



Jennifer J. Johnson, Secretary
Board of Governors
The Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C.

Re: Reserve Requirements of Depository Institutions, Docket No. R-1262
Bankers' Bank Exemption from Reserve Requirements

Dear Ms. Johnson:

We thank the Board of Governors of the Federal Reserve System for the opportunity to comment on: Regulation D - Reserve Requirements of Depository Institutions [R-1262]. I am President and CEO of the Bankers' Bank Northeast located in the First Federal Reserve District in Glastonbury, Connecticut. Our bank is a member of the Federal Reserve System since September 8, 1998, the day we opened with a bankers' bank charter issued by the State of Connecticut. Our bank is FDIC insured and is a member of the Federal Home Loan Bank of Boston.

As a bankers' bank, we provide a total of 23 services to banks in New England and the State of New York. Most of our client banks are located within the Federal Reserve's First District. We are one of the youngest of the 21 bankers' banks; however, we currently do business with 160 client banks which amounts to 30% of the community banks in our market. Our core services include Cash Letter clearing and settlement, Fed Funds-as-agent Investments, Coin and Currency vault and delivery, International Payments, Funds settlement services encompassing an OFAC compliance regimen and Commercial Loan participations.

The original founders of the Bankers' Bank Northeast, a group of community bankers and related parties, approached the Connecticut Department of Banking in the mid 90's to request that a special charter be granted to form a bankers' bank. Our intention was to provide bank-to-bank services under the stipulation that we: 1) be owned by banks, 2) provide services only to banks and/or to banks' employees, officers and/or directors, and 3) not do business with the general banking public. Our charter was created by the Connecticut Legislature to provide authority and impose restrictions similar to the precepts of existing bankers' bank at the time the statute was enacted. Accordingly our State statute has wording that is very similar to language set forth in section 19(b) of the Federal Reserve Act. The "bankers' bank concept" was embraced because it provides an effective and efficient means for community banks to receive services that enable them to compete with large depository and other financial

institutions. It was widely agreed that community banks are beneficial to the well being of the general banking public and accordingly an entity designed to assist smaller banks to compete was deemed to be of significant benefit.

Of note is the statistic that the existing bankers' banks provide services to over 7,700 banks and bankers' banks list over 3,700 shareholder banks nationwide. These numbers indicate that our business plans and our unique structure are supported by the very banks that we service. And our client and shareholder bank ranks continue to expand especially in geographies such as the Northeast which are relatively newly serviced territories. Bankers' banks are a small subset of the total banking industry however we feel that we are significant players in the sense of the number of community banks that we serve.

The Bankers' Bank Northeast concurs with proposals that would assist our ability to serve community banks by operating accounts for non-bank entities that in turn would facilitate service to our client banks. However, we would oppose any change that would weaken the basic concept of a bankers' bank. Enabling a bankers' bank to fully compete with its shareholders and/or client banks would weaken that concept. Bankers' banks would lose a unique and significant tenet of our business strategy. As a former correspondent banker at a large bank, I saw firsthand the absolute refusal of community bankers to seek services from large bank competitors. The best example is the fear of community banks of engaging in commercial loan participations with large banks. Their fear was well founded in the sense that if they turned to a traditional correspondent for an over-line [participation], they were likely to lose the complete commercial relationship because large banks could "do the whole credit". These large banks could also offer cash management services that the community bank could not offer competitively. The advent of bankers' banks has provided a solution for such a dilemma.

Since our authority to operate as a bankers' bank is issued by the State of Connecticut, and since we are limited by the state charter, we could be at a competitive disadvantage to bankers' banks that are managed solely in compliance with Federal Reserve regulations if the Federal Reserve adopts its proposal and expands that authority. Therefore, we would request that the Federal Reserve provide early indications of requests for expansions of servicing capabilities by publishing a notice in the *Federal Register* and offering the public an opportunity to comment on any proposed expansion. Early notice also would allow us to seek State authorization to keep pace with such changes. Timely notice is especially important since the Federal Reserve does not intend to publish standards by which it would determine compliance on a case by case basis.

We trust that there will be no change to the Federal Reserve's stance which does not require banks who comply with the definition of a bankers' bank to maintain reserves. Bankers' Bank Northeast has opted to take advantage of the Federal Reserve's program to choose not to pay reserves. Although we accordingly do not enjoy the benefit of access to the Discount Window, we are able to pass on the savings to our client banks by not requiring that they pay reserves on the collected dollars on deposit with their bankers' bank. We have been able to find other liquidity resources to meet our short term

borrowing needs. We are pleased to pass on the benefit to our client banks that have already paid reserves on their deposits. The fact that we do not reduce the client banks' collected balances for reserve assessments reduces their required balances by approximately 10%. This feature of our service is particularly beneficial to our client banks since they are currently struggling with a reduced interest margin during this period of relatively high interest rates on deposits. We applaud the Federal Reserve's position which recognizes that bank-to-bank balances should not be burdened with reserves related to bank-to-bank balances.

Of significant concern to us is the fact that we have learned of banks who describe themselves as a bankers' bank in their marketing and business development efforts yet refuse to comply with the mandates of a true bankers' bank. We suggest that such banks be required to comply with not only the letter of the regulations but with the spirit of the rules which are designed to enable a specialized charter to assist community banks to grow and prosper without the threat of competition from their correspondent bank. We would ask that all the banking industry regulators take action in such situations to demand that the use of the designation "bankers' bank" be restricted to banks that meet the statutory and/or regulatory definition of a bankers' bank. Use of the term "bankers' bank" should be restricted to banks who have chosen to be owned by banks, to offer services only to other banks and to embrace the concept of serving only community banks so that they in turn can compete effectively with the largest financial institutions. We believe that bankers' banks are fulfilling a role that enhances the banking public's ability to enjoy a wide choice of banking institutions. We are proud that our client banks can offer more services; receive competitive pricing derived from bankers' bank provided economies of scale; and that they are trustful of our commitment not to compete with them.

Again, thank you for the opportunity to respond to the proposed change in regulation. Please contact me with your questions and/or comments.

Sincerely,

Peter J. Sposito
President and CEO