WRITTEN TESTIMONY OF PATRICK J. KENNEDY, JR.
BEFORE THE TEXAS SUNSET ADVISORY COMMISSION
MAY 24, 2018

Chairman Birdwell and Members of the Commission, thank you for letting me testify and submit written testimony. My name is Patrick J. Kennedy, Jr., I am Managing Partner of Kennedy Sutherland LLP, s law firm which represents community banks and thrifts, their shareholders, directors and officers in Texas and numerous other states. We have decades of familiarity with the Texas Department of Banking (DOB), the Texas Department of Savings and Mortgage Lending (TDSML) as well as the three federal bank regulatory agencies. I am also the principal shareholder of a TransPecos Financial Corp, a registered bank holding company that owns TransPecos Banks, a state savings bank, which operates in small rural communities in West Texas.

I am here on my own behalf and on behalf of our Board of Directors to respectfully express strong opposition to the Staff's recommendation to merge the TDSML into the DOB.

State Savings Banks are Different

A Texas State Savings Bank is required to meet the qualified thrift lender test established under federal law and as such must have at least 50 % of its total assets measured monthly invested in residential mortgage loans, small business loans and a list of related qualifying securities, loans and investments. There are other not insubstantial differences as well. This specialized lending mission is consistent with the decades of experience and developed expertise of the TDSML.

In addition to residential lending and small business focus, TDSML has encouraged community development lending and related activities, including the New Markets Tax Credit program and low income housing tax credits. This is one of the reasons our Bank converted its charter to a state savings bank in July 2016.

State Savings Banks Pay lower Assessment fees than State Banks

The assessment fees of TDSML are substantially lower than those of the Department of Banking. Our Bank CFO advised that we saved $43k/year the first year we switched to TDSML which is a 60% decrease from the TDOB. For 2017, I was advised the DOB rate would have been $40K vs. the $28K that TDSML assessed. The DOB uses an assessment rate tied to the OCC while the TDSML uses an assessment rate tied to total assets and a current annual rate schedule approved by the Finance Commission. This kind of difference is very important for smaller institutions such as ours.

TDSML Does More For Less and small size offers more personalized relationships

My observation is that TDSML "does more with less" in terms of examination teams on site and the efficiency with which they work. The close working relationship which our bank management team and principal shareholders and board has developed with TDSML has supported a very positive and beneficial exchange, focused on the best interests of the Bank, the shareholders, the public and the FDIC insurance fund.

Merging TDSML will be a significant multi-year project that may costs millions of dollars

TDSML has an entirely separate set of laws, rules and regulations governing SSBs and its examiners and corporate administrative staff are trained and knowledgeable about these. If merged, there would be an enormous effort to integrate the SSB legal, regulatory and policy guidelines into the DOB, requiring statutory and rule changes and a significant effort to re-write regulations and policies and procedures and requiring a significant amount of effort and expense in re-training senior leadership, mid-level management, examination staff and legal and corporate staff of DOB which could take years and millions of dollars, something we do not believe was considered or envisioned by the Staff Report. The Comptroller of the Currency (OCC) took years and thousands of man hours to do the same thing when Congress moved thrifts under the authority of the OCC.

Choice for Texas is good

Having a choice of state banking regulators and charters are important options for an innovative and business friendly state like Texas and is another substantive legal characteristic that sets Texas apart.

There is no cost to the Taxpayer to maintain separate regulators and charters since the TDSML is strictly funded by regulated institutions. If a merger were to occur, we are confident that there would be significant hidden costs to the state as a result of the above referenced integration effort.

Finance Commission structure works well with all three Agencies

The Finance Commission structure works well and provides oversight but allows independence and specialization among the three regulatory agencies it oversees. The Finance Commission's rejection of the Staff's recommendation in a formal vote should be a clear message to the Sunset Commission that the Staff report is misguided.

The complex nature of banking regulation makes conclusions like this recommendation difficult

With respect, I am certain that the Staff was trying to objectively analyze the current regulatory structure in arriving with its recommendation for merger; however, it is not a simple analysis since our businesses are so highly regulated and so complex, that it would take years and a specialist to understand the importance of the differences and the nuances involved in the banking and thrift businesses.

Indeed when two of the staff sat in on a portion of our examination by TDSML and listened to the complexity of the discussion between management and the examination regarding certain matters, including forward looking issues such as CECL, BSA and CRA changes, I was confident it was far above their understanding as it would be anyone not involved in the business.

We should strongly support the independence of both the DOB and TDSML

I have been involved in this business as an attorney for 30 plus years and understand it well. I was privileged to participate in a small group which re-wrote the Banking Code under Governor Bush's leadership and worked closely with the DOB staff in that effort.

I believe in competition and free enterprise and have been privileged to observe its positive effect on communities throughout Texas and elsewhere during my years of practice. While the DOB certainly can claim a much larger group of regulated institutions, I believe the TDSML provides a unique and appropriate counter-point and if you will, competitive regulatory scheme much like the choice the industry has between FDIC and Federal Reserve as primary regulators.

The Mortgage Regulation Function of TDSML is another compelling reason to maintain the separate existence of TDSML

The Staff Report says little about the important mortgage regulation function the TDSML exercises. Today I understand that the TDSML licenses and regulates 32,000 mortgage industry participants. This is an extremely important function which again requires the special knowledge of the TDSML to effectively regulate and stay abreast of the unique issues facing participants in that industry.

TDSML promotes creativity and innovation and Texas SSBs are some of the best Banks in the US

The Banking industry is challenged by the need for innovation and the SSBs in Texas are some of the most unique and profitable business models in the industry. Many focus on very specific customer segments that are not necessarily characteristic of the typical community bank, but provide great products and services to their chosen markets. The TDSML management for decades has shown a willingness and indeed encouraged innovation and thoughtful development of specific niches and markets, regardless of geographic boundaries or the typical community bank. This receptive and flexible regulatory attitude should be preserved and celebrated for Texas. The Texas State Savings Bank is by no means a "dying industry".

In sum, I believe following the Staff's recommendation to merge TDSML with DOB would be a giant step backward for Texas.

Respectfully Submitted,

Patrick J. Kennedy, Jr.