



**STATEMENT OF MICHAEL P. SMITH
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BEFORE THE
NEW YORK STATE ASSEMBLY STANDING COMMITTEE ON BANKS
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Good morning. My name is Michael P. Smith and I am President and Chief Executive Officer of the New York Bankers Association (NYBA). Chairman Towns and Members of the Assembly Banks Committee, thank you for the opportunity to appear before you today. Our Association is comprised of the commercial banks and thrift institutions doing business in New York State, with assets ranging from trillions of dollars to some of the smallest depository institutions in the country.

Chairman Towns and Members of the Assembly Banks Committee, thank you for the opportunity to appear before you today. This hearing into the future of the "dual banking system" is very opportune. Public policy decisions are being made at a rapid pace by the Executive, Judicial and Legislative branches on the continued viability of the system. For example, the Supreme Court this summer, in a case brought by New York's Attorney General, clarified the relationship between State and federal law enforcement. The new Administration has proposed an extraordinary package of financial regulatory reform bills that would directly impact the ability of States to regulate and supervise institutions that they charter and for which they have always had primary jurisdiction. And Congress is currently considering this package and other bills that would, we believe, place New York's continued preeminence in the world financial services business into jeopardy.

My testimony will 1) focus on the role of New York in creating and maintaining the nation's vital dual banking system; 2) describe some of the recent actions by the State that have placed it in a leadership position in the national debate on banking regulation; and 3) raise a number of concerns about legislation pending in Washington that, we believe, would disrupt the balance in the dual banking system.

The New York Bankers Association strongly supports the dual banking system. New York's banking system is far older than that instituted by the federal government, with the Bank of New York's charter issued before the U.S. Constitution was written. Our State's Banking Law was

enacted fully a quarter century before the National Bank Act and was the model for that statute that created the federal banking system. With more than two centuries fostering and regulating the banking system, and as the home of some of the largest banks in the world, New York can take pride that it has a vibrant dual banking system – one which the industry hopes to sustain.

What is the dual banking system? In short, it is a legal construct that allows banks and thrifts to choose whether they want to be chartered under state or federal law. The reasons for these charter choices have varied over the years as federal or state law has provided a climate that encouraged most effectively institutions they chartered to be successful in the marketplace. The “charter of choice” has varied, with one or the other system gaining precedence over the years. For example, the original National Bank Act, passed to help finance the Civil War, was intended to enforce a monopoly in the issuance of currency by national banks. The state system responded creatively, inventing checking accounts to establish a payment system that would rival cash. As recently as the early 1990’s, most of the largest New York banks had State charters.

The enactment of interstate banking and branching legislation, first in New York and then in Washington, in the mid-90’s, has put pressure on the State-chartered banking system. While many newer banks have chosen State charters, some of the largest banks have converted to federal charters. A national banking charter or federal thrift charter appeared to make sense in the first years of this century, when the Comptroller of the Currency offered the opportunity to operate across state lines with a single regulator, a single set of rules, and a single system of examination and supervision. However, New York, over the past two decades, has continued its leadership role, beginning the re-vitalization of the dual banking system by, among other acts, passing a “wild card” law to ensure that State banks and thrifts had powers commensurate with those of their federal counterparts, engaging neighboring state banking departments in an interstate compact to provide a single regulator for state-chartered banks in the states into which they can branch, reviewing its Banking Law to prune obsolete provisions and graft in important new powers, such as the ability to branch interstate de novo, and enacting tax legislation that

accommodates the merger of banks, securities firms and insurance companies – a provision that dramatically enhanced the ability of regulators to deal with the collapse of several large, non-bank financial institutions last year. As a result of these progressive measures, the State's banking charter remains vibrant – as testified to by, among other things, Goldman Sachs' choice of a New York State charter when it became a bank holding company last year.

It has been asserted that the dual banking system provides a “competition in laxity,” allowing banks and thrifts to choose a regulator that imposes the least restrictive conditions on its operations. This argument is patently false. The strength of the State's banking system is amply demonstrated by the extent to which New York avoided some of the problems that have plagued other urbanized states during the current financial crisis. New York's extremely effective regulation of predatory lending, enacted originally in 2002, years before the current crisis emerged, and updated by additional enactments almost every year – including the major mortgage and foreclosure statute advanced by Governor Paterson last year – has kept the State's foreclosure rate – still tragic for each family affected – among the lowest in the nation. Most recent figures available from RealtyTrac, the most comprehensive source of foreclosure statistics nationwide, show that New York has the 39th highest foreclosure rate in the nation, approximately 1/4th the national average. While the State certainly has troubled pockets of foreclosures, it has avoided the worst of the nation's problems.

As it has led in mortgage and foreclosure laws, the State has also adopted ATM safety provisions, basic banking accounts, credit card disclosures and other laws too numerous to detail that have protected New York consumers while allowing the State's banking system to grow. Importantly, most of these laws are complied with by the State's federally chartered banking institutions as well as State banks and thrifts, because they make sense. And many – such as the State's predatory lending law and mortgage regulations - have now been adopted by federal legislators and regulators. The dual banking system as a proving ground for new laws has demonstrably succeeded in New York.

As if to confirm New York's position in financial services, the U.S. Supreme Court this summer chose a case arising from the State, Cuomo v. Clearing House, to clarify a provision of national banking regulation. The Court ruled that a state may enforce its valid, non-preempted laws against national banks, an important holding that preserves State law enforcement while continuing to permit national banks and federally chartered thrifts to operate under uniform federal laws.

Unfortunately, provisions contained in the President's regulatory reform package would threaten the clarity and consistency of the federal preemption doctrine, potentially subjecting all banks and thrifts to a confusing clash of federal and State law and even potential conflicts in direction between their regulators charged with safety and soundness enforcement and a newly established entity charged solely with consumer protection.

The legislation would create a new Consumer Financial Protection Agency (CFPA) designed to develop and enforce regulations that enhance consumer protection in the financial services industry. We understand the concern regarding the current regulatory system. But even the Treasury Department acknowledges that 94% of troubled sub-prime loans were made by non-bank lenders. However, the new agency, as currently designed, will not effectively regulate non-bank financial institutions, but would layer a new and costly level of regulation on federally insured banks and thrifts. When New York set out to regulate mortgage bankers, it enacted a new article of the Banking Law to do so; when it regulated check cashers, it put in place specific provisions of law applicable to that business; when it wanted to ensure appropriate supervision of finance companies, it passed a licensed lender law. The federal bill that would authorize the CFPA contains no such provisions, leaving the agency without direction as to how it would regulate such disparate businesses.

The new CFPB would be composed of the consumer protection arms of the existing federal bank, thrift, credit union and consumer financial enforcement agencies. Because its mission would involve the regulation and supervision of all financial institutions doing business in the United States (other than insurance firms and SEC- and CFTC-supervised companies), however, it would have a vastly greater scope of authority than current financial consumer protection entities. But with personnel and funding based on that provided by the traditional financial institution regulators, the scope of the agency is simply too vast to be funded and staffed at the old level.

At the same time, the reliance in the legislation on potential State enforcement of both federal and State consumer protection laws is seriously misplaced. Very few of the State banking or financial institution regulators have anywhere near the staffing and funding necessary to take on effectively regulating all of these types of financial institutions. Even the New York State Banking Department, which we believe is the best staffed and most well-funded in the country, does not have enough examiners to oversee each of the types of financial institutions which it currently supervises. Given the State's current budget problems, it seems unlikely that the Department's resources will be dramatically expanded in the near future.

We are therefore urging that the federal banking and thrift regulators retain their current missions of providing both consumer protection and prudential supervision over federally insured depository institutions and their affiliates. Consumer regulation and safety and soundness regulation are two sides of the same coin. Neither can be separated from the other without negative consequences. FDIC Chairwoman Sheila Bair, in testimony before Congress this summer, stated: "The current bank regulation and supervision structure allows the banking agencies to take a comprehensive view of financial institutions from both a consumer protection and safety and soundness perspective. Banking agencies' assessments of risks to consumers are closely linked with and informed by a broader understanding of other risks in financial institutions. Conversely, assessments of other risks, including safety and soundness, benefit from knowledge of basic principles, trends, and emerging issues related to consumer protection.

Separating consumer protection regulation and supervision into different organizations would reduce information that is necessary for both entities to effectively perform their functions. Separating consumer protection from safety and soundness would result in similar problems.”

Retaining safety and soundness and consumer protection supervision in the same agency will increase the efficiency of bank and thrift regulation, while allowing the CFPB to concentrate on regulating the non-federally insured financial services businesses that have so long gone without effective federal or State regulation. In order to assure that all types of financial institutions play by the same rules, we would urge that the CFPB be required to consult and reach agreement with bank and thrift regulators in issuing new consumer protection regulations. If it is felt that a single federal regulator is needed for traditional federally insured banks and thrifts and their affiliates, we would not oppose concentrating enforcement authority for consumer protection regulation in one of the bank or thrift prudential regulators.

The President’s proposed regulatory reform package would also have eliminated the federal thrift charter, threatening the entire system of dual banking for savings and loans and savings banks. New York is home to some of the largest thrift institutions in the country, including savings institutions in mutual form. These institutions have served as a system of dedicated housing lenders, and have typically held their mortgage loans on their books. In stressed times, such as those which the State has experienced for the past 18 months, maintaining a steady flow of neighborhood-based credit is extremely important. Fortunately, it now appears that there is little appetite in Congress to repeal the federal thrift charter, or to eliminate mutuality. We strongly urge that any legislation finally adopted recognize these values.

The CFPB bill would also seriously impair the system of federal preemption that has allowed nationally chartered banks and thrifts headquartered in New York to operate nationwide under a uniform set of laws. We support strong nationwide standards in lending and oppose the establishment of a patchwork of state laws which would threaten New York’s position as the world

financial capital. The bill, as currently structured, would strongly cloud the ability of New York-headquartered, federally chartered banks to carry with them the same set of laws and regulations wherever they operate in the country. Every bank would potentially be subject to as many as 51 competing State and District laws on top of the regulations adopted by the new CFPB. This potentially confusing and costly legal system would be a recipe for operational inefficiency, but also for consumer confusion. Since a New York consumer could potentially be receiving solicitations from banks and thrifts in many different jurisdictions and with many different regulatory mandates, the consumer would have no idea what protections they actually enjoyed. Restricting national standards, we believe, would both handicap New York's ability to retain its place as the nation's premier financial services headquarters State, but also sink its consumers in a maze of conflicting and confusing consumer protection provisions. We urge that the current system of uniform national standards, as clarified in the Supreme Court's Cuomo decision, be maintained.

Moreover, while most public attention has focused on the establishment of the new Consumer Financial Protection Agency, other provisions of the President's regulatory reform package would directly override sections of State law. For example, the Treasury's recommended section 610 would override the authority of states to adopt loan-to-one-borrower limits for their state-chartered institutions, subjecting the institutions instead to the same lending limits as federal banks and thrifts. New York provides higher lending limits than those available to national banks. If the States cannot prudently and incrementally enhance the authority of their State-chartered institutions, the State banking system, and the dual banking system, cannot exist.

We greatly appreciate the opportunity the Committee has provided to comment on the important issue of the role of the State in financial regulation. I would be happy to answer any questions you might have.