Testimony of

Tyrone Fenderson

On behalf of the

American Bankers Association

before the

Committee on Financial Services

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Chairman Hensarling, Ranking Member Waters, my name is Tyrone Fenderson, President and Chief Executive Officer of Commonwealth National Bank in Mobile, Alabama. I appreciate the opportunity to be here to present the views of the American Bankers Association (ABA) regarding regulatory relief for small financial institutions. The ABA is the voice of the nation's $14 trillion banking industry, which is composed of small, mid-size, regional and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits and extend more than $8 trillion in loans.

Commonwealth National Bank is a $60 million minority owned bank. We have 3 branches serving the Mobile area and extend $30 million in loans to our local community.

ABA appreciates the opportunity to be here today to talk about how the growing volume of bank regulation—particularly for community banks—is negatively impacting the ability of banks throughout the nation to meet our customers' and communities' needs. This is not a new subject, yet the imperative to do something grows every day.

Community banks are resilient. We have found ways to meet our customers' needs in spite of the ups and downs of the economy. But that job has become much more difficult by the avalanche of new rules, guidances and seemingly ever-changing expectations of the regulators. This—not the local economic conditions—is often the tipping point that drives small banks to merge with banks typically many times larger. The fact remains that there are 1,200 fewer community banks today than there were 5 years ago—a trend that will continue until some rational changes are made that will provide some relief to America's hometown banks.

Each and every bank in this country helps fuel our economic system. Each has a direct impact on job creation, economic growth and prosperity. The credit cycle that banks facilitate is simple: customer deposits provide funding to make loans. These loans allow customers of all kinds—

businesses, individuals, governments and non-profits—to invest in their hometown and across the globe. The profits generated by this investment flow back into banks as deposits and the cycle repeats—creating jobs, wealth for individuals and capital to expand businesses. As those businesses grow, they, their employees and their customers come to banks for a variety of other key financial services such as cash management, liquidity, wealth management, trust and custodial services. For individuals, bank loans and services can significantly increase their purchasing power and improve their quality of life, helping them attain their goals and realize their dreams.

This credit cycle does not exist in a vacuum. Regulation shapes the way banks do business and can help or hinder the smooth functioning of the credit cycle. Bank regulatory changes—through each and every law and regulation, court case and legal settlement—directly affect the cost of providing banking products and services to customers. Even small changes can have a big impact on bank customers by reducing credit availability, raising costs and driving consolidation in the industry. Everyone who uses banking products or services is touched by changes in bank regulation.

I would like to share some specific examples of how bank regulation has impacted consumers across the country:

- Another $500 million bank in Texas has had to take all lending discretion away from loan officers and rely exclusively on a numbers-driven computerized underwriting model for fear of inadvertently violating fair lending regulations. As a result they were forced to turn down a 30-year customer who has never been late on a payment who wanted to guarantee a loan to fund a new HVAC system to restore heat to his daughter's home. Another customer was denied a loan despite having fully paid 20 loans to the bank.
- In one case, the customer of an Oklahoma bank passed away. The customer's daughter had been living with the mother and supplementing her mortgage payments while she was alive. Upon the mother's death the daughter wanted to remain in the house and continue paying the mortgage. The daughter did not qualify to purchase the home under ability to repay standards. This left the bank with the choice of foreclosing on the home and evicting the daughter or ignoring its policy and making a non-QM loan. **Instead this bank decided to charge off the loan – taking an immediate loss – and allow the daughter to continue making payments on her deceased mother's loan,** recapturing portions of the loss as the daughter makes monthly payments.

These stories are common at hometown banks across the country. Community banks have always prided themselves on being flexible to meet the unique circumstances of their customers. But the inflexible rules, regulatory risk, and potential law suits have led to fewer loans, hurting customers and the communities they live in. This is why it is imperative that Congress take steps to ensure and enhance the banking industry's ability to facilitate job creation and economic growth through the credit cycle. The time to address these issues is now before it becomes impossible to reverse the negative impacts. When a bank disappears everyone is affected.

We thank Representative Luetkemeyer for introducing the CLEARR Act (H.R. 1233) and Chairman Neugebauer for introducing the Financial Products Safety Commission Act (H.R. 1266). We also thank Representative Barr for introducing the HELP in Rural Communities Act (H.R. 1259) and the soon to be introduced American Jobs and Community Revitalization Act. These measures are an important first step. We urge Congress to work together— Senate and House—to pass legislation that will enhance the ability of community banks to serve our customers.

More can and must be done. In particular, Congress can take action to ensure credit flows to communities across the country by:

- removing impediments to serving customers,
- improving access to home loans, and
- ensure proper oversight of the Consumer Financial Protection Bureau.

In the remainder of my testimony, I will highlight some specific actions under each of these that would help begin the process of providing meaningful relief to help community banks and help bank customers.

I. Remove Impediments to Serving Customers

Rules and requirements surround every bank activity. When it works well, bank regulation helps ensure the safety and soundness of the overall banking system. When it does not, it constricts the natural cycle of facilitating credit, job growth and economic expansion. Finding the right balance is key to encouraging growth and prosperity as unnecessary regulatory requirements lead to inefficiencies and higher expenses which reduce resources devoted to lending and investment.

Bank Testimonial:

An 80 employee bank in Massachusetts has had to hire an additional compliance officer and 3 additional software engineers over the past three years to address new documentation and compliance requirements.

The bank is forced to pass along a portion of these costs to customers in the form of fees and less favorable rates on loans.

The key to changing the consolidation trend is to stop treating all banks as if they were the largest and most complex institutions. Financial regulation and examination should not be one-size-fits-all. All too often, regulation intended for the largest institutions become the standard that is applied to every bank—Basel III being the most egregious. Such an approach only layers on unnecessary requirements that add little to improve safety and soundness, but add much to the cost of providing services—a cost which customers ultimately bear. Instead, ABA has urged for years that a better approach to regulation is to tailor bank supervision to take into account the charter, business model, and scope of each bank's operations. This would ensure that regulations and the exam process add value for banks of all sizes and types.

By eliminating unnecessary impediments to the natural credit cycle, Congress can help stem the tide of community bank consolidation driven by these unnecessary impediments which negatively impacts every community across the United States.

American Jobs and Community Revitalization Act

ABA supports Representative Barr's soon to be introduced American Jobs and Community Revitalization Act which contains a number of provisions that will reduce the burden on community banks in ways that make it easier for community banks to meet their customers' needs. In particular, this legislation would:

- **Require a review and reconciliation of existing regulations**. Congress should require a review and reconciliation of existing regulations that may be in conflict with or duplicative of new rules being promulgated by the banking agencies, or which in their application badly fit the variety of institutions that make up the banking industry.

- **Provide a longer examination cycle for community banks.** This bill would expand the number of banks eligible for an 18-month exam cycle for highly rated community banks. This would reduce significantly the resources required to deal with yearly examinations by the regulators. The Comptroller of the Currency, Thomas Curry, publicly stated such a change would reduce burden on well-managed community institutions and would also allow the agencies to focus their efforts on institutions that may present supervisory concerns.

- **Streamline currency transaction reporting.** Anti-money laundering efforts by financial institutions can be improved by eliminating needless currency transaction reporting through a "qualified customer" exemption to the Currency Transaction Reporting (CTR) rules. This would significantly reduce the more than 13 million CTRs filed annually, saving banks many hours each year in filling out unneeded and used forms.

- **Ensure Subchapter S banks are treated equitably.** Banks are required to build capital under the Capital Conservation Buffer requirements of the agencies' Basel III regulations. However, the current regulations do not take into consideration the unique cash flows applicable to S Corporation banks where income is calculated prior to consideration of distributions for payment of taxes arising from S Corporation activities. This puts S Corporation banks at a disadvantage when compared to C Corporation banks.

- **Improve Access to Home Loans.** This bill also contains a number of provisions to ensure consumers have access to home loans that are discussed further below.

CLEARR Act

ABA supports Representative Luetkemeyer's CLEARR Act which also contains a number of provisions that would lift or modify many requirements, better allowing community banks to meet the needs of their customers. In particular, this legislation would:

- **Reduce unnecessary and redundant paperwork.** This legislation would provide an exemption from the Gramm-Leach-Bliley Act's annual notice requirement for institutions that have not changed their privacy policies and only share personal information within the statutory exceptions, resulting in significant savings in mailing costs for banks across the country. Institutions that changed their privacy policies during the preceding year still would be required to provide privacy notices.

- **Ensure that both the costs and benefits are considered before issuing new regulation.** The bill also would require the Securities and Exchange Commission (SEC) to conduct an analysis of the costs and benefits, including economic benefits, of any new or amended accounting principle. Benefits to investors would have to outweigh costs before the SEC could recognize the principle.

- **Provide a longer examination cycle for community banks.** This legislation would also expand the number of banks eligible for an 18-month exam cycle for highly rated community banks.

- **Improve Access to Home Loans.** This bill also contains a number of provisions to ensure consumers have access to home loans that are discussed further below.

Tailor Regulation to a Bank's Business Model

In addition to measures mentioned above, the ABA also recommends that Congress ensure that regulation is tailored to a bank's business model. Time and again, I hear from bankers wondering why the complex set of rules, reporting requirements, and testing that are imposed upon the largest most diverse and global institutions become the standard applied to the smaller community banks in the country. The approach seems to be: "If it's the 'best practice' for the biggest banks it must be the best practice for all banks." Such an approach makes no sense in our diverse banking system with different business models and strategies.

Of course, the supervisory process should assure risk is identified and managed prudently. This risk assessment must be appropriate to the type of institution. In the aftermath of the financial crisis, the pendulum of bank examination has swung to the extreme—affecting every sized bank. Overbroad, complicated restrictions supplant prudent oversight. Inconsistent examinations hinder lending, increase costs, and create procedural roadblocks that undermine the development of new products and services to bank customers.

The banking agencies should move towards customized examinations that consider the nature of a bank's business model, charter type, and perhaps most important, bank management's success at managing credits, including a borrower's character, prior repayment history and strength of personal guarantees. In today's complex banking environment, an array of risk factors have a far greater impact on a banks' ability to serve its customers—as well as its likelihood to get in trouble—than asset size.

This proposal is an excellent starting point. Although no single piece of legislation could remedy all concerns about the current supervisory environment, this legislation would ensure that banks are regulated according to their business model.

II. Improve Access to Home Loans

The mortgage market touches the lives of nearly every American household. Banks help individual consumers achieve lifelong goals of homeownership by giving them access to the funding they need. Without home loans most Americans would not be able to purchase a home.

Banks are a major source of mortgage loans—holding more than $2 trillion in one-to-four family home loans on their books and originating others under government guarantees. In addition, banks support the housing industry with construction and development loans, and homeowners with home equity lines of credit. These critical services of banks results in more income and jobs in communities, along with a larger tax base for local governments.

It is painfully clear that new regulatory requirements have restrained mortgage lending and have made it particularly difficult for first-time homebuyers to obtain a home loan. The complex and liability-laden maze of compliance has made home loan origination more difficult, especially for borrowers with little or weak credit history. Over-regulation of the mortgage market has reduced credit available to bank customers, raised the cost of services, and limited bank products. The result has been a housing market still struggling to gain momentum.

Congress can help reduce needless impediments to mortgage lending that have constrained the banking industry's ability to help first-time homebuyers and dampened the growth of prosperity across the nation's communities. For example, Congress should:

Treat Loans Held in Portfolio as Qualified Mortgages:

The Dodd Frank Act (DFA) is very restrictive in its definition of "ability to repay" (ATR) and this is having a detrimental impact on the market and consumer access to credit. In fact, the Consumer Financial Protection Bureau (CFPB) has been forced to delay implementation of some aspects of the rule which would eliminate balloon loans. These loans, which are in virtually all cases held in portfolio, are a useful and in-demand product for many customers, particularly those in rural areas seeking smaller dollar loans and those that do not meet secondary market eligibility requirements. It helps bank manage interest rate risk, and without tools like this some borrowers would not have access to mortgage loans at all. While the bureau has recently proposed expanded exemptions for smaller lenders serving rural and underserved areas, more relief is needed for lenders and borrowers in all areas of the country.

Bank Testimonial:

A $500 million Massachusetts bank noticed a spike in loan declines to women. Further investigation revealed a number of women who were attempting to buy their family home to settle a divorce and stabilize their family. These women had often recently reentered the workforce, and therefore did not have the work history required to meet ATR requirements.

Previously the bank would have written these loans, recognizing that she would do what is necessary to keep the home provide stability for her family. The ATR requirement does not allow this flexibility.

ABA is thankful for the CFPB's work to address this issue, but legislation is needed for a real fix. Both H.R. 1233 and the American Jobs and Community Revitalization Act would deem ***any*** loan made by an insured depository and held in that lender's portfolio as compliant with the Qualified Mortgage rule under the DFA (so long as the loan is not sold). The Qualified Mortgage or QM label is given to loans which can be shown to meet the qualifications of the Ability to Repay provisions of DFA. Loans held in portfolio are, by their very nature, loans which can be repaid because the bank takes **all** the risk that the loan might default. A bank would not stay in business very long if it made and held loans on their books that cannot be repaid. The approaches taken in both of these bills common sense approaches to showing that a loan has been properly underwritten and meets the QM and ability to repay requirements of the DFA.

Eliminate the Excessively High Life-of-Loan Liability:

Not only are the rules complex and liability-laden, the level of liability is both high and often extends for the life of the loan. A liability with such a long life will give any lender pause when considering any but the lowest-risk borrowers. Why should ability to repay liabilities hang over a lender's business for twenty years or more into the life of a thirty-year loan? Common sense suggests that any mortgage loan that has remained current for a number of years has certainly demonstrated the borrower's ability to repay. Congress should replace the ATR life of loan liability with a more reasonable term so that liability ends after a loan has performed for a reasonable number of years.

Mandate a Study of the Basel III Capital Requirements Impact on Mortgage Servicing Assets:

Implementation of Basel III is disrupting the market for mortgage servicing rights by imposing punitive capital requirements that are causing many banks to sell these assets, usually to nonbank mortgage servicing firms that have little connection with the original borrowers. ABA supports the American Jobs and Community Revitalization Act which requires the banking regulators to study the overall impact of these requirements on the safety and soundness of the banking system, including the impact on the value of such assets as sales are required; the financial stability of nonbank purchasers of mortgage servicing assets; and the risks posed by shifting servicing duties from the banking industry to nonbank entities. The regulators should be required to report to the committees of jurisdiction within one year on recommendations for legislative and/or regulatory changes to address concerns identified by the study, and steps to implement the provisions should be halted until Congress has the opportunity to review the study and act.

III. Ensure proper oversight of the Consumer Financial Protection Bureau

The banking industry fully supports effective consumer protection. We believe that Americans are best served by a financially sound banking industry that safeguards customer deposits, lends those deposits responsibly, and processes payments efficiently.

Fair service to our banking customers is inseparable from sound management of our banking business. Yet despite this axiom, the Dodd-Frank Act erected a Bureau that divides consumer protection regulation from safety and soundness supervision. It is for this reason I and my fellow bankers, from banks small to large and everywhere in between, have common cause to advocate for improvements to assure this new Bureau is accountable to the fundamentals of safe and sound operation, to the gaps in regulating non-banks that motivated financial reform, and to the principles of consistent regulatory standards consistently applied. In order to accomplish this ABA recommends that Congress:

Ensure proper oversight of the CFPB:

ABA supports H.R. 1266, introduced by Chairman Randy Neugebauer, which would replace the position of Director of the CFPB with a bi-partisan 5-member commission, similar to other financial regulatory agencies. ABA has long supported the commission concept and believes that a commission structure is appropriate to address the extremely broad authority of the Bureau's Director. We believe that the commission approach would broaden the perspective on any rulemaking and enforcement activity of the Bureau, and it would provide needed balance and appropriate checks in the exercise of the Bureau's authority.

We urge Congress to require the commission to include members with consumer finance business experience and direct safety and soundness regulatory expertise. We believe this expertise provides an important and necessary perspective as standards are set and enforcement activities are undertaken.

Establish an Effective Appeals Process to the Definition of a Rural Area:

The definition of rural and underserved is critical and can dramatically affect banks and the communities they serve. The CFPB has already recognized this and has used its DFA discretionary authority to exempt certain loans from the qualified mortgage rule. This has been very important to accommodate community banks that make short-term balloon loans as a means of hedging against interest rate risk. However, the exemption applies only if, during the preceding calendar year, the creditor extended more than 50 percent of its total covered transactions that provide for balloon payments in one or more counties designated by the Bureau as "rural" or "underserved." Thus, the definitions used can be limiting and hurt mortgage customers that are inevitably in counties that may have been inappropriate excluded.

ABA supports H.R. 1259 and the American Jobs and Community Revitalization Act which would direct the CFPB to establish an application process to have an area designated as a rural area if it has not already been designated as such by the Bureau. An appropriate exemption process is critical since it would help to assure that whatever definition of rural is ultimately used by the CFPB, there would be an avenue to apply to the Bureau to extend the definition of rural in those inevitable cases where a county may have been inappropriately excluded.

Conclusion

Community banks have been the backbone of hometowns across America. Our presence in small towns and large cities everywhere means we have a personal stake in the economic growth, health, and vitality of nearly every community. A bank's presence is a symbol of hope, a vote of confidence in a town's future. When a bank sets down roots, communities thrive. We thank Representatives Barr, Luetkemeyer, and Neugebauer for introducing the American Jobs and Community Revitalization Act, the CLEARR Act, the Financial Products Safety Commission Act and the HELP in Rural Communities Act. These measures are an important first step. We urge Congress to act now and pass these pieces of legislation to help turn the tide of community bank consolidation and protect communities from losing a key partner supporting economic growth.