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Decisions, decisions for community banks

By Robb Soukup

Deciding whether to remain independent, and whether to switch charters, will be the key strategic decisions facing banks in the coming year, according to speakers at FinPro's 2011 Presidents and Directors Conference.

They addressed the ways in which the current operating climate – with its pinched margins, increased regulatory costs and bone-dry loan demand – has transformed the strategic environment and considerations for bank boards.

An issue many bank boards should be revisiting, according to FinPro CEO and President Don Musso, is one they may have neglected since the founding of their institutions: their charter. With regulatory consolidation under way, banks should strongly consider whether a national charter still makes sense, he said. The most important consideration for a board weighing that decision was the state of the institution's relationship with its primary regulator. "The regulator that you know is better than the regulator that you don't know," Musso said. "If you've got a good working relationship with your regulator, even if there's a cost-benefit to moving, stick with your current regulator."

He did see one likely victim of the changing regulatory guard. "MHCs are on the downturn. That's the one bad message I have. If you're an MHC, I don't see long-term survivability," Musso told the audience.

He also said that access to capital markets, one of the main reasons many banks adopted a holding company structure, has essentially become a nonissue to most community banks. "The real world is we don't have access to capital markets ... we don't need holding companies anymore," he said. There are a number of scenarios in which it is a requirement, such as for organizations that have complex capital structures, Musso admitted, though many community banks will not fall under one of those categories.

"Eliminating the holding company is going to save you considerable dollars: it eliminates a regulator, the Federal Reserve; it makes you exempt from the SEC, and it cleans up your legal structure," he told the audience. He estimated that about half of the bankers in attendance didn't actually need a holding company.

Of course, the biggest issue that looms over many institutions is a fundamental one. With so many headwinds facing smaller institutions, Leonard Rubin, a partner with Nelson Mullins Riley & Scarborough, said that boards will be forced to sit down and debate staying independent or exploring a merger. He urged board members to carefully think about the implications of both options and to keep detailed meetings at minutes so they can justify their course to both regulators and shareholders. He also said institutions deciding to stay independent may have to resign themselves to shrinking the balance sheet or accepting a recapitalization, among other options.

Still, while Musso also expects these deliberations will occur or continue, he is skeptical that they will set off a wave of mergers. "We don't have buyers and sellers on the same page, and we're not going to have buyers and sellers on the same page until or unless regulators demand it," he said. "The pricing is so off on either side, I just don't see a lot of deals getting done."

Rubin, for his part, said that many bankers will likely be tempted into agreeing to a merger of equals as pressures on their institution continue to rise. He added, though, that regulators will likely make these complicated transactions even more difficult. "Expect increased regulatory scrutiny for M&A deals, especially for community bank so-called mergers of equals," Rubin told the audience. "The regulators are likely to require additional capital, and perhaps new management, as conditions for approval."