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Weighing the Benefits of a State Charter

Within the past year, several national banks and federal savings banks have come to realize the benefits of converting to a state bank charter. This is not a new concept. Since 2000, hundreds of national banks and federal savings banks across the country have converted to state charters. These banks typically cite three reasons for converting: cost savings and increased earnings, regulatory access and relationships, and the dilution (or disuse) of national bank powers.

1. **Lower Expenses & Increased Earnings**
   Most national banks pay significantly higher regulatory and examination fees than their state bank peers. Depending on the state, a $250 million asset national bank may save $25,000 to $50,000 or more in annual supervisory assessment fees by converting. In addition, banks in many states may see their legal lending limit increase, allowing them to better compete for loans and reduce participations.
   However, the conversion process is not free. **Each state has a filing fee, and the applicant must pay for legal costs**, a state regulatory examination and the costs of rebranding the institution to remove any references to being a national bank. Even with these costs, several banks have found that the costs of converting are justified when compared to the aggregate costs saved and the potential for increased earnings.

2. **Improved Regulatory Access and Relationships**
   In the current regulatory environment, banks are increasingly attuned to the benefits of having local access to their primary regulators. In certain parts of the country, the Office of the Comptroller of the Currency has been experiencing significant turnover, thus making it hard for some banks to establish and maintain continuity with their regulatory contacts. In some areas, seemingly routine matters are being handled through a regional or national office. Further, the OCC has been rotating examination staff around different areas of the country. This constant change in examination staff may impact the examiners' ability to gain a thorough understanding of the bank, its markets and culture.
   With a state charter, **all decision makers are local and should be better aware of the issues affecting banks in their state**. That being said, with a state charter, the bank will now have two regulators: the state, and the Federal Deposit Insurance Corp. or the Federal Reserve. Even so, for many it is appealing to be able to visit the state's banking commissioner face-to-

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face on relatively short notice to discuss the bank, appeal a finding, or seek guidance and assistance.

3. **Dilution of National Bank Powers**
   Historically, a primary benefit of a national bank charter was the broad federal preemption of state laws that the charter offers. This was especially important for banks operating in multiple states, as they did not need to comply with many aspects of the differing laws in the states where they operated. However, the enactment of the Dodd-Frank Act resulted in significant cutbacks and a reduction in the availability of federal preemption. In addition to narrowing the differences between state bank charters and national bank charters, the majority of national banks are community banks that do not actually operate nationally. Therefore, national banks should consider whether the availability of federal preemption is truly benefiting the bank, and what other real or perceived benefits the national charter carries.
   Each state will have its own statute providing the authority for converting from a national bank to a state bank. It is important that the board and management team of a bank considering a conversion determine whether its current charter is best suited for its business model, goals and objectives. If the state agency believes that the bank is just forum shopping for regulators in order to avoid difficulties with the OCC, the agency will be more likely to decline the conversion application.

Note that Dodd-Frank generally restricts the charter conversion of troubled banks, including a bank with any formal enforcement order or memorandum of understanding. Dodd-Frank also requires a bank seeking a conversion to file its application with both its current and its prospective regulator. Therefore, be aware that the OCC will know in advance of the plan to convert.

Overall, the combination of reduced costs, potential for increased earnings, easier access to regulators and favorable state laws make the conversion to a state charter an enticing choice for many financial institutions. If your bank has a national charter, it is something to consider.

If you have specific questions, please contact John Reichert or Jim Sheriff.

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