state lines had to establish a bank holding company (BHC) and, with certain restrictions, acquire or charter a bank in each state in which they wanted to operate. With the advent of interstate branching, (1) banks that previously could not expand across state lines may do so and (2) some multistate BHCs may combine their operations into single banks with multistate branches.

When Congress passed Riegle-Neal, there was a concern that information regarding the distribution of bank deposits and loans by state would be lost. As a result, Congress mandated that we determine whether implementation of the act would result in a material loss of information that is important for federal bank regulation and oversight. Specifically, and in accordance with our responsibilities under section 112 of the act, our objectives in preparing this report were to (1) examine how the interstate branching provisions of Riegle-Neal are likely to affect the

[1]Riegle-Neal gives states the right to opt out of this arrangement if they pass legislation prohibiting merger transactions with out-of-state banks before June 1, 1997.

usefulness of the deposit and loan data collected and reported to federal regulators by the banking industry under statutory and regulatory requirements and (2) determine whether modifications to such data requirements would help to ensure that the implementation of the act's interstate branching provisions does not result in a material loss of information important to regulatory and congressional oversight of banks. Our analysis was limited to identifying information reported to regulators that would potentially be lost as a result of the implementation of Riegle-Neal.

Background

Oversight of federally insured state-chartered banks is provided by state bank regulators and either the Federal Reserve System—for banks that are members of the Federal Reserve—or the Federal Deposit Insurance Corporation (FDIC)—for other state-chartered banks. National bank oversight is provided by the Office of the Comptroller of the Currency (OCC). As the deposit insurer, FDIC has back-up oversight authority for all FDIC-insured banks. This authority allows FDIC to examine potentially troubled institutions and take enforcement actions, even when it is not the institution's primary regulator. In addition to its authority over state-chartered member banks, the Federal Reserve oversees all BHCs.

In accordance with a variety of federal laws and regulations, banks routinely provide federal bank regulators with reports containing information about their deposit and lending activities. These reports include the following:

- a quarterly financial report (call report), which is submitted to the primary federal bank regulator;
- an annual independent audit report (for banks with $500 million or more in assets), which is submitted to FDIC and relevant federal and state bank regulators;
- an annual summary of deposits report for each branch, which is submitted to FDIC;
- a statement of amounts required to be held as reserves, which is submitted to the Federal Reserve; and
- an annual report on home mortgage lending (for banks that originate, purchase, or receive applications for home purchase and home improvement loans and that have assets greater than $28 million in 1997), which is submitted to the bank's primary federal regulator.

In addition, as of January 1997, revisions to the Community Reinvestment Act (CRA)[2] interagency regulations require banks that have assets of $250 million or more, or banks that are affiliates of a BHC with assets of $1 billion or more, to report to their regulators some new data. These banks are required to annually report, by geographic location, the aggregate number and aggregate amount of small business and small farm lending loans originated or purchased, and the aggregate number and aggregate amount of community development loans originated or purchased. BHCs are also required to submit to the Federal Reserve quarterly financial reports (Y-9 reports) on the consolidated activities of their bank and nonbank subsidiaries.

Federal bank regulators, along with other agencies, typically use the lending and deposit information gathered in these reports and special purpose reviews to carry out their oversight responsibilities. Congress gets information through a variety of means, including directly from bank regulators and also from the legislative support agencies including us, the Congressional Research Service (CRS), and the Congressional Budget Office (CBO). These support agencies, in turn, use the information gathered in these banking reports, along with other sources, to do various analyses for Congress.

Parties other than federal regulators, such as industry analysts and community organizations, may also use call reports and Y-9 reports (both of which are publicly available) to produce state, regional, and national summaries of the types and overall dollar amounts of loans and deposits held by banks and BHCs. These parties also frequently use home mortgage-related lending reports to assess the availability of credit to various groups within a geographical area, such as a state. Because a state was the largest area within which a bank could expand, information collected at the bank level has been used by such parties to approximate bank loan and deposit activity within a state.

Results in Brief

To the extent that interstate branching becomes prevalent, call report data—as currently collected and reported—will become less useful for approximating bank loan and deposit activity within a state. As BHCs consolidate by merging multistate banking operations and as banks

[2]CRA requires each federal bank or thrift regulator to (1) assess an institution's record of helping to meet the credit needs in all areas of the community that the institution is chartered to serve, which is consistent with safe and sound operation of the institution, and (2) take this record into account in the agency's evaluation of an application for a deposit facility by the institution.

expand across state lines by opening or acquiring branches, call report information reported at the bank level will increasingly encompass the loans and deposits from more than one state. However, accurately measuring loan and deposit activity by state was subject to limitations even before Riegle-Neal. BHCs had already begun establishing interstate operations and creating regional booking centers for some of their activities and national markets have developed for certain bank products.

Compared with the information that existed before it was enacted, the implementation of Riegle-Neal is unlikely to result in a material loss of information necessary to perform regulatory and congressional oversight for three reasons. First, as previously mentioned, the usefulness of call report data to approximate bank loan or deposit activities within a state was already somewhat limited and has become increasingly so, but only in part due to Riegle-Neal. Second, sources of information collected at the branch level or by geographic location should not be affected by interstate branching. For example, summary of deposits data should still be available to measure deposit activities that are booked in a particular state, although these data will not provide information on the geographic source of those deposits. Also, home mortgage loan data should be available as an indicator of mortgage loan activity in a geographic area. Finally, the most useful and detailed information about bank activities is attained through examinations. Regulators with primary supervisory responsibility still have this tool available, although those who rely solely on off-site information will not. For these reasons, at this time, there does not appear to be sufficient need to modify regulatory or statutory reporting requirements.

Objectives, Scope, and Methodology

To determine what information regulators collect from banks, we reviewed the laws and regulations pertaining to the requirements for banks and BHCs to report data on bank activities (focusing on loans and deposits).[3] These laws and regulations consisted primarily of those authorizing federal bank regulators to conduct examinations, collect financial statement data, collect bank deposit information, and encourage banks to provide credit to the communities in which they operate. In addition, we obtained regulators' and others' views about whether interstate branching would pose new or different needs for information. We concentrated our review on information that is currently collected from banks and BHCs. We did not conduct an independent analysis to

[3]We limited our scope to banks since federally chartered thrifts were allowed to branch across state lines before Riegle-Neal was passed. However, the issues cited in this report, with respect to the usefulness of bank loan and deposit data, would also apply to thrifts.

identify all of the information that regulators and Congress may need to execute their regulatory and oversight responsibilities.

To obtain views on the effect that Riegle-Neal is likely to have on the usefulness of reported loan and deposit data, we held discussions with staff members at the Board of Governors of the Federal Reserve System, the Federal Reserve Bank of Dallas, and headquarters and field offices of FDIC and OCC. We also spoke with staff members at CBO and CRS in their roles as users of data for congressional oversight. In addition, we interviewed representatives of several community organizations (the National Community Reinvestment Coalition, the Center for Community Change, and the Association of Community Organizations for Reform Now). We did not attempt to identify all users of reported loan and deposit data.

To determine whether there would likely be a material loss of information important to regulatory and congressional oversight of banks, we reviewed call, Y-9, Summary of Deposit, Home Mortgage Disclosure Act (HMDA) loan application register, and required reserve reports collected by the regulators pursuant to laws and regulations. We also reviewed the loan and deposit data the regulators make available to us as the investigative arm of Congress. We then reviewed in greater detail the loan and deposit information that regulators summarized by state, region, and nationwide.

We conducted our work between March 1994 and November 1996 in Dallas and Washington, D.C. We provided a draft of this report to the heads of the Federal Reserve, FDIC, and OCC for their review and comment. We also provided the community organizations and other parties we contacted with the opportunity to comment on portions of the draft report that we attributed to them. The comments we received are discussed and evaluated on pages 12 to 14, and the written comments are reprinted in appendixes I and II. Our work was done in accordance with generally accepted government auditing standards.

Call Report Data May Become Less Useful for Approximating Bank Activities by State

Regulators collect a variety of information about bank loan and deposit activities through reports filed by banks and BHCs. These reporting requirements were not affected by Riegle-Neal. In table 1, we briefly describe the loan reports and the information collected from them. Call reports and Y-9 reports are the primary sources of data that banks and BHCs provide to regulators. Both reports contain a summary of the entity's loan portfolio categorized by type of loan (e.g., real estate or consumer). The HMDA loan application register[4] and the new CRA report on small business and small farm lending are to collect data, by geographic location, on specific categories of bank loans to assist the regulators in enforcing the federal fair lending laws. Unlike data from call reports and Y-9 reports, data from these reports are collected to assess a bank's compliance with federal fair lending laws and to assess the bank's performance in meeting the credit needs of its local community. In addition, the HMDA data are submitted only by banks engaged in originating home mortgage loans; banks that merely purchase loans are not required to submit HMDA data.

Table 1: Reports Containing Information on Bank Loans

Report	Loan information	Reporting level	Recipient	Frequency
Call report	Amounts by type of loan	Bank	Federal bank regulators	Quarterly
Y-9 report	Aggregate amounts of all banks in the BHC, by type of loan and income of applicant	BHC	Federal Reserve	Quarterly
HMDA loan application register	Race, ethnicity, gender, and geographic location of collateral for home mortgage-related loan and type of loan action	Banks with assets greater than approximately $28 million in 1997 that originate, purchase, or receive applications for home purchase and home improvement loans each calendar year, and that had an office within a standard metropolitan statistical area	Federal bank regulators	Annually
CRA report (effective January 1, 1997)	Geographic location, the aggregate number and aggregate amount of small business and small farm loans originated and purchased and the aggregate number and amount of community development loans	Banks with assets of $250 million or more or banks that are affiliated with a BHC whose total assets exceed $1 billion	Federal bank regulators	Annually

Source: GAO analysis of bank reports to and reporting requirements of bank regulators.

[4]The HMDA loan application register is the vehicle for collecting data on home mortgage lending as required by HMDA.

In table 2, we describe the reports that banks and BHCs use to provide regulators with information about their deposits. Call reports again provide the greatest detail about a bank's total deposits because they provide a summary of a bank's total deposits by type (e.g., demand deposits). The Summary of Deposits report provides the most comprehensive information on bank deposits by location, but only provides information on the total bank deposits based on the branch in which the account is located. Additionally, these data are only collected yearly. The Required Reserve report provides more limited information on bank deposits.

Table 2: Reports Containing Information on Bank Deposits

Report	Deposit information	Level of reporting	Recipient	Frequency
Call report	Amounts by type of deposit	Bank	Federal bank regulators	Quarterly
Y-9 report	Aggregate amounts of all banks in the BHC, by type of deposit	BHC	Federal Reserve	Quarterly
Summary of Deposits report	Amounts held in each insured office of a bank	Branch	FDIC	Annually
Required Reserve report	Reserves held by banks as a result of reserve requirements on deposits	Bank	Federal Reserve	Weekly or quarterly, depending on bank size

Source: GAO analysis of bank reports to and reporting requirements of bank regulators.

Data From Call and Y-9 Reports Have Historically Had Limited Usefulness in Determining State Banking Activity

Although regulators and other interested parties have used call report data to produce state, regional, and national summaries of the types and overall dollar amounts of loans and deposits held by banks, the data reported have always had limitations in their ability to provide information about the geographical location of banking activity. In measuring loan activity, limitations have existed because the data used to compile call reports do not explicitly identify the geographic location of the borrower or the project being funded. As a result, questions exist as to how appropriate it has ever been to assume that the loans held by a bank were made (1) by a banking entity located in the same state in which the bank reporting the loan was chartered or (2) to a party living or doing business in the state where the bank reporting the loan was chartered. These limitations could become more apparent and more widespread once Riegle-Neal is implemented, since the activities reported by banks with interstate operations will clearly include activities in a number of states.

According to regulatory officials, loan data reported in the call reports and Y-9 reports do not represent total bank lending in a particular state or region for the following reasons:

- A significant percentage of a bank's mortgage loans are sold in secondary markets through such entities as the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac).
- Banks sometime transfer all, or a portion, of a loan to an affiliated bank or sell loans to unaffiliated banks. Banks make such transfers to diversify portfolios and to ensure compliance with legal lending limits. In addition, some BHCs have their bank subsidiaries transfer all loans of a certain type to one bank to better serve customers and reduce operating expenses.
- Banks that serve a multistate market (e.g., the metropolitan area of Washington, D.C.) may directly lend to out-of-state customers.

Therefore, if a study were trying to determine the amount of loans made by banks to borrowers in a state or region, call report data alone, at least as currently collected and reported, could not answer the question. Researchers interested in studying the geographic distribution of loans noted such limitations before Riegle-Neal was considered. For such studies, data from the HMDA loan application register, and presumably the data to be collected on small business and small farm loans, may be more useful since they provide specific geographic information on borrowers. However, similar geographic information on a bank's entire loan portfolio is not available from these sources.

Call report data on deposits do not identify the location of a bank's depositors, much as the loan data does not identify the location of a bank's borrowers. The Required Reserve report serves a specific bank oversight function, as previously described, and is not suited to providing detailed information about the types of deposits or the location of depositors. The most detailed information on the location of depositors is provided by the Summary of Deposits report. This report is the only one that identifies a bank's deposits by branch. However, regulators pointed out that even the Summary of Deposits report contains inherent limitations regarding the origin of a bank's deposits. For example, banks may purchase deposits in the national market; in this case, the reporting branch need not reflect either the depositor's home or business location. Therefore, while a state-by-state analysis of a bank's Summary of Deposits report identifies where deposits exist, it does not necessarily identify the location of the depositor and, thus, the location from which the funds come. In addition, unlike call report data, which are collected quarterly, the data in the Summary of Deposits report are collected yearly.

Interstate Branching Could Increase the Number of Banks Reporting Data From Activities in More Than One State

To the extent that interstate branching becomes prevalent, the usefulness of information reported to bank regulators, which is currently used to compile banking data on a state-by-state basis, would become even more problematic. If BHCs consolidate their operations by merging multistate banking operations or if banks expand across state lines by opening or acquiring branches, call report information would increasingly encompass the loans and deposits of more than one state. Therefore, although the data collected will not change, the geographical information content of the data is likely to become less useful because the data are collected at the bank level rather than the branch level.

Implementation of Riegle-Neal Is Unlikely to Lead to Material Loss of Information

While the usefulness of data collected at the bank level to provide information for state-by-state measures of banking activity—including monitoring the industry's geographic concentrations—may be affected by Riegle-Neal, it is unlikely to have a material effect on federal regulation or oversight for three reasons. First, as previously mentioned, the data reported on call reports have always had limitations from the standpoint of imparting geographic information about bank loans. Second, deposit data should continue to be provided at the branch level and, with the limitations noted, should provide some measure of state-by-state banking activity. Third, the most useful and detailed information about bank activities is attained through examinations. Regulators with primary supervisory responsibility still have this tool available, although those who rely solely on off-site information will not.

Regulators Do Not Rely Solely on Off-Site Information in Their Oversight

Regulators use the information described in the previously mentioned reports to perform various off-site analyses of banks and BHCs, including (1) financial statements and financial trends, (2) fair lending practices, and (3) market concentrations of deposits. Additionally, bank regulators use call reports and Y-9 reports to assist them in planning, scoping, and conducting safety and soundness examinations or inspections, respectively. Data from these reports provide regulators with financial information about the institutions' activities and reported financial conditions. Analyses of the data provide insights about the institutions over time and compared with other institutions. To a lesser degree, regulators use the annual independent audit reports in planning safety and soundness examinations for those institutions required to have annual independent audits.

Bank regulators are responsible for assessing compliance with various fair lending and consumer protection laws, including the CRA, and they rely, in part, on annual home mortgage-related lending reports to plan, scope, and conduct their compliance and CRA examinations. Likewise, the new small business and small farm loan report is likely to be used in those examinations. The other deposit and reserve reports are not routinely used by regulators in discharging their examination responsibilities, although the related information may be made available to them upon request. These reports are used primarily by FDIC and the Federal Reserve in monitoring institutions' deposit and reserve activities to assess insurance premiums and to determine that banks are maintaining the proper amount of reserves, respectively.

When considering banks' applications for mergers and acquisitions, bank regulators and the Department of Justice also use the various reports—particularly the Summary of Deposits report and the home mortgage loan report—to assess any antitrust or fair lending implications. With respect to their antitrust review, bank regulators and Justice officials typically look to see if the new banking entity could create an undue concentration of loan or deposit activities in a particular market, which could impede fair and open competition among institutions.

Regulatory staff told us that, although the data collected in the various reports are essential to effective off-site monitoring, regulatory actions are rarely, if ever, premised solely upon this information. Off-site information is to be supplemented by on-site examinations or visitations. For example, call reports, which are the most comprehensive and frequently used sources of publicly available information, typically provide regulators with indicators about an institution's activities and condition. However, the call reports must be supplemented with more detailed and explicit information about the institution's deposits, lending, and other investment activities. Similarly, the annual home mortgage loan report is used by the bank regulators as an initial indicator of a bank's performance under the fair lending and CRA laws and regulations, but assessments of the bank's lending practices involve detailed analyses and generally are supplemented by on-site examinations. Regulators recognize that call reports, as well as the other reports, can only provide indicators of an institution's activities and must be supplemented through examinations.

Off-Site Information Has Been Useful in Identifying Trends in Industry Activity

While bank supervisors use call report data primarily for planning their on-site examinations, FDIC staff members told us that they use these data in their back-up oversight authority. In the past, FDIC staff members have analyzed call report data to identify patterns or trends in industry activity or within geographic areas, particularly those that may indicate a problem that could affect industry stability. Their research is important in identifying historical patterns or trends that can be used to project or anticipate potential bank losses, failures, or crises. FDIC staff members expressed concern that call report data are increasingly becoming less useful for these purposes as consolidation occurs, and they are concerned about further deterioration in the data's usefulness after Riegle-Neal is implemented. FDIC staff members are considering recommendations to change the call reports to require banks to report their loan and deposit activity by state.

Views Are Mixed Regarding the Need for More Detailed Bank Data

Representatives from financial institutions and industry trade groups told us that, on the basis of their past experience, they did not believe that interstate branching would materially affect the usefulness, for regulation or oversight purposes, of lending and deposit information currently collected by federal regulators. Specifically, none of these representatives thought that interstate branching would necessitate that federal bank regulators collect additional data to conduct CRA examinations. They pointed out that Riegle-Neal expands the CRA examination process to require separate state-by-state written evaluations, including a rating, for banks with interstate branches. The act also requires that separate written evaluations, including a rating, be prepared for branches located in multistate metropolitan areas. Finally, officials at the federal bank regulatory agencies stated that section 109 of Riegle-Neal requires their agencies to promulgate uniform regulations by June 1997 that prohibit banks with interstate branch networks from using their out-of-state branches simply to operate as deposit production offices (i.e., as offices that take deposits but do not make loans in their communities). On March 12, 1997, the agencies released for comment a proposal setting forth such regulations. Moreover, at least 1 year after a bank establishes or acquires an interstate branch(es), the appropriate federal banking agency should determine whether the bank is operating the branch(es) as a deposit production office.

Representatives from consumer and community organizations did not necessarily believe that a material loss of information would result from interstate banking. However, they stated that to ensure there is no material loss of information necessary to oversee bank activities in an interstate branching environment, banks should be required to submit information on the origin of their loans and deposits. Some representatives suggested that this requirement should take the form of having banks submit call report data for each state in which they operate. In general, the representatives believed that regulators and Congress would better be able to carry out their regulatory and oversight functions if banks were required to submit information on loans by branch as they are required to do for deposits. They also pointed out that such data, by branch, would make it easier for their groups to monitor bank lending activities. As previously noted, many of these organizations had expressed similar concerns about the usefulness of call report data before Riegle-Neal was even considered because information regarding the geographical distribution of loans is one of the groups' particular concerns. Therefore, the implementation of Riegle-Neal did not give rise to their concern, but does heighten it.

Agency Comments and Our Evaluation

We provided a draft of this report to the Chairman of the Board of Governors, Federal Reserve System; the Chairman of the Federal Deposit Insurance Corporation; and the Comptroller of the Currency for their review and comment. We also provided the community organizations we contacted the opportunity to review and comment on a draft of this report. The Federal Reserve and the community organizations did not offer any comments on the draft report. However, the Comptroller of the Currency provided comments in a letter dated February 6, 1997, and the FDIC Chairman commented in a January 27, 1997, letter. The comment letters are reprinted in appendixes I and II.

OCC generally agreed with our conclusions, especially given the call report limitations we described. OCC stated that it understood the potential value of more precise geographic information for researching and monitoring regional trends and the relationship between regional economic conditions and bank performance. However, OCC also recognized that reporting is not without its burdens and that proposals to increase reporting requirements must be considered carefully.

FDIC expressed some concern with the draft report's conclusion, but did not disagree that the implementation of Riegle-Neal in and of itself will not cause a material loss of information. FDIC pointed out that for the last decade banks have expanded their lending beyond traditional geographic boundaries and that, to the extent this trend continues, the usefulness of institution-level data will continue to erode. FDIC's primary concern with our conclusion was that FDIC believes it does not place sufficient emphasis on the effects that interstate branching will have in accelerating this trend and eventually leading to what FDIC considers a material loss of information it uses for statistical and economic studies that assist FDIC in fulfilling its responsibilities.

FDIC believes that its need for the geographic data being lost is greatest for large institutions that FDIC insures but does not supervise because these institutions are more likely to have lending exposures outside of their home states. Given FDIC's unique role and responsibility as deposit insurer, it believes the ongoing loss of geographic data is material to FDIC. In addition, FDIC believes that call report data are the best source of aggregate data, while on-site examinations are less useful for this purpose. However, FDIC acknowledges that, from a cost-benefit perspective, there is a question about what kinds and how much additional data could be justifiably collected—either in call reports or other regulatory reports—that would permit more effective off-site monitoring.

FDIC also suggested that our conclusion was in conflict with our report on the bank oversight structure[5] because in that report, we encouraged the use of off-site monitoring to better target and plan on-site examinations. FDIC believes our position in this current report (i.e., the best institution-level information is available through on-site investigation) contradicts our previous position.

We understand why FDIC places more emphasis than other regulators on the effect Riegle-Neal may have in eroding the geographic content of call report data, given FDIC's responsibility to monitor institutions that it does not directly supervise. As deposit insurer, FDIC may have unique research-based information needs that other federal bank regulators do not have. However, while FDIC may need this type of information, we agree with both FDIC and OCC that this need must be balanced against the burdens additional reporting requirements could impose on the industry. Collectively, the bank regulators are in the best position to make such cost-benefit determinations.

[5]Bank Oversight Structure: U.S. and Foreign Experience May Offer Lessons for Modernizing U.S. Structure (GAO/GGD-97-23, Nov. 20, 1996).

We do not believe our position in this report contradicts our earlier position on the value of off-site monitoring. Off-site monitoring provides regulators with useful indicators about a bank's activities and performance that are generally further analyzed through on-site examinations involving the review of more specific information. Regulators are not precluded from requesting information from banks, beyond the information that is reflected in call reports, to enhance their off-site monitoring as well as decisions about on-site examinations.

We are sending copies of this report to the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the Federal Deposit Insurance Corporation, the Comptroller of the Currency, other members of the banking committees, other interested congressional committees, and other interested parties. We will also make copies available to others upon request.

This report was prepared under the direction of Mark Gillen, Assistant Director, Financial Institutions and Markets Issues. Major contributors to this report are listed in appendix III. If there are any questions about this report, please contact me at (202) 512-8678.

Thomas J. McCool
Associate Director, Financial
Institutions and Markets Issues

Contents

Abbreviations

BHC	bank holding company
CBO	Congressional Budget Office
CRA	Community Reinvestment Act
CRS	Congressional Research Service
FDIC	Federal Deposit Insurance Corporation
HMDA	Home Mortgage Disclosure Act
OCC	Office of the Comptroller of the Currency

Comments From the Comptroller of the Currency

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

February 6, 1997

Mr. Thomas J. McCool
Associate Director, Financial Institutions and Markets Issues
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. McCool:

We have reviewed your draft audit report titled Bank Data: Material Loss of Oversight Information From Interstate Banking Is Unlikely. The review was mandated by the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (Riegle-Neal). GAO was to determine whether implementation of the act would result in a material loss of information that is important for federal bank regulation and oversight. The report concludes that call report data may become less useful for approximating bank activities by state but that implementation of Riegle-Neal is unlikely to lead to material loss of information for federal bank regulation and oversight.

We generally agree with your conclusions. Call Report data have always had limitations, which is one reason why regulators do not rely solely on off-site information in their oversight. More complete information, including geographic information about bank loans, may be obtained through on-site examinations or other means. For example, the OCC uses loan-to-deposit information in small bank Community Reinvestment Act (CRA) examinations. In the case of small banks that cross state lines, if we have difficulty determining a loan-to-deposit ratio for each state, we can compose a ratio by compiling information gathered on site.

On the other hand, we understand the value of banks reporting more precise geographic information. Such reporting might enable the regulators to do more CRA and other compliance work off-site. It would also enable them to monitor and research regional trends and the relationship between regional economic conditions and bank performance. Lastly, there may be an independent public interest in more accurate geographic information. However, reporting is not without its burdens and so proposals must be considered carefully. The Congress recognized this dilemma as well in passing Riegle-Neal.

While enforcement of section 109 of Riegle-Neal would be easier and our determinations more accurate if we collected state by state loan and deposit information, the legislative history of the provision specifically provides that the regulators are not to collect **additional** information in order to carry out their responsibilities.

Thank you for the opportunity to review and comment on the report. Technical comments were provided to your evaluators separately.

Sincerely,

Judith A. Walter
Judith A. Walter
Senior Deputy Comptroller for Administration

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Comments From the Federal Deposit Insurance Corporation

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

FEDERAL DEPOSIT INSURANCE CORPORATION, Washington, DC 20429

OFFICE OF THE CHAIRMAN

January 27, 1997

Mr. Thomas J. McCool
Associate Director
Financial Institutions and Markets Issues
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. McCool:

Thank you for the opportunity to provide comments on the draft GAO report, "Bank Data: Material Loss of Oversight Information From Interstate Banking is Unlikely," scheduled for publication in February 1997. The FDIC has also been assessing the supervisory and regulatory challenges created by an interstate banking environment, including any additional data needs, through an internal Task Force established in 1995. Members of this Task Force have reviewed the GAO report in light of the mandate in Section 112 of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1995 (Riegle-Neal). The FDIC has some concern with the report's conclusion and is providing several more comments related to specific sections of the report.

We would like to preface our comments with the observation that interstate banking will benefit the banking industry by providing institutions with greater opportunities to diversify their risks geographically. Risk diversification should result in a stronger banking system and reduce risk to the FDIC insurance funds.

Concerns About GAO's Conclusion

The statute directs GAO to consider whether there will be any material loss of information important to regulatory and Congressional oversight once interstate branching takes effect, and if so, what modifications are required to prevent a loss of information for this oversight. The report concludes that a material loss of information is unlikely. This conclusion is based principally on the assumption that the regulators will continue to collect Reports of Condition and Income (Call Reports) and Y-9 reports in their current form.

The report characterizes Call Reports and Y-9 reports as the primary off-site sources of data that banks and bank holding companies provide to the regulators. The data in these reports, however, generally is presented on a fully consolidated basis for each institution as a whole without regard to the number and locations of its domestic offices and without any disclosure of the specific geographic area within the United States from which each institution's deposits and loans are derived. Therefore, the FDIC does not disagree with the GAO that the implementation

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of Riegle-Neal in and of itself will not cause an immediate material loss of information. However, for the last decade banks have expanded their lending beyond traditional geographic boundaries. To the extent that this trend continues, the usefulness of the institution-level data collected for off-site analysis and other risk assessment purposes will continue to erode.

Until the early 1990s, aggregate Call Report loan data for banks headquartered in a particular state or region served as a somewhat reasonable proxy for the location of lending and insurance fund risk because banks, their borrowers, and real estate collateral were typically located within the same state or contiguous states. The loan information reported in Call Reports and Y-9 reports could easily be aggregated to determine the risk exposure of the banking system to borrowers, especially commercial borrowers, in any particular state or region. However, in recent years, many institutions have increased their lending outside of their home states for a number of reasons so that an institution's main office location is not necessarily indicative of the geographic location of most of its commercial borrowers. For such institutions, it is not possible to measure an institution's credit exposure to the economies of the different states or regions of the country in which its borrowers are located based on Call Report data as it is currently collected. In fact, with the interstate branching that has already occurred and other market developments, it is increasingly more difficult to construct a time-series from available information that reliably identifies cyclical lending patterns within regions.

As banks expand into electronic banking and further centralize the origination or booking of various products, a bank could have a home office in one state with branches and borrowers in several other states. Given the regional nature of recent recessions, the potential effect of economic downturns on banks and the banking system may be clearly discernible only if the FDIC and the other agencies collect data concerning borrower and real estate collateral location on a regional or state-by-state basis. The enclosed charts, which were discussed during the FDIC staff's August 15 meeting with the GAO staff, illustrate that the usefulness of the institution-level data collected is eroding. Thus, the FDIC's primary concern with the GAO report is that it does not emphasize that, given the current institution-based reporting scheme, interstate branching will exacerbate this adverse trend and eventually lead to what the FDIC considers to be a material loss of information used for statistical and economic studies that assist the FDIC in fulfilling its responsibilities.

For example, in the banking crisis from the mid-1980s through the early 1990s, Call Report data illustrated the effect of regional economic problems on the condition of bank loan portfolios. These cyclical regional lending patterns, which occurred first in the Southwest and later in the Northeast and West, consisted of rapid increases in commercial and commercial real estate loans followed by increases in delinquencies and then in charge-offs. The Bank Insurance Fund was depleted when large numbers of banks located in geographic regions experiencing economic downturns became insolvent from excessive loan losses concentrated in these same regions.

Moreover, the insurance funds suffered significant losses during the 1980s from savings institutions that used out-of-state brokered deposits and acquired loans for real estate projects that were distant from their normal local market. Several of the largest commercial banks also suffered difficulties from geographic lending concentrations. Since existing reports do not adequately provide this geographic data for all banks, it seems prudent for the FDIC and the other regulators to gather sufficient information to identify trends of this type.

As one of the reasons for reaching its conclusion, GAO states that bank examinations provide the most useful and detailed information about bank activities. While this is true in terms of data for an individual bank, the FDIC believes that data developed during examinations is less valuable for evaluating aggregate lending and other activities for the industry as a whole or segments thereof. Cyclical regional lending patterns cannot be easily observed over time from data gathered during examinations, which focus on individual depository institutions, are conducted as of varying dates, and are not compiled on an aggregate basis. Despite the flaws in Call Report data identified in the GAO study, off-site information was once the best source for identifying geographic lending trends. As acknowledged in the report, Call Report data is becoming less useful for approximating bank activities geographically and this adverse trend is likely to accelerate as a result of the June 1, 1997, authority for interstate branching.

The report also emphasizes the availability of geographic home mortgage-related data reported for fair lending purposes. While this data is certainly important for consumer protection, from the standpoint of risk to institutions and the insurance funds, data on the geographic distribution of commercial lending is not available through that type of reporting and is particularly relevant. Many banks and thrifts with commercial real estate and commercial lending portfolios concentrated in certain regions of the country experienced huge losses during the 1980s and early 1990s. For the reasons already mentioned, as interstate branching proceeds, data on commercial real estate and commercial lending on a state-by-state basis could identify these concentrations.

From the perspective of the FDIC, the need for state-level loan information is greatest for larger institutions, all of which the FDIC insures, but many of which it does not supervise, as they are most likely to have significant lending exposures outside their home states. As the insurer, but not the supervisor, of most of these institutions, the FDIC would benefit from off-site geographic data to complement our review of examination data for banks for which we are not the primary supervisor. Given our unique role and responsibility as deposit insurer, the ongoing loss of geographic data relevant to bank lending is material to the FDIC.

Furthermore, the conclusion in this GAO report appears to conflict with the recommendations in GAO's September 1996 draft report on "Bank Oversight Structure: U.S. and Foreign Experience May Offer Lessons for Modernizing U.S. Structure." In the latter report, one of the four mechanisms proposed to improve consistency of bank oversight and reduce regulatory burden is to "[r]equire enhanced off-site monitoring to better plan and target examinations and identify and raise supervisory concerns at an earlier stage." As we mentioned in our comment letter on that report, our off-site monitoring programs are intended to supplement and guide the on-site examination process by providing an early indication that an institution's risk profile may be changing. As long as Call Reports continue to be prepared as institution-level reports, the loss of data, which could serve as a reasonable proxy for geographic information, will increase as banks further expand their lending and other risk-taking activities beyond their home states.

See comment on
p. 29.

4

There is certainly a question about what kinds of, and how much, additional data could be justifiably collected from a cost-benefit standpoint in order to provide information on regional geographic trends that would permit more effective monitoring of potential adverse effects on the insurance funds. The FDIC stands ready to work with the GAO and the other bank regulators on this important issue.

Other Specific Concerns and Comments

Off-Site Information Has Been Useful in Identifying Trends in Industry Activity. The presumption made by regulators in the past that the loans reported on an institution's balance sheet were primarily to borrowers from within its state or service area has become less valid in recent years. This is because institutions may purchase out-of-territory loans or loan portfolios and sell loans made to borrowers in their service area to diversify their lending and because recent technological advances and other developments have enabled institutions to increasingly expand their ability to lend outside their home state without establishing actual branches. In addition, some banks provide credit to "national" companies that are not tied to a state or region. Thus, because Call Reports and Y-9 reports are institution-level reports, the federal banking agencies have been progressively losing borrower location information important to their statistical and oversight responsibilities.

Views Are Mixed Regarding the Need for More Detailed Bank Data. GAO's characterization of the requirements of section 109 of Riegle-Neal in the first paragraph of this section differs from the FDIC's understanding of that section. Under our interpretation of section 109, at least one year after a bank's establishment or acquisition of an interstate branch or branches, the appropriate federal banking agency should determine whether the bank is operating these branches as deposit production offices. This determination is to be based on the ratio of the bank's lending in the host state compared to all banks for which that is the home state. In our opinion, the federal regulators do not have, at this time, sufficient information on total deposits and total loans by state in which the depositor or borrower is located to appropriately determine this ratio.

We have included as an enclosure several other technical comments for your consideration.

We appreciate the opportunity to comment on this report.

Sincerely,

Ricki Helfer

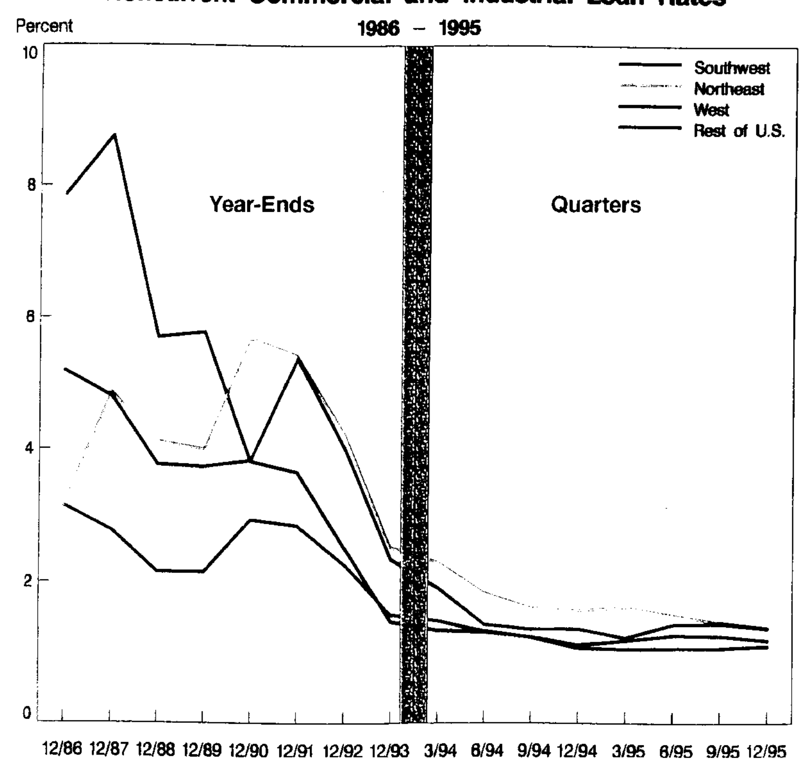
Ricki Helfer
Chairman

Enclosures

Note: The charts on pages 24 to 27 were scanned from color originals, which do not produce high-quality, black-and-white copies.

In the past, geographic correlations between the location of an institution and the location of its borrowers were discernable from Call report data. The impact of rolling recessions can be seen in the regional noncurrent rates for commercial and industrial ("C&I") loans in the 1980s and early 1990s. Note that the problems struck first and strongest in the Southwest, then in the Northeast, and most recently in the West. The convergence of the regional rates in recent years reflects the absence of regional recessions. The potential for loss of this correlation in the future will be shown in subsequent charts.

Noncurrent Commercial and Industrial Loan Rates*
1986 – 1995

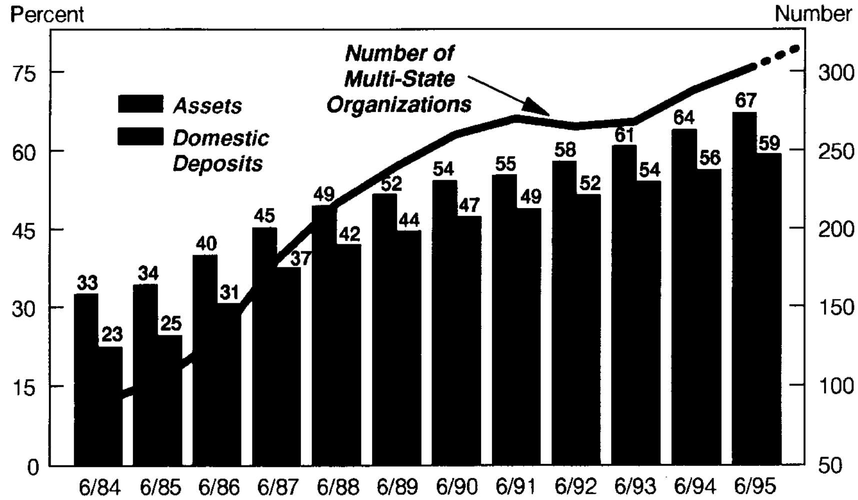


*Commercial and industrial loans past due 90 days or more or in nonaccrual status as a percent of total commercial and industrial loans.

1

An increasing share of the industry is contained within multi-state companies. In the last ten years, a small but growing number of companies with deposit-taking offices in more than one state have acquired market share. Since 1985, the number of companies with multi-state operations has increased from about 100 to more than 300. These 300 companies now have sixty percent of the domestic deposit market and two-thirds of the industry's assets. The share held by multi-state organizations is expected to grow as mergers are completed.

Number of Multi-State Organizations and Their Share of Assets and Deposits*



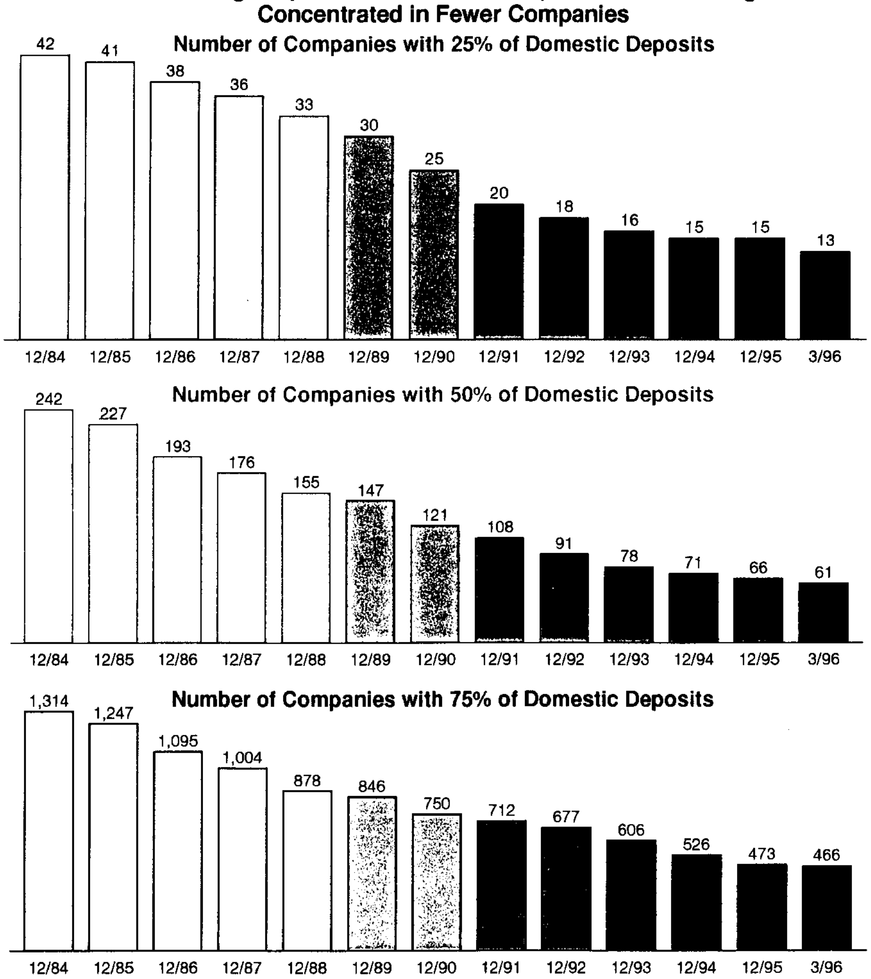
*Multi-state organizations are holding companies and independent depository institutions with operations in two or more states.

Sources: Bank Summary of Deposits, Thrift Branch Office Survey, FRB NIC Database, FDIC DRS RIS Database.

2

At the same time that Call reports are becoming less useful for identifying geographic risk concentrations, the industry is becoming more concentrated in a shrinking number of companies. Since 1984, the number of companies holding 25 percent of domestic deposits has fallen from 42 to 13. Fewer than 500 banking companies now hold three-quarters (75 percent) of domestic deposits. Mergers among large companies are expected to further consolidate the system.

A Growing Proportion of Domestic Deposits* Is Becoming Concentrated in Fewer Companies



* Includes deposits of insured commercial banks and savings institutions.
Individual companies have been accounted for at their highest level of consolidation (multi-bank holding companies, single-bank holding companies or independent banks/thrifts)

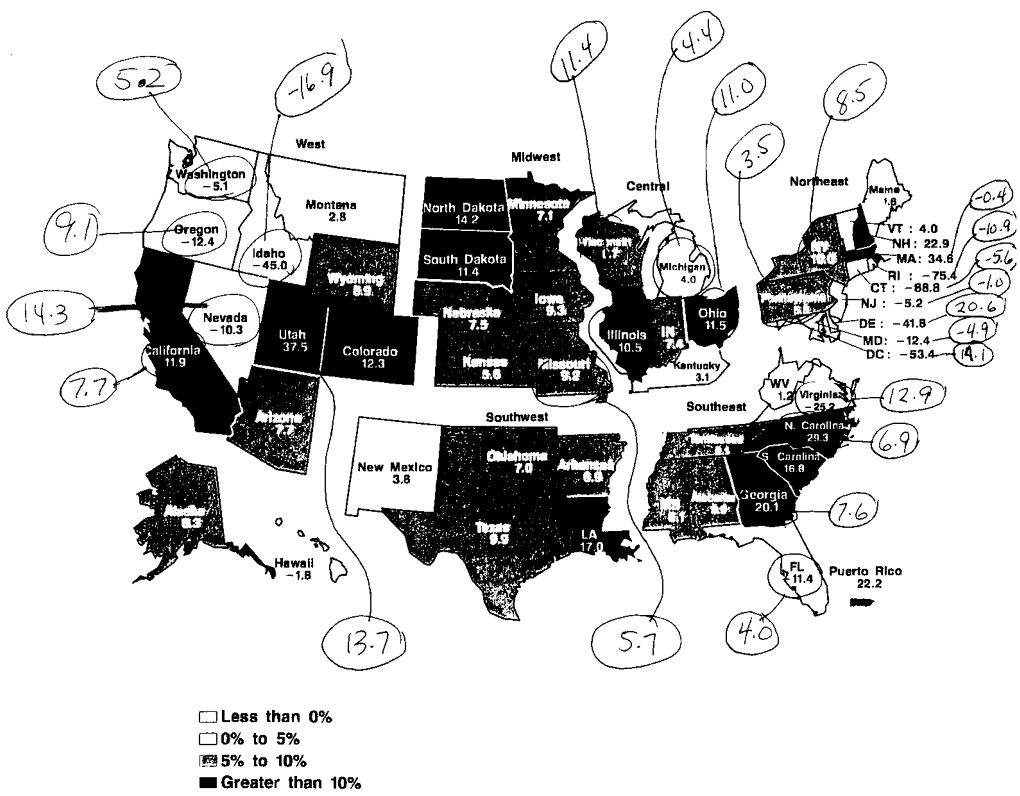
Prepared by: Division of Research and Statistics
Sources: FDIC DRS RIS Database

3

Correlations between the location of a bank's headquarters and the location of its customers are disappearing. The implementation of the "30 mile rule" has enabled some companies to branch across state lines by consolidating commercial bank subsidiaries. The map, as annotated, illustrates adjustments needed to "normalize" 12 month growth rate calculations through June 30, 1996. Twenty-three states had to be adjusted to calculate C&I loan growth rates based on the location of main offices.*

Commercial and Industrial Loan Growth Rates

June 30, 1995 – June 30, 1996



* For example, to adjust for the movement of Riggs Bank, N.A. from DC to Virginia in January, Riggs C&I loans as of 6/30/95 were subtracted from the total for DC and added to the total for VA before the 6/95-6/96 growth rates were computed.

4

The full implementation of interstate banking will eliminate the ability to identify geographic concentrations of credit risk. The following table shows what would happen if existing multi-state holding companies consolidate all their banks and savings institutions into a single "lead" subsidiary bank. Thirty-eight states show apparent shrinkages in loans while a few states show substantial growth.

CHANGES THAT WOULD RESULT FROM CONSOLIDATION ($Millions)

STATE	DOMESTIC LOANS As of 3/31/96	INCREASES*	DECREASES**	NET CHANGE $ AMOUNT	NET CHANGE %
AZ	37,290	0	34,840	(34,840)	-93.43
ID	8,837	0	7,973	(7,973)	-90.22
SD	22,814	57	18,359	(18,302)	-80.22
WY	5,648	20	4,158	(4,138)	-73.27
DC	2,091	18	1,494	(1,476)	-70.61
NV	20,370	0	12,899	(12,899)	-63.32
CO	23,778	37	13,909	(13,872)	-58.34
DE	82,150	1,636	46,857	(45,221)	-55.05
NM	8,974	161	4,862	(4,700)	-52.38
WA	61,275	87	32,021	(31,933)	-52.11
TX	155,589	93	76,875	(76,782)	-49.35
MD	50,858	2,118	27,154	(25,036)	-49.23
SC	20,730	44	9,982	(9,938)	-47.94
FL	115,271	459	55,461	(55,001)	-47.71
RI	14,317	2,550	9,089	(6,539)	-45.67
KY	38,470	210	17,694	(17,485)	-45.45
IN	57,285	1,815	27,477	(25,662)	-44.80
ND	8,987	1,278	5,059	(3,781)	-42.07
CT	46,130	0	18,979	(18,979)	-41.14
GA	93,288	24,340	56,699	(32,360)	-34.69
IA	28,405	102	9,447	(9,345)	-32.90
ME	11,291	576	4,264	(3,689)	-32.67
MT	6,280	256	2,141	(1,885)	-30.01
AK	3,223	0	892	(892)	-27.67
KS	21,984	318	5,644	(5,326)	-24.23
WV	14,585	358	3,552	(3,193)	-21.89
LA	27,326	143	6,105	(5,963)	-21.82
NH	13,223	71	2,909	(2,838)	-21.46
OK	21,397	103	4,178	(4,075)	-19.05
TN	48,382	4,354	13,185	(8,831)	-18.25
AR	18,733	1,466	4,430	(2,964)	-15.82
NJ	84,973	3,292	15,426	(12,135)	-14.28
OR	31,570	13,246	17,291	(4,045)	-12.81
NE	21,944	1,847	3,740	(1,893)	-8.63
VA	59,428	4,206	8,477	(4,271)	-7.19
MI	95,308	14,462	20,060	(5,598)	-5.87
WI	56,947	6,707	8,436	(1,730)	-3.04
MS	17,828	1,780	1,834	(54)	-0.30
HI	16,350	270	0	270	1.65
VT	5,848	1,108	649	459	7.85
IL	157,472	42,930	28,020	14,911	9.47
NY	324,757	68,132	28,105	40,027	12.33
UT	13,572	5,257	2,897	2,360	17.39
CA	375,790	86,365	17,632	68,733	18.29
PA	148,812	32,620	3,619	29,001	19.49
MO	57,656	21,283	1,270	20,013	34.71
MA	84,949	38,579	7,152	31,427	37.00
AL	39,605	20,856	1,875	18,981	47.93
OH	144,333	98,512	3,820	94,692	65.61
MN	45,948	41,803	2,352	39,450	85.86
NC	116,963	164,907	864	164,042	140.25
Total	**2,989,033**	**710,834**	**712,111**	**(1,277)**	

* the amount of loans reported by banks headquartered in other states before consolidation.

** the amount of loans that would be reported by banks in other states after consolidation.

Increases do not equal decreases because banks and savings institutions headquartered in U.S. territories are excluded.

5

The following is GAO's comment on the Federal Deposit Insurance Corporation's letter dated January 27, 1997.

GAO Comment

Text was added to eliminate confusion about when FDIC must produce regulations and make determinations about deposit production offices.

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