INTERCHANGE & PCAOB REQUIREMENTS

by Steve Brown

Today we have two odd issues to consider, so this article is designed to serve as a reminder. Neither issue is life threatening to bankers, but both are important and could cause material harm if it applies to your bank and you do nothing.

The first issue is whether or not to make a comment on the debit interchange cap proposal. As we wrote last month, the Fed released a proposed rule that is out for

comment. Under that proposal, debit card interchange fees will be capped (at about 55% to 70% of the current level). So far, we have not seen community banks getting involved much. While that is probably because the proposal doesn't apply to banks under $10B, this doesn't mean that it won't have a potentially significant impact. First, community banks are part of the industry, so despite the carve out, the proposal will hurt revenues, valuations, harm public opinion and weaken the stability of the system. More importantly, perhaps, despite the $10B exemption, a 2-tiered system is not likely to develop, since the large banks control most of the debit volume and will be placing pressure on the networks (Visa/Mastercard) not to allow all the changes needed to develop a 2-tier structure. Ultimately, we see the networks doing the right thing, but the programming and changes required to support such a system is significant and will likely not occur before the law goes into effect by July 21st.

While we could go off on how the rule is unclear, doesn't fully take into account risk and generally has design flaws, the Fed should simply hear from your institution on the potential impact to your revenue stream and how it relates to your cost and risk around debit cards. An overview of the issues can be found here http://tiny.cc/BIG_FDA_Interchange-OV. In addition, at the bottom of the release is an easy application that allows banks to view and submit comments. Given that a comment takes less than 15 minutes to do, we consider that a pretty good investment, given the amount of money and customer impact involved. If we can just help water down this rule and or raise the cap (or make it more workable), that would be a step in the right direction.

Our other issue this morning is a little more esoteric and has to do with making sure your auditor is PCAOB registered. Starting this year, most stock custody agents are requiring your auditors be Public Company Accounting Oversight Board (PCAOB) registered, in order to be able to hold the stock of your bank in an investor's name. If you are a public bank, then your auditors are most likely registered. However, we pulled up a group of local and regional CPA firms and found that they were not registered. Thus, if you are a privately held bank and have stock in custody (which most banks do), you should probably check to see whether your auditor is registered (the list can be found here: http://tiny.cc/BIG_PCAOB_Reg). Even if they are on the list, bankers are also urged to check to be sure paperwork is complete with your custody agent. When we were doing research for this story, we found several banks that haven't yet submitted the paperwork (which was due last year for most firms).

Unfortunately, the two issues we highlighted today are going to be typical of the flow we can expect over the next 3-5 years. The industry is shifting sharply, driven in no small part by Dodd Frank, so remembering things to do this year will be especially critical.

Related Links:
[Interchange Overview]
[PCOAB Registered Auditors]

BANK NEWS

M&A

BankFirst ($606mm, FL) entered a deal to purchase Commercial Bancorp Inc., holding company of East Coast Community Bank ($89mm, FL) for an undisclosed sum. As of 3Q, East Coast had $5.4mm in delinquent loans with a loan loss reserve of $1.8mm.

BofA Fee Structure

The bank will begin testing new account structures in states that represent 10% of its customers. Basic checking accounts will be charged $9/month with no ability to waive the fee. For accounts with more features, fees will be larger but customers will be able to overstep the cost by maintaining minimum balances, online banking or etc.

Consumers 2010

After furious holiday spending, the ratio of household debt outstanding to personal income was 122% at the end of the year. A ratio below 100% (last seen in 2002) is required for household debt outstanding to be less than disposable personal income (a level many economists feel is needed to support robust consumer spending once again).