TESTIMONY

OF

OLIVER IRELAND

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

OF THE

UNITED STATES HOUSE OF REPRESENTATIVES

COMMITTEE ON FINANCIAL SERVICES

EXAMINING LEGISLATIVE PROPOSALS TO REDUCE REGULATORY BURDENS ON MAIN STREET JOB CREATORS

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Chairman Neugebauer, Ranking Member Clay, and members of the Subcommittee, my name is Oliver Ireland. I am a partner in the financial services practice of the firm Morrison & Foerster LLP here in Washington DC. I have more than forty years' experience as lawyer in the area of the regulation of banking institutions. I spent more than twenty-five years as an attorney in the Federal Reserve System, including fifteen years as an Associate General Counsel at the Board in Washington, working on a wide range of issues. Since leaving the Federal Reserve, I have spent fifteen years in private practice representing banks and other financial institutions. I am pleased to be here today to address legislative proposals to improve our system for regulating banking institutions.

In this hearing, the Subcommittee is considering seven different proposals that cover a broad range of issues. My testimony will focus first on the most significant proposals where I believe that I can offer the most value to the Subcommittee, but I will address all of the proposals and will be happy to answer questions on any of the proposals to the best of my ability. First, however, I would like to express my support for the Subcommittee's continued efforts to examine the bank regulatory system at this time. It is important to seek improvements as the economy heals, as well as in times of stress. Significant disruptions to our banking system almost always trigger legislation designed to address the problems that led to those events as they are perceived at the time. Later on, with the benefit of hindsight, it often becomes apparent that our bank regulatory system has become unnecessarily complex and constraining, whether due to the remedial legislation or to the normal evolution of banking services and markets.

The most recent financial crisis was followed by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which was enacted more than five years ago. Although that Act is still in the process of implementation, it is not too early to look again at our regulatory system to see whether we have appropriately balanced caution and restraint with the ability to innovate and to provide financial services to consumers and businesses.

The proposals that the Subcommittee is considering today include proposals dealing with lessening regulatory burdens on smaller banking institutions, streamlining the registration of mortgage loan originators, providing greater transparency and oversight into the budgetary processes of the National Credit Union Administration and the Office of Financial Research, and fine tuning the new liquidity rules applicable to banks. As is the case with virtually all financial services legislation, the details of individual proposals could raise technical issues that need to be worked out, but I believe that the purpose of these proposals is constructive. In light of where we are in the legislative process, I will focus on the policy issues raised by these proposals, although I will be happy to discuss the details.

Turning to the individual proposals, H.R. 2896, the Taking Account of Institutions with Low Operation Risk Act of 2015, or the TAILOR Act, would require the Federal financial institution regulatory agencies with jurisdiction over banking organizations to take the risk profiles and business models of the institutions subject to regulatory actions into consideration in taking regulatory action, including issuing proposed and final rules as well as guidance and interpretations. Today, our banking system has evolved so that the business models of banking institutions have become increasingly varied and more specialized. While community financial institutions continue to focus on taking deposits and making loans in their communities, other, often far larger, financial institutions provide highly automated, nationwide services and provide complex financial products that their sophisticated business customers demand.

The result is that regulatory requirements have become increasingly complex and difficult for smaller institutions to understand and implement. Congress has repeatedly sought to address the issue of regulatory burden, particularly the burden on smaller institutions, through legislation such as the Paperwork Reduction Act, which was originally adopted in 1980, and the Economic Growth and Regulatory Paperwork Reduction Act of 1996, or EGRPRA. Regulators, too, have tried to implement risk-based requirements, but the burdens on smaller financial institutions continue to increase and to threaten both the economic viability of the small bank business model and access to financial services that meet the needs of the consumers and businesses that these institutions serve. Although Congress made conscious efforts to differentiate between the business models of small institutions and larger institutions in the Dodd-Frank Act, the end result does not leave smaller institutions unscathed. For example, smaller institutions that do not engage in activities regulated by new requirements, such as the Volcker Rule, may nonetheless have to understand the new rules in order to confirm that the rules do not apply to them. The need to review hundreds, or thousands, of pages of *Federal Register* publications cannot help but divert resources from serving main street customers. In addition, the costs of compliance efforts that are relevant to these institutions are spread over a relatively smaller base and, therefore, the burden of the regulatory requirements is relatively higher. It is the customers of these institutions that ultimately bear the burden of new regulatory requirements. The TAILOR Act is another effort to raise regulators' awareness of these burdens, and it should be adopted.

H.R. 2987, the Community Bank Capital Clarification Act, would refine the grandfathering provisions of the Collins Amendment in Section 171 of the Dodd-Frank Act. As one of the provisions of the Dodd-Frank Act that sought to lessen the potential burden that the provision would create on smaller institutions, the Collins Amendment, which set minimum capital requirements and disallowed certain instruments from consideration as capital, grandfathered capital instruments issued before May 19, 2010 for depository institution holding companies with total consolidated assets of less than $15 billion as of December 31, 2009. H.R. 2987 would extend the grandfathering provision to holding companies with assets that were in excess of $15 billion on December 31, 2009, but that fell below that level at a later date. H.R. 2987 does not change the date of the issuance of the original instruments and, therefore, does not open the door to evasion of the original requirement. This is a common-sense refinement of the original grandfathering provisions, and it demonstrates how attention to detail can have significant benefits for individual smaller institutions.

H.R. 2473, the Preserving Capital Access and Mortgage Liquidity Act, would amend the Federal Home Loan Bank Act to broaden the membership criteria to allow credit unions to become members of the Federal Home Loan Banks, even if the credit unions do not meet the requirement that residential mortgages represent at least ten percent of the credit unions' assets. H.R. 2473 would also broaden the collateral on which long-term advances could be made by Federal Home Loan Banks to credit unions to include secured loans to small businesses, agriculture and community development activities. The combined effect of these changes would be to expand the availability of Federal Home Loan Bank credit to fund loans for small businesses, small farms and community development. Access to additional sources of funding for loans for these purposes can only promote small businesses, small farms and community development.

H.R. 2121, the SAFE Transitional Licensing Act of 2015, would amend the S.A.F.E. Mortgage Licensing Act of 2008 to provide that a registered loan originator shall be deemed to be state licensed for a transitional 120-day period when moving from a depository institution, a depository institution subsidiary or an institution regulated by the Farm Credit Administration to a nonbank originator or from one state to another state. Making it easier for mortgage originators to change jobs should make the job of mortgage originator both more attractive and more competitive. I understand that discussions among interested parties may suggest revisions to ensure that H.R. 2121 achieves its intended purpose. I urge the subcommittee to consider any appropriate changes.

H.R. 2287, the National Credit Union Administration Budget Transparency Act, would provide greater transparency in the National Credit Union Administration's budgeting process. While the National Credit Union Administration is an independent agency and is self-funded, greater transparency can provide discipline from public accountability, without jeopardizing the agency's policy independence.

H.R. 2209 would amend the Federal Deposit Insurance Act to clarify that municipal obligations that are liquid, readily marketable and investment grade are considered to be Level 2A assets for purposes of the Liquidity

Coverage Ratio rules. The Liquidity Coverage Ratio rules require larger banks to calculate outflows and inflows of funds under specified assumptions over a thirty-day period. A covered bank is required to hold high-quality liquid assets to meet any outflows that are not offset by inflows under the rules. High-quality liquid assets are divided into three classes—Level 1 assets, Level 2A assets and Level 2B assets. Level 2A and Level 2B assets are both discounted and capped out of concern that they will represent less reliable sources of liquidity than Level 1 assets.

At larger banking institutions, the Supplementary Leverage Ratio discourages the holding of high-quality liquid assets, which yield a relatively low return, because it imposes the same capital charge on those assets as it imposes on less liquid, but higher yielding, assets. Conversely, the designation of assets as high-quality liquid assets under the Liquidity Coverage Ratio rules encourages the holding of the designated high quality liquid assets. Therefore, the designation of assets as high-quality liquid assets may significantly improve the demand for, and hence the marketability of, those designated assets and reduce the costs to issuers of those assets. Municipal obligations are not considered to be high-quality liquid assets under the current Liquidity Coverage Ratio rules. The Board of Governors of the Federal Reserve System has proposed to include some municipal obligations as Level 2B high-quality liquid assets subject to specific limitations.

H.R. 2209 would short cut the agency rule writing process and provide municipal obligations with more favorable treatment than has been proposed. Although the precise characterization of assets within all tiers created by the Liquidity Coverage Ratio rules is, in part, a factual question based on market conditions and historical performance of the assets, there is also something of a self-fulfilling prophecy component to the designation process. The demand generated by the designation itself may create liquidity, and result in a lower yield on these assets and lower-cost funding to the governmental entities issuing them. Accordingly, in order to assure an efficient market for municipal obligations, it is important that those obligations receive the appropriate classification in the rules, taking into account the benefits in marketability and liquidity that will flow from the designation of those assets as high-quality liquid assets.

Finally, H.R. 3340, the Financial Stability Oversight Council Reform Act, would subject the Office of Financial Research in the Department of the Treasury, which was established by the Dodd-Frank Act in conjunction with the Financial Stability Oversight Council in order to provide support to the Council, to the appropriations process and would subject any rule writing by the Office to notice and comment for not less than 90 days. The powers of the Council are broad, and Congressional control over the Council is limited at best. Subjecting the Office of Financial Research to additional oversight and public accountability could help provide accountability for actions of the Council in the vital area of financial stability and could help avoid precipitous actions in the name of financial stability that could have adverse consequences that outweigh the benefits.

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Thank you for your attention. I would be happy to address any questions that you may have.

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