3-RATED AND WAITING FOR SBLF MONEY? GO WHISTLE

Dividend waiver issue may keep your bank from getting funds

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News Announcement: The Small Business Lending Fund is available only to CAMELS 1- and 2-rated banks.

You won't read that in the paper or on a website (until now, in this blog), but that's the case, effectively. Read on if you want to know why I say that.

A nonrestriction restriction, perhaps?

Many of you remember the much-ballyhooed Small Business Lending Fund. This program was passed by Congress as part of the Small Business Jobs and Credit Act of 2010, last September. The act set up a $30 billion fund administered by the Treasury to encourage community banks to increase small business lending. When the fund was first announced, many jokingly called it "TARP LITE."

At the time, we were told that it is not TARP LITE or TARP II because it would not have the same type of restrictions that TARP had, and because the Small Business Lending Fund would be available to any bank that is other than 4 or 5-rated, and had not been on the problem bank list for the previous 90 days.

A couple of weeks ago, Treasury, in connection with the administration of the Small Business Lending Fund program, sent letters to every bank that applied for money. The letters asked each bank to either confirm that it was not under any type of dividend restriction from its the primary federal regulator, or affirm that the bank, if it was under a dividend restriction, was going to attempt to have the dividend restriction lifted.

In order to have the Small Business Lending Fund application considered, any dividend restriction on a bank applicant would need to be lifted by August 1, the letter stated.

Doing the math on banks affected

By my best estimate, there are approximately 2,500 banks in the country under some kind of enforcement action. Every one of those actions, as a practical matter, has a provision in it that says the bank cannot pay dividends without permission of the regulator.

Now, let's exclude the 4- and 5-rated banks that are under some kind of formal enforcement action, and only focus on the 3-rated banks that would typically be under something totally unenforceable and nonpublic, such as a Board Resolution or a Memorandum of Understanding. Actually, even those documents, virtually every time, contain some kind of a dividend restriction, i.e., no payment without permission of your primary federal regulator. Even though the dividend restriction is unenforceable and nonpublic, it is present and most banks follow it.

Thus, the imposition of the bar to participation for any bank with a dividend restriction creates some interesting issues. A bank participating in the Small Business Lending Fund could reduce dramatically its cost of capital from 5%, for example, under the TARP, to possibly as low as 1% under the small business fund.

For most banks, that would result in a dramatic savings. It would also result in a higher capital ratio at the end of the day and a stimulation of the economy through the increase in small business lending.

But...

Even though a 3-rated bank's participation in the Small Business Lending Fund would appear to be a win-win for everybody, i.e., the bank, the industry, the regulator (higher capital maintained), and the economy, it apparently will not happen. Not if the regulators are expected to waive their right under these informal documents to approve the bank's dividend on a quarterly basis.

Regulators who will not budge

I have had several interesting meetings and phone discussions with federal regulators in various parts of the country.

For example, in one case, I advised the federal regulator that if the agency involved would simply waive it dividend

restriction in the informal, nonpublic Memorandum of Understanding, the bank involved could save over $4 million in interest payments over a five-year period. It could have done so by refinancing their TARP into the Small Business Lending Fund.

The answer, effectively, was "We really don't care."

The rationale was that the agency was not going to waive the dividend restriction because a dividend restriction is "in every enforcement action we have ever done for a 3-rated bank and we are not changing that policy."

In other words, we are going to do this because we have always done it this way. It really does not matter that if we waived it, the bank could reduce its interest on the Small Business Lending Fund from 5% to 1%, that it would save $4 million and its capital account would go up by 50 basis points, and that everybody, including the regulators, would be better off.

We are simply not going to do that because we have never done it before.

So much for "Let's get the banks to increase small business lending." That is as long as the regulators do not have to do anything they have never done before when considering it.

Frustrating, to say the least.

About the Author

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