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J. THOMAS CARDWELL
COMMISSIONER

FOR INTERNAL REVIEW

March 31, 2011

Internal Revenue Service
CC:PA:LDP:PR
Room 5203
PO Box 7604
Ben Franklin Station
Washington, DC 20044

RE: **Notice of Proposed Rulemaking 146097-09**
(76 Fed. Reg. 1105 (January 7, 2011))

Dear Sir or Madam:

I write as the Commissioner of the Office of Financial Regulation of Florida (OFR) to express serious concerns regarding Notice of Proposed Rulemaking 146097-09. OFR is the agency responsible for the regulation of state banks, international banks and banking agencies chartered or licensed by Florida. We charter 171 banks with total deposits of nearly \$50 billion. We also regulate international banks and bank agencies having deposits of \$15 billion in Florida.

Florida, among other states, is home to significant non-resident alien (NRA) deposits. Our bankers tell us that most of these are stable long term deposits that play a significant role in funding our banks. These accounts have not been associated with money laundering or the conduct of illicit activities.

Although precise data is difficult to obtain, based on our conversation with and examination of banks we would estimate NRA deposits in Florida fall in a range of \$15 billion to \$20 billion. This includes both institutions we regulate as well as those regulated by the federal government and other states.

NRA deposits are often driven by a distrust of foreign economies and their governments by their citizens. Experience with inflation, devaluation, nationalization and corruption causes ordinary citizens quite rationally and appropriately to wish to put some part of their life savings in a safe place. The United States is such a place.

FINANCIAL SERVICES COMMISSION

RICK SCOTT
GOVERNOR

PAM BONDI
ATTORNEY
GENERAL

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OFFICER

ADAM PUTNAM
COMMISSIONER OF
AGRICULTURE

Florida's geographic location has long made it a hub for business, trade and travel for people from Central and South America. Governments and economies in the area are often unstable. This has resulted in banks located in Florida receiving significant deposits from people in the region who are attracted by the safety of our financial system and by Florida's geographic proximity.

Beyond economic concerns, citizens in some countries rightly distrust their governments. Dictators, demagogues, political partisans, corrupt state and local officials often act outside the law. Extortion, abduction, robbery and embezzlement are facts of life. Providing such governments with a list of assets is felt by their citizens to jeopardize not only their property but also their lives and those of their families and associates.

We have given substantial consideration to the consequences of the proposed rules and we have concluded that it will have serious negative impacts.

- THERE WILL BE A NEGATIVE IMPACT ON THE SAFETY AND SOUNDNESS OF INDIVIDUAL INSTITUTIONS.
- THERE WILL BE A NEGATIVE IMPACT ON STATE AND LOCAL ECONOMIES IN FLORIDA.
- THERE WILL BE A NEGATIVE IMPACT ON THE NATIONAL ECONOMY.
- THERE WILL BE A NEGATIVE IMPACT ON UNITED STATES POLICY AND THE INTERNATIONAL COMMUNITY.
- THE NEGATIVES OF THE RULE FAR EXCEED THE POSITIVES.

1. IMPACT ON THE SAFETY AND SOUNDNESS OF INDIVIDUAL INSTITUTIONS.

There are over 70 financial institutions in south Florida alone that have NRA deposits. Some have over 50% and some as much as 90% of their deposits NRA accounts. If there are substantial withdrawals of these funds in a relatively short period of time there will likely be liquidity issues that could cause the financial institutions to fail. This arises from the fact that financial institution deposits are loaned to borrowers. Those loans are illiquid. While bank regulators require institutions to have liquidity plans, there comes a point in major runoffs of deposits that there are not sufficient liquid funds to pay them. The financial institution then fails. We have a strong concern that the proposed rule will spark just such runoffs.

In addition to liquidity issues, loss of deposits will shrink the ability of institutions to make loans and engage in other financial transactions. With less in deposits there is less to lend. This negatively impacts the income of banks. Banks in Florida have been under significant stress following the financial and real estate crises we have sustained. Over the last two years we have closed 30 financial institutions. Approximately two-thirds of our banks are on our regulatory watch list. Many have impaired capital levels. Of the banks we regulate 64% were unprofitable last year. Of all banks headquartered in Florida both state and national 66% were unprofitable.

Continued losses erode capital and lead to further closures. Withdrawal of deposits will impair earnings and can lead to further failures. At best the process of returning to fiscal soundness will be delayed and made more tenuous. At worst some banks will not be able to earn their way out of their current difficulties and will fail.

The existing NRA deposits cannot be quickly replaced with domestic or other NRA deposits. Since NRA deposits are generally a low cost source of funds when a financial institution must replace them with higher cost funds the net interest margin is squeezed. The result is either greater losses or lesser profits depending on the condition of the bank. This is a particularly bad time to further reduce community bank earnings.

2. IMPACT ON THE STATE AND LOCAL ECONOMY.

The banks we regulate are largely community banks. It is well accepted that community banks are the key to small business lending. Withdrawal of deposits diminishes the lending capacity of financial institutions. It is generally agreed that bank deposits have a nine to ten times multiplier effect on lending depending on Federal Reserve reserve requirements. As an example withdrawal of \$10 billion of deposits could result in reduced lending capacity of \$90 billion or more.

The current Florida unemployment rate is 11.8%, one of the highest in the nation. Florida lacks the presence of large corporations or manufacturing facilities. It has a predominantly small business economy. The diminution of lending capacity of community banks is particularly harmful to the state's economic recovery.

The largest concentration of banks with NRA deposits is in the southern part of the state. The impact of diminished lending will be exacerbated there as it will fall on a more concentrated area. Currently, 19.4% of the residential mortgages in Florida are 90 days or more overdue and/or in foreclosure. This is the moment when Florida most needs to prime the lending pump particularly to small businesses. The proposed rule will materially undercut the effort to do so.

Reduction of NRA deposits will have a long term as well as a short term negative impact. The permanent departure of a class of stable deposits reduces the lending base into the foreseeable future.

Current federal policy has expressed a critical need to encourage small business lending, particularly by community banks. To promote this policy, Congress passed the Small Business Jobs Act which included a \$30 billion fund to provide Tier 1 capital for community banks to encourage their lending to small businesses. The implementation of this rule will directly undermine that policy.

3. IMPACT ON THE NATIONAL ECONOMY.

The effects of the proposed rule are not limited to Florida. We are advised by other state regulators that large NRA deposits from Latin and Central American countries are found in Texas and California.

Not only Latin and Central American accounts are at risk. Throughout the world many regimes and rulers operate outside the bounds of law as recent events underscore. We estimate that at least \$1.8 trillion dollars is deposited in United States financial institutions from abroad. This is in large measure because we are a nation of laws and because we offer stability that cannot be achieved in the home country of the depositor. This money comes in from all over the world. It is our experience that NRA accounts tend to locate in areas where kindred national groups live. Because national groups often concentrate themselves, when the money leaves it can have a magnified effect on a geographic area as it does in South Florida and its financial institutions.

4. IMPACT ON UNITED STATES POLICY AND THE INTERNATIONAL COMMUNITY.

Non-resident alien deposits are not taxed in the United States because it is in our economic interest to encourage them. These deposits help fund and provide capital for our economy. Not all foreign deposits are by non-resident aliens but the proposed rule is likely to discourage a meaningful segment of this \$ 1.8 trillion of such deposits. At a time we are seeking to increase lending, shrinking deposits hardly seems to be sound policy.

From the perspective of Florida we would observe that the ability of residents of our neighboring countries to place funds in a safe and secure environment helps to stabilize those countries. Creating conditions that make it difficult for persons in countries with unstable economies or governments to preserve stability in their own economic lives does not promote the long term interests of this nation.

5. THE NEGATIVES OF THE RULE FAR EXCEED THE POSITIVES.

Since the United States does not tax NRA deposits there is no need to collect account information for the purpose of seeing that domestic taxes are paid. We understand the reason for the rule is to promote international tax transparency so that this country will have access to information about our citizens who may be avoiding United States taxes by moving funds abroad.

There is nothing in the Background and Explanation of Provisions in the published notice that gives any indication of the extent to which the rule will be of any benefit to the United States.

The asserted interests of the United States taxing authorities can be achieved by methods other than the blanket collection of the entire universe of non-resident alien deposit information with the authority to make it available to other governments. The United States has tax treaties with many countries. These treaties could provide for the reciprocal exchange of information on an appropriate case by case basis.

There is nothing in the rule to address confidentiality of the information. In a general “trust me” statement that the IRA will use its authority wisely will not be sufficient in the minds of depositors who already have a skeptical view of government. The rule creates room for doubt and it is that doubt that will cause deposits to leave.

The proposed rule treats a nuanced issue with what some would call a “meat ax” approach. It disregards obvious specific problems in favor of a generalized approach which might be

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convenient to administer and to advocate with others but causes substantial harm to a broad spectrum of institutions, regulators, individuals, and long established policies.

The rule does impose substantial regulatory burden on financial institutions and particularly on those which are small businesses. The options are to gather the information by hand or to invest in software or software changes. Cost will vary from institution to institution depending on the number of NRA accounts and the ability of existing software to carry out the task. Based on anecdotal information the cost could be many thousands of dollars for some institutions. The burden of the costs will be much higher on smaller institutions which have less revenue over which to spread those costs. It is in particular a burden to our many institutions which in the current environment are not profitable.

For the reasons stated above we believe that the proposed rule should be withdrawn.

If there are significant objectives that need to be addressed in the area of tax transparency that call for transmission of non-resident alien account information to the IRS an effort should be made to create a rule that achieves those objectives and also addresses the harms the current proposal creates.

At a minimum before proceeding further with the proposal an appropriate credible study should be undertaken. We need to make sure that we truly understand both the positives and the negatives of what will happen if the rule is implemented. The failure to do so can cause significant and in some cases irreversible damage to many of the stakeholders in this issue.

Thank you for considering our views. If we can be of any assistance or provide any additional information please let me know.

Sincerely,



J. Thomas Cardwell