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THE STATE OF RURAL BANKING: CHALLENGES AND CONSEQUENCES

HEARING

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER PROTECTION

OF THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING THE REGULATORY BURDENS ON RURAL BANKS

OCTOBER 28, 2015

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C O N T E N T S

WEDNESDAY, OCTOBER 28, 2015

THE STATE OF RURAL BANKING: CHALLENGES AND CONSEQUENCES

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U.S. SENATE, SUBCOMMITTEE ON FINANCIAL
INSTITUTIONS AND CONSUMER PROTECTION,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee met at 10:04 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Patrick J. Toomey, Chairman of the Subcommittee, presiding.

OPENING STATEMENT OF CHAIRMAN PATRICK J. TOOMEY

Chairman TOOMEY. The hearing will come to order.

Without objection, the Chair is authorized to declare a recess of the Committee at any time necessary. The Chair now—turns on his mic. The Chair now recognizes himself for the purpose of an opening statement.

First, I want to thank the witnesses for joining us. We will go through the introductions in a moment, but I appreciate your taking the time to share your unique insights into the topic that we are examining this morning. And the topic, of course, is the regulatory burdens on rural banks, and these burdens are not a new matter, but the fact is our rural banks and financial institutions are among the smallest financial institutions in the country, and they are struggling in the current regulatory environment.

I helped to start a small bank in the Lehigh Valley of Pennsylvania and the western part of New Jersey with the goal of lending to small businesses and local residents. And that was back in 2005, so I have some firsthand personal experience with the regulatory environment as it existed then. It has clearly gotten much worse in the meantime.

What I think sometimes folks from urban and suburban areas may not appreciate is the extent to which in rural areas a town's local bank is often a citizen's first, sometimes only exposure to the financial system. And these banks survive by offering exceptional service to these customers, personalized products, and fostering an ongoing, long-term relationship.

The fact is in small town across Pennsylvania and the United States, George at Bailey Building and Loan on Main Street still exists. Unfortunately, new regulations are straining the business of continuing to bank rural customers.

Congress and the President attempted to deal with threats to our financial system, threats that were posed by a handful of the largest institutions in the world in 2010 through Dodd-Frank. But, unfortunately, even the smallest institutions have been caught up in regulation that has resulted in more red tape.

In fact, in some ways this burden has been disproportionately felt by banks that are small and rural. Even though some of them have some of the healthiest balance sheets, business models, and relationships in the entire financial sector, the fact is compliance costs, at least a portion of them, are often fixed costs, and small institutions have a smaller revenue source with which to absorb those costs.

There's a striking example of the harm that has been happening in the very small bank and the new bank sector, and that is, the absence of new bank charters that have been issued recently. We have a chart here that depicts what has been happening across America. Between 2000 and 2009, the vertical gray bars on the graph reflect the new bank charters each year. And what you can see is that that number completely collapses and goes to zero after Dodd-Frank is passed. In fact, since 2010, only two de novo banks have been formed.

The red line is a measure of the amount of new regulations that have been imposed on financial institutions, and you can see the dramatic upward spike corresponds roughly but pretty well with the complete collapse of the formation of new banks. This I think is devastating. The fact that America no longer launches new community banks is devastating for Americans across the country.

But I understand why it is happening. It is hard for me to imagine taking the risk of starting a new bank today, having had that experience in the past, given the combination of this avalanche of new regulations that one faces and the artificial interest rate environment where interest rates are basically at zero and margins are so compressed.

Well, apparently I am not the only one that cannot imagine starting a new bank. Nobody is doing it anywhere in America. So we have destroyed de novo bank formations. That no longer happens in America. And we are forcing a stunning wave of consolidation among small banks. It started a long time ago, but it has been accelerating recently. And as we have this consolidation, we are not replacing these institutions with new startups.

A Harvard Kennedy School paper in 2015 said, and I quote, "Community banks' vitality has been challenged more in the years after Dodd-Frank than in the years during the crisis." And again I quote, "The rapid rate of consolidation away from community banks that has occurred since Dodd-Frank's passage is striking given that this regulatory overhaul was billed as an effort to end 'too-big-to-fail'."

The fact is in the absence of new community banks and the absence of a thriving small bank sector, we have less competition, less dynamism, and fewer financial services for men and women and small businesses who need these services.

So this Subcommittee, we have been working for some time now to try to provide some regulatory relief for the smallest financial institutions. We have had five hearings focused on community banks and credit unions, two others on credit access for small businesses. We had the Financial Regulatory Improvement Act of 2015 with dozens of measures designed to provide relief. I am proud to have authored several of these provisions in separate bills that got rolled into one, and I am very disappointed that we have not been able to get bipartisan support so that we can move this on the Senate floor.

I do want to also point out one particular industry that depends so much on the smallest of banks, and that is agriculture. It is very often the case in rural agricultural areas that there is only one financial institution—and it is often a very small community bank or credit union—that provides credit to the ag community to the ag community in that market. But these small institutions in the aggregate provide a huge percentage of all agricultural lending. This chart depicts that.

The light-green area on the top represents the percentage of all loans, agricultural loans, that are made by banks that are less than $1 billion in total assets, and you can see that is about half of all the loans. The dark-green area are loans that are made by banks of $1 to $10 billion, still quite small. Combined, you can see this is over 70 percent of all the loans that are made to agricultural America are made by small and very small banks. This is an absolutely essential part of the financial services industry for rural and agricultural America.

So the fact is while we have been unable to provide this regulatory relief, in my view, the burden is carried not just by financial institutions but the folks on Main Street and the folks in the rural communities who would otherwise be served by a more robust small banking market.

Our witnesses today represent institutions that have been unduly burdened by Dodd-Frank and other regulatory creep. I hope their views and suggestions will be taken into account as we continue to pursue ways in which we can relief that burden.

And, with that, I will recognize the Ranking Member, Senator Merkley, for his opening statement.

STATEMENT OF SENATOR JEFF MERKLEY

Senator MERKLEY. Thank you very much, Mr. Chairman, and thank you to all of you for bringing your frontline experience to this conversation.

Seven years ago, our economy plunged into a free fall that took us deeper than any crisis since the Great Depression, impacting both consumers and financial institutions across the country. And Congress responded with the Wall Street Reform and Consumer Protection Act to protect consumers and our economy, to prevent or decrease the odds of a similar plunge off an economic cliff.

Our economy has slowly bounced back, and the memory of the crisis is still fresh in the minds of many Americans, millions of whom lost their homes, they lost their jobs, they lost their retirement savings. And for this reason, there remains strong bipartisan support for reforming the activities of Wall Street, with nine in ten likely voters saying it is important to regulate financial services and products to ensure that they are safe for consumers.

That said, we all know that community banks and small credit unions did not cause the financial crisis. As legislators, then, we need to strike a balance, provide appropriate consumer protection from predatory products, while ensuring that community banks and credit unions can do their job providing credit in rural America.

The Democrats on the Banking Committee recognized that some regulatory relief was needed and joined together to propose just such a bill. We offered a path forward to ensure that rural areas can continue to depend on community banks for mortgages and agricultural loans and small business loans. A *Wall Street Journal* article paints a positive picture saying that in some ways community banks are the picture of health with loans balances, profitability, and increased number of loans held on portfolio. But we have all heard from our community banks about the challenges that they have with, as the Chairman described, regulatory creep, and that needs to be addressed, and thus the Democratic initiative.

Banks and credit unions in Oregon almost exclusively fall into the community and small financial institution categories, especially true of financial institutions that serve our rural communities, many of which have deep roots in small communities, from the Bank of Eastern Oregon—headquartered in Heppner with a population of 1,300; it has 13 branches and $325 million in assets—to Rogue Credit Union in southern Oregon—which has grown to have about $1 billion in assets, 15 branches, and is serving rural areas like Klamath County—and Mid Oregon Credit Union, which is headquartered in Bend, serving rural central Oregon, as well as Warm Springs Tribe. Mid Oregon has six branches and $213 million in assets. I think that these are representative of the types of institutions we would find all across America. And while I am familiar with the feedback from our Oregon community banks, I look forward to hearing feedback from all of you on the front line in South Dakota and Pennsylvania.

I am not going to go through the details of the Democratic bill that was designed to address many of the issues that we have been hearing from rural banks. I can submit those for the record.

Chairman TOOMEY. Without objection.

Senator MERKLEY. I want to turn to your experience. The caution I would have is against trying to use the challenges of banks in rural America as a wedge to restore the New York Wall Street casino operations that brought down America. That has been a choice strategy that we have been witnessing here on Capitol Hill, and that would be a mistake. Enabling essentially taxpayer-subsidized hedge funds to operate with our deposits and put the entire banking system at great risk would be absolutely no service to Americans in urban or rural America. Meanwhile, we stand united in wanting to address the types of issues that you will be identifying. Thank you.

Chairman TOOMEY. Thank you very much, Senator Merkley.

I am now going to recognize the gentleman from South Dakota, Senator Rounds, for the purpose of introducing one of the witnesses who is a constituent of Senator Rounds.

Senator ROUNDS. Thank you, Mr. Chairman.

Roger Porch grew up on a farm and ranch in West River, South Dakota, where both banks and towns are few and far between. For those who have never been there, West River is shortgrass country where cow-calf operations are the norm. It still takes a cowboy and a cow to raise a calf, and a banker needs to understand the land in order to serve the needs of his or her customers. Roger understands the geography of West River. He knows the land, and he knows the people.

I served with Roger in the South Dakota State Senate, and I found him not only reasonable but knowledgeable and a very concerned person with his constituents' needs always firsthand.

Roger graduated from Kadoka High School in 1969 and the University of South Dakota in 1974, and for those of us who graduated from South Dakota State, we put up with him anyway.

He returned to his family's ranch after college and operated it until 1995, when he started working at the First National Bank in Philip. He was elected to the South Dakota House of Representatives in 1984, served until 1990, and was Vice Chairman of the Ag Committee. He was elected to the South Dakota State Senate in 1990, where I first met him, where he served for 6 years chairing the Committee on Education, and he later served on the State Board of Education for 5 years.

Roger is currently the vice president and head of the loan department for the First National Bank in Philip. He sits on the Board of Directors of the Philip Health Services, which operates a clinic, a hospital, a nursing home, and is the secretary of the Philip Charities, which is the local economic development organization. He and his wife, Lois, have been married for 44 years, have three children and five grandchildren, last count. They still own and operate the family ranch which consists of about 3,500 acres of pasture and farmland. I know that our Committee can benefit from Roger's long experience and use his testimony to help make it easier for rural bankers to effectively serve their customers.

Thank you, Mr. Chairman.

Chairman TOOMEY. Thank you, Senator Rounds.

At this time I would like to extend a warm welcome to all of our witnesses, and let me proceed with a brief introduction for our other witnesses.

We have with us Mr. Terry L. Foster, the executive vice president and chief executive officer of MCS Bank in Lewistown, Pennsylvania. And Senator Rounds just introduced Mr. Porch. Welcome to both of you.

Ms. Carrie Wood is the president and chief executive officer of Timberland Federal Credit Union in DuBois, Pennsylvania.

And Ms. Sarah Edelman is director of housing policy at the Center for American Progress.

Thank you all for joining us today. I will recognize each of you for a 5-minute oral summary of the testimony that you have submitted. Your full testimony will appear in the record, and then we will proceed to questioning. So thank you again, and, Mr. Foster, please proceed.

STATEMENT OF TERRY FOSTER, EXECUTIVE VICE PRESIDENT AND CHIEF EXECUTIVE OFFICER, MIFFLIN COUNTY SAVINGS BANK, LEWISTOWN, PENNSYLVANIA, ON BEHALF OF THE PENNSYLVANIA ASSOCIATION OF COMMUNITY BANKERS

Mr. FOSTER. Thank you, Chairman Toomey, Ranking Member Merkley, and Members of the Committee. My name is Terry Foster.

I serve as executive vice president and CEO of MCS Bank. We are a $137 million asset bank headquartered in Lewistown, Pennsylvania. We are a State-chartered mutual savings bank, and we were originally chartered in 1923. Our bank serves exclusively rural populations in the central part of the State. I have served in my current role at MCS Bank since 2009, but I have served the bank in other capacities for the past 20 years.

I would like to add that I have also been a customer of this very bank since I was a young boy.

I also serve as the current chairman of the Pennsylvania Association of Community Bankers and as a member of the Mutual Bank Council of the Independent Community Bankers of America. I wish to thank you for convening today's hearing and providing me with the opportunity to testify.

I want to state that my testimony is based upon my own experiences and observations as a rural community banker, as well as from the perspective of my fellow bank employees' dealings with our customers and stakeholders. I also speak from the perspective of a $137 million institution trying to preserve our ability to survive and maintain a presence in communities where local banking and service is so very important. I refer you to my written testimony for greater details on our bank, its history, staff, and markets, but I do think it is important to mention that and stress the fact that within two of the communities in which we have branches, we are the only bank in town.

By their nature, rural markets create unique efficiency challenges in terms of serving dispersed populations as compared to the more densely populated suburban and urban areas. The fact that MCS Bank, at just $137 million in assets, operates five full-service branches to reach our customer base illustrates this point. Every dollar of cost rural institutions must incur to maintain compliance with new or heightened regulatory requirements disproportionately impact institutions like mine.

Unique population dynamics in the rural markets call for specialty servicing knowledge and are a critically important reason that community banks in rural markets do survive. In our market, we serve a unique population in the "plain sect" or the Amish community.

Amish, for those of you who are not familiar, live simple agrarian existences, avoid the use of modern technologies, including electricity and automobiles. In place of automobiles, they travel by horse-drawn buggy. Because of their social and religious conventions and aversion to technology, serving this demographic takes a keen, local understanding of this community to meet its members' needs, a community that will never be understood by banks headquartered in suburban or urban centers and whose needs are not a part of the equation when branch consolidation or closure decisions are being contemplated.

I like to tell the story of how in the wake of a large regional bank abandoning a rural community with a high concentration of Amish residents we were able to figure out a way to restore local banking. The loss of this branch was devastating to the community's residents and businesses, particularly to the Amish residents whose transportation limitations created an unusual hardship by forcing them to travel long distances to another community to do their banking at a branch to which their account servicing was transferred.

MCS Bank worked with community leaders and business owners, and eventually we partnered with a local businessman to build and open a 530-square-foot branch within his family's building supply and hardware store. Today this branch is thriving, albeit much smaller, and supporting the community, and we have provided financing to the Amish community for such projects as the purchase of land for farm expansion and for the construction of a new retail store.

The potential loss by this particular community is just one example of situations that are playing out in communities across the Nation. I believe very strongly that the community banking industry is experiencing consolidation, particularly in rural markets, at an accelerating rate, for a host of reasons, but one being escalating compliance-related cost and complexities.

I argue that a great deal of time and resources we are devoting toward our efforts to comply with the letter of the laws and regulations, their complexities, and many inconsistencies have had a detrimental impact on our ability to serve our customers with both products and service delivery.

Has Dodd-Frank, for instance, impacted the products our bank offers? Absolutely. Since the introduction of QM and Ability-To-Repay, MCS Bank has discontinued offering balloon-type loans. With the volume of rules to interpret and implement, we had to focus our efforts on the most utilized of our mortgage products.

The required escalation of our compliance focus negatively impacts bank stakeholders such as community organizations, charities, et cetera, which have historically been the beneficiaries of our philanthropic efforts. The more time our people must devote to compliance is less time available for them to spend on volunteer and charitable endeavors. Increased regulatory costs also negatively impact the community by way of diverting financial resources away from community investment. As increased costs and other pressures work collectively to incentivize further consolidation, larger organizations with distant headquarters locations lack the appreciation and commitment to local needs in rural areas.

Are the theories behind consumer-focused regulations well intended? Absolutely. The notion of "ability-to-repay," as generally defined, has long been an underwriting practice of prudent community bankers and lenders, but the codification of such concepts into regulation is fraught with complexity, inconsistencies, and in some cases lacks logic. The unintended consequence is confusion, which ultimately leads to human error, additional costs, and potential examiner criticism. I refer the Committee Members to the detailed example in my written testimony for examples of human error situations that we have experienced.

Because the timing of today's hearing which coincides with the ongoing work to fully implement the rules of the new TRID requirements, I have also included some TRID examples in my written testimony.

The complexity involved in implementing TRID is taxing all parties involved. In our case, our third-party loan origination software provider's applications were not ready to go on October 3rd. As a result, our testing protocols were delayed. At this point, we are still determining if the new rules will allow us to continue to offer certain types of single-closing construction loans that have ARM features, which have benefits to consumers from the standpoint of cost reductions as well as reduced time and efficiency. It also impacts our ability to reduce our interest rate risk.

A final issue I wanted to share with the Committee is what I term "the flood map creep." Flood zone expansion has exposed our bank to reputation damage and instances of a formal consumer complaint being lodged with the Pennsylvania Department of Banking and Securities and ultimately a lost customer. Again, in my written testimony, I have provided a detailed example of this very instance.

In terms of recommendations, there are a number of bills that are in front of the Senate that we believe will provide some significant relief from many of the concerns that I raised, and I am sure other witnesses will also raise, and I cite a sampling of these specific bills and their favorable provisions within my written testimony.

Last, I would just again like to thank you for the opportunity to testify today, and I do hope that my comments will be beneficial to the work of the Subcommittee.

Thank you.

Chairman TOOMEY. Thank you, Mr. Foster.

Mr. Porch.

STATEMENT OF ROGER A. PORCH, VICE PRESIDENT, FIRST NATIONAL BANK, PHILIP, SOUTH DAKOTA

Mr. PORCH. Senator Rounds, thank you for that kind introduction. Chairman Toomey, Ranking Member Merkley, and Members of the Committee, my name is Roger Porch, and I am a vice president at First National Bank in Philip, South Dakota. I would like to thank you for affording me the opportunity to appear before you this morning to share some information about regulatory challenges faced by rural banks. My hope is that we can find some regulatory relief that will help community banks across the country. More importantly, however, we hope that we can, by making credit more readily available to those who live in rural areas, sustain our lifestyles and expand local economies.

The area in which I live—western South Dakota—is highly reliant upon agriculture and tourism, and we are doing well. But we take nothing for granted and are pleased to be here this morning.

My bank is headquartered in Philip, South Dakota, and we have one branch in Faith, South Dakota, located 85 miles to the north. We are a $250 million bank and serve a large area of western South Dakota. We have customers as far west as Wyoming and south to Nebraska. First National Bank is privately owned and has successfully served the needs of our trade area for over 100 years.

We live by the motto, "Partners in Banking." Our principal scope of business is the financing of farmers and ranchers with lines of credit and real estate and machinery loans. However, excessive, unfocused regulations are changing the way we do business.

The ability to meet local needs has not been easy with the increased regulatory costs and second-guessing by bank examiners. During the last decade, the regulatory burden for community banks has multiplied greatly.

In my testimony today, I would like to make the following three points: unnecessary regulatory burden limits banks' ability to serve their customers; these challenges have real costs for our banks and the communities they serve; and then some commonsense solutions which would help alleviate this burden.

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 growth, facilitating credit, and economic expansion. It has been noted by others that regulatory cost as a percentage of overhead has increased. Specifically for First National Bank, we spent $220,000 on regulatory expense, which is 19 percent of overhead. Looked at differently, it is approximately 7.5 percent of our bottom line, including salaries.

Today First National Bank does not make home loans. The avalanche of new mortgage regulations is too complex and costly to comply with. The added cost and risk of making these loans is not something our bank can justify. The economic life of rural America depends upon financial products and services that only community banks provide. By forcing many banks out of mortgage lending, significant harm is done to the rural communities that bankers are trying to serve.

In rural areas, an appraiser is difficult and sometimes impossible. For ag property up to $1 million, we can get by with an inhouse evaluation, which works quite well. For larger appraisals, we might find ourselves waiting several months for a certified appraiser to complete the appraisal. In certain cases involving homeownership, an appraisal might not be available.

Our main scope of business is lending operating money to ranchers and farmers. Although we do use projected cash-flows in our annual credit analyses, we consider ourselves equity lenders. We measure equity for each customer once a year. If we are required to rely on cash-flow analysis, we could possibly find ourselves in the situation of not being able to loan operating money to ranchers and farmer with equity in the millions.

The Consumer Financial Protection Bureau is inquiring into overdraft procedures to determine how those practices are impacting consumers. First National Bank considers itself an "ad hoc" bank, meaning we generally cover overdrafts rather than return checks. We know our customers and feel that they can best meet their needs.

As an example of burdensome regulation, 25 years ago the call report that we submitted was less than 10 pages long. Today for our bank it is 86 pages.

Competition from nonbank lenders is an ongoing problem. Farm Credit System and credit unions enjoy special tax treatments giving these institutions a competitive advantage.

I believe my time in front of this Subcommittee would be wasted if some possible solutions were not offered, and so in that light then, I believe that HMDA rules could be relaxed to allow rural community banks some flexibility before the rules apply.

With respect to appraisers, there might be some relaxation of requirements in becoming certified. We would request that there be some directive given to bank examiners in the area of cash-flow lending versus equity and collateral-based lending.

For rural community banks, we hope that account overdrafts can be managed internally. We know our customers. And we would ask that call reports be simplified to reflect a bank's business model and size. And I understand that this is not the time nor place to take up the issue of Farm Credit and credit unions, but the issue does need to be noted.

We ask for regulation and oversight that is truly beneficial to rural consumers who rely on local banks for credit. The focus should be on enforcing existing laws rather than creating new rules and regulations that threaten banks' future existence. Rural banks can compete, but they cannot compete while burdened with red tape and unnecessary, unfocused regulations. It is not fair to local banks and the communities they rely on.

At the end of the day, this is not about banks. It is not about First National Bank in Philip. It is about people. It is about the communities and lifestyles of those who populate rural America. We have a unique opportunity this morning to begin the process of effecting change which will truly help the residents of rural America.

I look forward to your questions. Thank you.

Chairman TOOMEY. Thank you, Mr. Porch.

Ms. Wood, please proceed.

STATEMENT OF CARRIE WOOD, PRESIDENT AND CHIEF EXECUTIVE OFFICER, TIMBERLAND FEDERAL CREDIT UNION, DUBOIS, PENNSYLVANIA

Ms. WOOD. Chairman Toomey, Ranking Member Merkley, and Committee, thank you for the opportunity to testify at today's hearing.

I am Carrie Wood, president and CEO of Timberland Federal Credit Union, a $60 million credit union located in DuBois, Pennsylvania. We serve 9,800 members, over three-quarters of which are low-income. My 15 full-time staff and I work hard every day to help meet their financial needs.

As a small credit union in a rural area, we have to comply with many of the same regulations as the too-big-to-fail banks who caused the financial crisis. While my title is CEO, I am also the security administrator, the H.R. department, the compliance officer, the marketing department, the backup IT person, and the NMLS administrator. To keep up with the changes coming out of Washington, I have assigned a team of five staff, a full third of my total, from various departments across the credit union.

When this team is working on compliance issues, they are not serving our members. They are not helping them get loans. They are not providing financial counseling. They are not helping to improve our services. Every time a rule is changed, my credit union and members incur costs. We must make the time to understand the new requirement, determine if it applies to us, modify our computer systems, update our internal processes, properly train our staff, design and print new forms, and produce materials to help our members understand the new requirement.

Rules are often changed in the name of consumer protection, but when regulators make it harder for me or more expensive to serve my members, that is not consumer protection.

This constant churn of new regulatory requirements takes a hit on our bottom line, which for a not-for-profit like us directly affects our members and our service. It has also kept us from entering new markets.

Our members want us to offer small business loans, but we are hesitant because of the regulatory and statutory restrictions in place today. We have also delayed our entry into indirect auto lending for similar reasons.

On top of all that, the CFPB has added an entire new level of regulatory anxiety for my credit union and others like us. A recent example is the TILA–RESPA Integrated Disclosure forms.

We have known TRID is coming down the pipe for some time, and we worked to prepare for it. TRID is a complicated rule, and the CFPB provided absolutely no transition time. One day we did things in one way; the next day, it was completely different. No transition period. No enforcement delay. No legal protections. As a small institution, when we ran into an unanticipated problem after we flipped the switch on the TRID forms, we were forced to manually input information, slowing down our process for our members and potentially exposing us to errors.

NCUA has said that their examiners are going to exercise tolerance for a reasonable amount of time. But I do not understand why Congress will not protect us from legal liability as we work the kinks out in our system.

Despite the ever-growing regulatory burden, we continue to help our members. And, in closing, let me tell you how.

When our members open an account, we offer a free credit review, and three members of our staff are trained to become Certified Financial Counselors to provide free credit counseling for our members.

We participate in a program called “Better Choice”, which is an alternative to payday lending. To participate in this program, we require our members to receive financial counseling, and we partner with our local Community Action to provide it. Timberland makes absolutely no money on this program. It is a member service.

Small loans are pretty common for us. Members request them to buy fuel, settle payday loans, buy an Amish mattress, among other things. I once did a loan for a man whose five granddaughters moved back in with him because his daughter lost her job. He needed $200 in a loan because the girls had contracted lice at school. He could not afford the treatments until his next Social Security check, and the girls could not go back to school until he took care of the problem. I have written car loans for members who have totaled their cars due to deer damage and once for a member who hit a horse. Public transportation is a struggle in central Pennsylvania, so my members need a car, which makes these loans very vital for us. Like all credit unions, the work we do at

Timberland helps families stay in their homes, members to hold jobs, and children to stay in school. We are a lifeline for our members.

My members need our credit union to be in a position to help them in these situations. Unfortunately, every rule makes it much more difficult for us to be there when they need it.

There is a reason that we are losing a credit union a day, and it is coming out of Washington in the form of ever-changing and ever-increasing regulatory burden. Again, your focus on the crisis facing small community financial institutions is critical, and I applaud your efforts.

Thank you for the opportunity to testify.

Chairman TOOMEY. Thank you, Ms. Wood.

Ms. Edelman, please proceed.

STATEMENT OF SARAH EDELMAN, DIRECTOR, HOUSING POLICY, CENTER FOR AMERICAN PROGRESS

Ms. EDELMAN. Thank you, Chairman Toomey, Ranking Member Merkley, and Members of the Subcommittee for the invitation to appear before you today. My name is Sarah Edelman, and I direct the housing program at the Center for American Progress.

Consumers living in rural areas rely on community banks to meet their credit needs. These banks provide vital support to the small businesses, farmers, and homeowners that make rural economies run. However, for decades, the number of community banks serving these areas has been in decline. The number of community banks peaked in 1984 and has declined ever since at a rate of about 300 banks per year.

There are many reasons for this trend, including changes in interstate banking rules that made it easier for banks to merge and consolidate, slower population growth in rural areas, and changes in the financial market. However, consolidation within the community banking sector has not been all bad news for banks or consumers.

First, the majority of consolidation has been voluntary and has taken place between community banks as opposed to large non-community banks buying smaller ones.

Second, even though the number of locally owned community banks has declined, the number of bank branches in rural areas has remained relatively stable over the years. There are only 5 percent fewer branches operating in rural areas today than there were before the financial crisis, mirroring overall national trends.

What is most important is that consumers and small businesses in rural areas have access to the credit they need in order to revitalize their economies.

In the wake of the Great Recession, recovery in the unemployment rate, job growth, and wage growth in rural areas have all lagged behind urban centers. And even as many housing markets are recovering, some rural markets are seeing further deterioration. The percentage of mortgaged homes with negative equity in rural counties increased from an average of 11 percent in the second quarter of 2011 to 20 percent in the first quarter of 2015.

Community banks, which represent more than 70 percent of bank branches in rural areas, are vital partners to businesses and farmers that can revitalize rural economies.

Unfortunately, much of the conversation in Washington about supporting community banks has focused on gutting the important financial reform laws put into place after the financial crisis. This approach is wrong-headed and overlooks the important fact that the challenges facing community banks have far more to do with shifting market dynamics rather than new regulation.

The overwhelming majority of community banks are already provided a host of exemptions to the Dodd-Frank Act, providing them with a competitive advantage over large banks and the flexibility to continue the relationship lending that is at the core of their business model.

Additionally, regulators have taken a number steps to make compliance easier for community banks and have worked closely with the industry throughout the rulemaking process. In fact, over the past 3 years, agencies have made changes to over 30 final rules based on feedback from community banks and credit unions. Regulators have done a good job of balancing the responsibility to protect consumers and the safety and soundness of the banking system while protecting access to credit.

The truth is that strong financial regulation supports a stable financial market. Banks of all sizes are more likely to fail or consolidate during periods of financial and economic crisis.

Right now, community banks appear to be getting stronger and healthier. Both smaller and larger community banks originated a larger share and number of home purchase mortgages today than they did in 2010. Last year, community banks increased their lending volume at almost twice the rate of larger banks. Data from the FDIC also show that the performance and financial health of community banks has experienced consistent improvement over the past 5 years.

While we encourage regulators to continue working with small banks and credit unions to help them adjust to new regulation, neither regulators nor Congress should weaken standards at the expense of consumers or the economy. Rolling back important regulatory measures, as proposed by the Financial Regulatory Improvement Act of 2015, makes the financial system more vulnerable to another crisis and makes it more likely that community banks will suffer even if they are doing everything right.

Thank you for your time, and I look forward to questions.

Chairman TOOMEY. Thank you, Ms. Edelman.

We have run over a little bit on the time with our witness presentations, so I am going to make sure to stick to my 5-minute limit and ask my colleagues to try to do likewise, if we could.

Thank you for that testimony. Gosh, where to begin.

For those who are actually involved in running financial institutions here, Mr. Foster, Mr. Porch, and Ms. Wood, you have talked about this new wave of regulation, this new burden, the new regulations that you have been hit with. In the absence of those new regulations, would you guys be risky institutions? Would you be in danger of failure? Are you much safer institutions now by virtue of these regulations? If each of you would briefly comment on that.

Mr. PORCH. No. We have been a strong, well-capitalized bank for nearly 100 years, and we would remain that. So it is not so much as our future survival as it is to be able to serve our consumers. We need to keep loan rates as best we can, deposit rates in the best light, and then we do not have much for fees. So that is more of it than financial strength, sir.

Chairman TOOMEY. Mr. Foster.

Mr. FOSTER. As a mutual bank, we have had historically very strong capital. You know, our concern—as they say, capital is king, and we have always been capitalized well above the minimums.

In terms of creating risk, our risk at this point is more to risk of earnings over time. As we are increasing our cost structure, our overhead costs have increased. Therefore, current earnings, that is the only way that we can build capital, is through retained earnings. So that is where the pressure lies—or our greatest pressure is.

Chairman TOOMEY. And compliance cost has been an increasing cost for you?

Mr. FOSTER. Absolutely. Yes, we have seen—again, compliance cost is not the only cost pressure, but just from a broad statistic, we have seen a 25-percent increase year over year from 2010 forward in our overhead costs.

Chairman TOOMEY. OK. Ms. Wood.

Ms. WOOD. I cannot say that we are any more sound today than we were 20 years ago. We have been doing mortgage lending, for example, for about 20 years. We have only lost five mortgages over the entire life of the program, and we have over 300 mortgages on our books. So it just has created more paperwork for us.

Chairman TOOMEY. Right. So prior to these regulations, it occurred to you to run a prudent institution that would be operating safely, it seems to me.

Let me go to an issue that has been raised by—Ms. Edelman in her testimony observes, correctly, that there are a number of regulations, including in the mortgage space, from which small banks are exempted. And so if I am correct, Mr. Foster, your institution actually is legally permitted to do balloon loans, but you have chosen not to do them. First of all, am I correct in that understanding? And if so, could you share with us why you have chosen to exit and to discontinue products for which you have demand, for which your bank is capable of providing, and which you are legally allowed to do but you have chosen not to? Could you shed some light on that?

Mr. FOSTER. Sure. In my testimony I mentioned that we did discontinue balloon loans. It was more so a factor—again, I rely on my compliance folks to guide me. But we opted—we looked at our product offerings and said, you know, we have this very complex rule and rules to implement. We needed to really dedicate resources to where—to the product lines that we had the most demand, and we just, frankly, said, "You know what? We are going to discontinue balloon loans." And there are very—there are circumstances where that is the right choice for a consumer. We never pushed a balloon loan. We would offer them in situations where there was a unique need, maybe a borrower who was going to be in a transitory—in a home for a transitory period, they were going—you know, professors and so forth.

Chairman TOOMEY. All right. And, Mr. Porch, did you say in your testimony that you exited certain residential mortgage lending for regulatory reasons?

Mr. PORCH. My bank actually exited mortgage lending a number of years ago, and believe it or not, the management of the bank at that time believed that regulations were excessive, and so they got out of the business. We have now, though, found that with TRID, we find it very difficult to even use bare ag land as security to finance the purchase and building of a home. So that has been an additional one for us.

Chairman TOOMEY. Thank you very much.

Senator Merkley.

Senator MERKLEY. Thank you very much, Mr. Chairman.

One of the things that I found very interesting was the rebound that has occurred on assets for banks of various sizes. For those of less than $100 million in assets, they went from basically zero percent return on assets in 2011 first quarter to 0.95 percent of assets in 2015. A similar thing happened with the $100 million to $1 billion banks. Whereas, the big banks were doing quite well in 2011, and their increase was very small. So the small banks have essentially caught up with the big banks in terms of return on assets.

The other thing that I found interesting was that the loan rates, the expansion in loans has been increasing at twice the rate for small banks as for big banks. And this general success of the small banks has occurred in a situation where there is a major problem—at least we keep hearing about it from people evaluating it—which is the very low interest spread that exists.

And so I just thought I would try to get all of your perspectives on this rebound from 2010–11 to 2015, if you have seen it in terms of your own bank's success or in general in your respective States, and especially how that has been managed to happen when the interest spread, which is so important for small banks, has been so compressed during this period. Anyone like to share your frontline experience?

Mr. PORCH. Well, I will make my remarks brief, because we are perhaps the unique animal sitting here at the table this morning. Our main scope of business is lines of credit to farmers and ranchers, and they have been quite successful over the last 5 to 6 years. Inflation, though, has caused operating costs to balloon. Livestock costs have ballooned. When we finance those operations, our loan volume certainly does go up. And it is not a function of mortgage lending or anything such as that. It is simply the scope of business that we are in.

Senator MERKLEY. Thank you.

Mr. FOSTER. In our experience in our market, we have seen since 2007 a continual decline in our outstanding mortgage loans. At this point in 2015, we are about flat in terms of mortgage growth for the year. So if we were to take today and go back to 2007–08, our portfolio is smaller.

Senator MERKLEY. In terms of return on assets, have you seen that change in general in the community banking community from 2010–11 until now?

Mr. FOSTER. If I reference the FDIC's quarterly reports, I would agree—or I do see that. In my own experience, our return on assets is going the other direction.

Senator MERKLEY. Thank you.

Anything you want to add on that, Ms. Wood?

Ms. WOOD. We are in the same position where our way has gone down. Our loan volume has gone down. We are seeing a lot of indirect in the market and a lot more squeezed margins.

Senator MERKLEY. OK. And, in fact, it has been just absolutely historic lows in terms of the interest rate spread over an extended period, which it has been fascinating to see banks do as well as they have during that period. But we have heard a lot of interest in the Fed that maybe it would be very helpful to small banks if the Fed was to, in fact, raise interest rates. Is that a viewpoint that you all might share? Ms. Wood.

Ms. WOOD. Yes.

Senator MERKLEY. Yes. OK.

Ms. WOOD. Absolutely. We have a lot of variable rate home equity loans, and they are market-driven.

Senator MERKLEY. OK. I wanted to turn to the point that was made about the challenge of getting good appraisals under the rules. Certainly we went through a period where we did lose a lot of small banks. When you look back at the number of small banks we lost, a lot of them were ones that you look at the practices and you go, Well, that was not the wisest practice. They had a lot of concentration in a particular segment of the market that was hit hard during the 2008–09 recession; or they were deeply engage in loans that had no underwriting, if you will, no-document loans. And I do not think anyone wants to return to that era.

But appraisals were part of the conversation about how we create this balance. How do we get good data, especially for loans that are going to be resold to the public? How can the public count on buying securities and make sure that the appraisals that went into establishing the collateral were accurate? And I am not sure—I think it was you, Mr. Porch, who mentioned the challenge you are having with getting appraisals on a timely basis. Do you want to expand on that a little bit or any specific suggestions on how do we address this in terms of timely appraisals but also for loans that might be being resold into the marketplace, accurate estimation of collateral?

Mr. PORCH. First of all, I certainly agree with you that there were situations where appraisers probably positively influenced values and certainly did impact the subsequent collapse of the banking system. So that is indisputable, in my mind.

For us, we have difficulty finding an appraiser. One of the gentlemen that does a lot of work for us is 80 years old, and he still works, but he is not going to last much longer. Another one that we have hired chooses really not to be very active in the field, so we are down to one and probably two. Keep in mind that typically these are ag land appraisers that we use. But the point that I would make with respect to the Committee today is that if we need to have an appraisal in the Philips of the world, finding comparables is virtually impossible. And then when that appraiser appraises a house in Philip and he cannot find comparables and tries to sell it in the secondary market, the whole deal falls apart. And that is where the problem really lies.

In South Dakota, we have, it seems to me at least, increased requirements to becoming an appraiser. It just becomes more and more difficult every year to become an appraiser. And whether those requirements need to be relaxed, whether some of the institutions need to offer appraisal classes or some such a thing as that, but it certainly seems to me that there would be a solution.

Senator MERKLEY. OK. My time is up, but I will just note that that is one of the things that we have heard, is a real dilemma that we do not have a solution to, comparables in rural banking. Thank you.

Chairman TOOMEY. Senator Rounds.

Senator ROUNDS. Thank you, Mr. Chairman.

I would like to go back just a little bit where Mr. Porch has identified the fact that while TRID was being implemented, it was causing some challenges. The new TILA–RESPA Integrated Disclosure Rule, or TRID, was an attempt by CFPB to simplify mortgage disclosures. While it was a long overdue step to make disclosures easier for consumers, I am concerned that the new rules are making it harder for banks to make loans to consumers.

Mr. Porch, could you just share with us a little bit about what you were talking about in terms of what TRID has done in terms of you capability to even use bare ag land in some cases to make a loan? Could you share a little bit about how that is working?

Mr. PORCH. Previously, we could use bare ag land without any buildings, and as far as the purpose, we did not really care, and if that purpose was for the construction of a home, that was totally fine. We had to meet all the disclosures in terms of truth in lending, et cetera, but now with TRID, we have to meet all the HMDA reporting requirements and everything, and, frankly, we do not do enough of that line of business that—we are terribly fearful of making a mistake. And you have heard some of the other witnesses this morning talk about mistakes, and that has us very uneasy about that kind of a thing.

And so we have seven loan officers in our bank, including the president. The other day we had a conversation about whether we even wanted to venture into that arena, and we said two of the guys maybe will undertake that issue, but for the majority of us, it is very difficult to be trained, it is very difficult to understand the program. And so we just virtually are almost out of that market.

Senator ROUNDS. Thank you. Just as a follow-up, in terms of the need to look at the appraisal situation, Senator Thune and I had been working trying to figure out why we were having such a tough time getting appraisers, and through our questions from the Appraisal Foundation—and this is the industry's regulator—it appears that they are making it harder for prospective appraisers to actually enter the profession, and that there had been a 19-percent decline in the total number of appraisers from 2007 to 2014. And when we started talking about on a day-to-day basis with one of the other banks in western South Dakota—and there are not that many of them, but one of them—and I will submit this for the record, Mr. Chairman. The note coming back in just yesterday was from one of the loan officers saying—this is to her boss: "I just wanted to let you know an interesting situation I just had ordering an appraisal the other day. I received one order for an FHA home purchase in Eagle Butte, South Dakota. The appraiser I could get to go there was charging $1,500, and it was going to take a month before she could get us the report. On that same date, I received another order for a home purchase with Flagstar in The Villages, Florida. The appraiser I engaged in that appraisal was going to charge $350 and would have it done in 10 days. Isn't the difference amazing?"

Eagle Butte is on the reservation in western South Dakota. We have got challenges in rural areas in terms of getting appraisers set up, and I think we ought to be making it a little bit easier for these guys to get in and be involved with it. And most certainly I think your testimony here has identified the need in the Philip area as well.

If I could, I would like to ask one question of the group, if you could. One of the biggest challenges we think that we have is trying to cut some of the red tape that is out there. The Federal Government is issuing an average of 3,500 more rules every single year. We have got over a million Federal regulations on the books today. The total cost of the regulatory burden to the American public is about $1.9 trillion per year compared to about $1.4 trillion in person income taxes, so it is a big deal.

If there was one single regulation out there that we could look at eliminating that would help you provide service to your customers, can you tell us what it would be today? Is there a single regulation which stands out, maybe two that stand out, that you would like to see us try to address?

Mr. PORCH. Well, I certainly do not mean to dominate the conversation this morning. Finding one would be terribly difficult. In my written testimony, we talk about the inability or the lack of knowledge for our examiners to understand the difference between commercial business and farm and ranch lending. And if there is one message that I could leave with the Committee today, it would be to understand that, perhaps give some directives to examiners and go forward from there. That really affects us.

Ms. WOOD. I am not sure I could pick just one. But I will think about that, and I will get something to you.

Senator ROUNDS. Thank you.

Mr. FOSTER. I would concur. It would be hard to pick one.

Senator ROUNDS. Thank you.

Thank you, Mr. Chairman.

Chairman TOOMEY. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman. Thank you all for being here today.

We have heard a lot about the regulatory burden on our smaller banks, and, look, I get it. There are certain rules that are either too broad or too burdensome given the risks that smaller banks pose. And that is why I have joined with all of my Democratic colleagues on the Banking Committee to introduce a bill that would provide targeted relief to small lenders without rolling back the rules on big banks that pose a real threat to our financial system.

But I do want to take a closer look at the idea that Dodd-Frank has dramatically increased costs for small banks and undermined their financial performance. So let us start with the costs part of this.

Dodd-Frank Act changed the law on how FDIC calculated what banks owe in deposit insurance assessments. The Dodd-Frank change allowed community banks to pay far less in assessments, while bigger banks would pay far more. The Independent Community Bankers of America, the main lobbying group for community banks, said at the time of Dodd-Frank that the change would save community banks collectively about $4.5 billion in just a 3-year period.

Now, Mr. Porch, do you know how much your bank has saved on FDIC assessments because of this change in Dodd-Frank?

Mr. PORCH. I do not know the answer to that question, ma'am. Thank you.

Senator WARREN. OK. Maybe you could get back to me later on that?

Mr. PORCH. I certainly would.

Senator WARREN. OK. Mr. Foster, do you know how much your bank saved?

Mr. FOSTER. If I could answer that maybe in a little bit different way, when I joined the Bank 20 years ago, up until the late 1990s, we were only paying the FICO assessment, which to our bank——

Senator WARREN. I appreciate that, Mr. Foster, that there was a big change.

Mr. FOSTER. OK.

Senator WARREN. What I am asking is that Dodd-Frank, when it was passed in 2010, changed the way FDIC assessments are calculated. The estimate was that over a 3-year period it would save community banks about $4.5 billion, and I wondered how much your bank saved.

Mr. FOSTER. I can give you the exact number. We have saved from that point forward. I can submit that.

Senator WARREN. I would appreciate having that.

Mr. FOSTER. Sure.

Senator WARREN. And just for the sake of comparison, I think you said, Mr. Porch, that your bank spent $222,000 in total regulatory costs last year. That is all in, that is everything. The regulations you did before Dodd-Frank, after Dodd-Frank, everything. Is that right?

Mr. PORCH. That is correct, but be mindful that of that $222,000, that does not include any salaries.

Senator WARREN. I understand.

Mr. PORCH. OK.

Senator WARREN. This is what you identified in your testimony, because I am trying to do the math on this, because according to the ICBA, the average community bank saves about $250,000 every year because of the change in FDIC assessments.

Now, I know that savings will vary depending on the size of the bank, but the point is Dodd-Frank included a tradeoff. It imposed new rules to protect consumers and our markets, necessary rules to stop the kind of behavior that led to the last crisis. And then, to reduce the financial burden on community banks, it also significantly reduced the cost of insurance that those banks had to pay.

To get the full picture of Dodd-Frank's impact, it is necessary to add both the regulatory costs and the regulatory savings, and that brings me to the issue of financial performance, which, since I am running low on time, I will just try to hit this as quickly as I can.

Ultimately, financial performance seems like a pretty good measure of the health of our community banks, and according to the latest quarterly report from the FDIC, year over year earnings for community banks in the first quarter of this year were up over 16 percent, which was three times the growth of larger banks in that same time period. Only 5.8 percent of community banks were not profitable in this quarter. That is the lowest level since the second quarter of 2005, long before Dodd-Frank was passed.

You know, community banks play a critical role in Massachusetts, all across this country, and Congress should look for ways to get rid of unnecessary rules for smaller banks and for credit unions. But as we consider legislation, we need to move past the idea that Dodd-Frank has crushed community banks. It is just not true. No matter how many times lobbyists say it in hearings or in the media or in our offices, when I look at the data, I see two big things: According to the banking lobby itself, Dodd-Frank was projected to save community banks billions of dollars in FDIC fees, and 5 years after the adoption of Dodd-Frank, the community banks collectively had their best quarter in a decade, and their profitability is increasing three times faster than the profitability of big banks.

This Committee should legislate based on the facts, not on a make-believe narrative that is pushed by lobbyists looking for sweeping changes to our financial rules, changes that would mostly help the big banks.

Thank you, Mr. Chairman.

Chairman TOOMEY. Senator Scott.

Senator SCOTT. Thank you, Mr. Chairman, and thank you for holding this important Subcommittee hearing, and certainly seeing the impact that the regulatory environment is having in Pennsylvania has been important for me to read the testimony of your Pennsylvania witnesses. I thank you for taking the time and having the courage to bring this issue to the forefront.

Just to follow up on the Senator's question, the three bankers at the table and the credit union, are you guys paid lobbyists? Paid lobbyists, no? OK. So my question is: Has the cost of complying with the regulatory burden increased or decreased since Dodd-Frank, the overall cost?

Mr. FOSTER. I would say it has increased.

Senator SCOTT. Mr. Porch.

Mr. PORCH. I am going to argue that it increased as well. I did submit the data for the current year. It is my dereliction of duty perhaps that I did not submit it from the year before, but I believe that it has increased.

Senator SCOTT. OK.

Ms. WOOD. And I would concur. The forms, the staff time that we spend on compliance has been much greater.

Senator SCOTT. Right. And in your asset size, how many of your institutions of your asset size were involved in the economic crisis, causing the economic crisis in 2008? Short answers.

Ms. WOOD. None.

Mr. PORCH. None.

Mr. FOSTER. I agree.

Senator SCOTT. Thank you. So with 800 pages of legislative text and nearly 20,000 pages of regulatory text, Dodd-Frank, which is only 70 percent implemented—only 70 percent implemented—is increasing the compliance costs for institutions all around the country and certainly for institutions that are smaller. The pain is felt by the customers. I think you said, Mr. Porch, the negative impact is passed down to the customer, and that is a reality. How does that look? Restricted access to products, elimination of services, and negative impact includes areas like residential mortgages, mortgage servicing, home equity lines of credit, overdraft protection, and if I read it correctly, one out of four small banks are either merging or looking at being acquired. Is that about accurate as far as you know?

Mr. FOSTER. I am not sure about the exact statistics as far as the one in four, but that is the trend. We see it in discussions in our market quite frequently. We have seen a number within Pennsylvania announcements this year already, and there are, I think, more in the offing before year end.

Senator SCOTT. All right. And I have about 2 minutes left, so I am going to ask just a couple questions. Thank you for your answer to the first two questions.

Mr. Foster, too often too many regulations are crafted from an urban, high-density paradigm. The economies of scale often work against smaller institutions like yours. Your mission to serve a dispersed population can be expensive. Therefore, any increase in regulatory burden makes profitability much harder to achieve. Is that accurate?

Mr. FOSTER. It is. As I mentioned in my testimony, our number of branches in relation to size, by nature of the market, we do have to have more facilities in place to be able to reach out and provide those services to our customers. Again, the Amish community, as I mentioned, a very unique population dynamic. They do not use mobile banking. You know, if they need to go to the bank—and we have a lot of Amish who are small businessmen as well, they have cash needs, they need to be at the bank on a daily basis. And if they do not have a branch in their community or very close by, that is a big part of their day that is tied up with doing their basic banking.

Senator SCOTT. Thank you. My final question, as my time is running out here, and the Chairman says he is keeping us on a very tight 5-minute timeline, and I want to respect the Chairman there.

Mr. Foster and Ms. Wood or Mr. Porch, Senator Donnelly and I continue to work on fixing issues with TRID. All around the country, lenders are using the new TRID forms required by the CFPB for mortgage originations and refinancings. While I appreciate Director Cordray's promise that the implementation phase will not be punitive, I think legislation is still the only way to achieve that sense of certainty. So I continue to work with my colleagues.

Are you able to share with us any firsthand accounts or data of how the risk of liability deriving from the new TRID forms is affecting lending or other loan variables in rural communities? We only have about 30 seconds.

Ms. WOOD. I can take that one. One of the things that happened with us when we—and I put that in my testimony. When we flipped the switch to the new forms, we had a glitch in the system. So we had to use the new forms. October 2nd we used the old forms. October 3rd we used the new forms. We dusted off the 40-year-old typewriter that we had at the office and brought it out, and we are hand-inputting some of that information on the forms because the computer system just—it was a glitch. So that a lot more time is put into printing out a simple form than what it really should be.

Senator SCOTT. Which only increases the likelihood of more human errors.

Ms. WOOD. Right.

Senator SCOTT. So by default, you are having a harder workload and, frankly, as the president and CEO of a small institution, realizing the number of jobs that you mentioned earlier, it is like you are a one-armed paper hanger. God bless your soul.

Mr. FOSTER. If I could just add to that real quick, we are just basically backlogging mortgage applications at this point because there are a number of bugs that we are still trying to work out. And so we are being ultra conservative, and we are not going to write the loan until we are confident that the bugs are fixed out and there are not going to be any glitches in the final paperwork.

Senator SCOTT. Remarkable impact. Thank you, Chairman.

Chairman TOOMEY. Thank you.

Senator Donnelly.

Senator DONNELLY. Thank you, Mr. Chairman. I want to follow up on what my colleague Senator Scott, who is our partner in this effort in the TRID rules that we are looking at, and, again, to Mr. Foster and to Ms. Wood, because you had cited this in your testimony. We have heard similar concerns in my home State of Indiana about the additional challenges that this has caused. And so what would a good-faith grace period do to help you in the mortgage process? Mr. Foster, if you could talk to that, if you had a grace period for getting to the point where this process, instead of just landing on you, that you kind of eased into it.

Mr. FOSTER. If I can just maybe make sure I understand your question. In terms of good faith in terms of the liability issue, is that the crux of your question?

Senator DONNELLY. Well, like a grace period where you look and you go, yeah, liability, everything else, 3 to 4 months you have a chance to learn this, to work with it, to get there without incurring any liability in the process.

Mr. FOSTER. We are still relying on our vendors. That is our biggest fear right now, is in terms of the vendor applications. I mentioned in my testimony we are a couple weeks into this, and our vendor is on the fifth update trying to fix—and I looked at just the other day the litany of bugs in each update they are trying to fix. We are so dependent there. I hate to answer a question in the sense of—I mean, off the top of my head if we had, you know——

Senator DONNELLY. Would it make your life easier?

Mr. FOSTER. Yes. The answer is yes, and a 3- to 6-month delay would be phenomenal.

Senator DONNELLY. Ms. Wood.

Ms. WOOD. And I agree. The longer that we can delay, with the grace period of TRID, you know, the better off that we will be. Like I said, we are manually typing stuff into forms because we do not—you know, our members want to purchase the home. They want to get their home equity. They have the home repairs that they need to do, college tuition, whatever it may be that they are doing their equity for. So we have to do that loan or, you know, we are not backlogging them. We want to be compliant. We want to do the right things. But we need some grace.

Senator DONNELLY. As part of your experience, when you look at this now, do you have a lot of homeowners who are not homeowners yet who are kind of in the queue, as you mentioned, that they want to get into the house, they want to buy the house, they want to complete everything, and you are just hung up right now?

Ms. WOOD. I think there have been a few cases of that. I cannot think of any specific examples right now.

Senator DONNELLY. OK.

Mr. FOSTER. I would say we have just a few at this point.

Senator DONNELLY. OK. Going to a longer exam cycle, Mr. Porch, I have joined with our Chair, Senator Toomey, in legislation so that highly rated small financial institutions qualify for an 18-month onsite examination cycle instead of the usual 12-month cycle. This bill allows an increase from $500 million to $1 billion for the asset threshold, and what I am wondering, Mr. Porch, is: If this is enacted, will that regulatory relief to your organization, would that make things simple for you? Would that make your operations easier? And would it also be able to save you money that you should not be wasting?

Mr. PORCH. Actually, it would not affect our bank because I think the—we are $250 million, and we are CAMELS 2. And so we are on an 18-month exam cycle.

Senator DONNELLY. OK. Is anybody here between that $500 million to $1 billion?

Mr. FOSTER. We are as well on an 18-month cycle currently.

Senator DONNELLY. OK. Well, if they had 500, they would need it.

With that, Mr. Chairman, I will kick it back.

Chairman TOOMEY. And we hope for a booming economy so they grow into that threshold.

Well, I want to thank all of our witnesses for their testimony and for answering the questions we had. All Members will be able to submit additional written questions to each of the witnesses. Thank you very much for being here today.

The hearing is adjourned.

[Whereupon, at 11:17 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF TERRY FOSTER

EXECUTIVE VICE PRESIDENT AND CHIEF EXECUTIVE OFFICER, MIFFLIN COUNTY SAVINGS BANK, LEWISTOWN, PENNSYLVANIA, ON BEHALF OF THE PENNSYLVANIA ASSOCIATION OF COMMUNITY BANKERS

OCTOBER 28, 2015

Chairman Toomey, Ranking Member Merkley, and Members of the Subcommittee, my name is Terry Foster. I serve as Executive Vice President and CEO of MCS Bank (Mifflin County Savings Bank), a $137 million dollar asset bank headquartered in Lewistown, Pennsylvania. We are a State-chartered mutual savings bank, which was originally chartered in 1923 as Mifflin County Building and Loan Association. Our bank serves exclusively rural populations in the central part of the State, with a market area primarily defined as Mifflin, Snyder, and Huntingdon Counties. I have served in my current role at MCS Bank since 2009, but I have served the bank in other capacities for the past twenty (20) years. I am a locally raised banker who grew up in a community long served by MCS Bank and my connection to the bank started many years earlier when I opened my first savings account in order to save monies I earned from a newspaper route and mowing lawns. In addition to my role at MCS Bank I also serve as the current Chairman of the Pennsylvania Association of Community Bankers (PACB) as well as serve on the Mutual Bank Council of the Independent Community Bankers of America (ICBA). I wish to thank you for convening today's hearing on "The State of Rural Banking: Challenges and Consequences" and providing me with the opportunity to testify.

I wish to state that my testimony is based upon my own experiences and observations as a rural community banker, as well as from the perspectives of my fellow bank employees' dealings with our customers and stakeholders. Further, my testimony is from the perspective of a $137 million institution trying to preserve its ability to survive and maintain a presence in communities where local banking and service is so very important; I hope to be able to illustrate this last point with an example in my testimony.

MCS Bank is headquartered in Lewistown, PA, the county seat of Mifflin County. The bank was originally formed as Mifflin County Building & Loan Association in 1923. In 1956, Mifflin County Building & Loan Association converted to Mifflin County Savings & Loan Association. In 1992 a final conversion occurred, creating Mifflin County Savings Bank (AKA MCS Bank). MCS Bank now operates five (5) full-service branches and one (1) loan operations office within the three-county market. Exclusive of our headquarters branch, the average size of our branch network is $12 million in assets. Within two (2) communities in which MCS Bank maintains branches, no other banking outlets exist. The Bank operates with a staff of forty-two (42) full and part-time employees, or 37 full-time-equivalent employees (FTEs).

The bank's market is comprised of an approximate 1,600 square-miles area with a population density of eighty-one (81) residents/square mile. Median household income across the market is $43.7 thousand, which is lower than both our State and the national figures. The percentage of persons below the poverty level is in line with the State average and below the national average. Population growth in our market is historically low, and has been nearly flat in more recent years.

By their nature, rural markets create unique efficiency challenges in terms of serving dispersed populations as compared to the more densely populated suburban and urban areas. The fact that MCS Bank, at just $137 million in assets, operates five (5) full-service branches to serve thinly served communities illustrates my point. Every dollar of cost rural institutions must incur to maintain compliance with new or heightened regulatory requirements disproportionately impact institution like mine.

A unique population dynamic in our market, although not exclusive to us in the central part of Pennsylvania, but one that I feel is a perfect example of why it is critically important that independent community banks in rural markets survive, is the existence the unique populations that require unique servicing, in our case, the "plain sect" or Amish community.

For those Subcommittee Members not familiar with the Amish and their unique traditions, they are a group of traditional Christian church fellowships of Anabaptist origins. The Amish live simple, agrarian existences, dress very plainly, avoid the use of most modern technologies, including electricity, telephones, automobiles, and modern banking conveniences, such as web banking, and more recently, mobile banking. In place of traveling by automobile, Amish travel by horse-drawn "buggy". Because of their social and religious conventions and aversion to technology, serving this demographic is difficult and it takes a keen, local understanding of this "community" to meet its members' needs; a community that will never be understood by banks headquartered in suburban or urban centers and whose needs are not a part of the equation when branch consolidation or closure decisions are being contemplated.

Proof positive: in 2011, a large regional bank, serving a rural community in our market with a high concentration of Amish residents, shuttered a branch that long served that community. Over the years the branch had changed ownership through acquisitions by successively larger organizations. Ultimately, the branch, along with other branches in other rural communities, were closed as a result of the current bank's internal "branch rationalization" process that concluded that the subject branches would not be retained due to size and other factors. What we learned at the time, anecdotally, was that the bank was closing rural branches that were under $15 million in size. In comparison, MCS Bank's branch network averages $12 million in size. The loss of this branch was devastating to the community's residents and businesses, particularly to the Amish residents whose transportation limitations created an unusual hardship by forcing them to travel long distances to another community to do their banking at a branch to which their account servicing was transferred.

In response to this community's loss, MCS Bank worked with community leaders and business owners to try to find a workable solution to allow the community to retain its banking outlet. After a lengthy process, numerous fact-finding community meetings and mail surveys, the Bank partnered with a member of the business community to build and open a 530 square-foot branch within a building supply/hardware store. Four years later, this branch, albeit very small, is thriving and supporting the community. To date, the bank has provided financing to the Amish community for such projects as the purchase of land for farm expansion and for the construction of a new retail store.

The potential loss by this particular community is just one example of situations that are playing out in communities across the Nation. I believe very strongly that the community banking industry is experiencing consolidation, particularly in rural markets, at an accelerating rate, for a host of reasons, but one being escalating compliance-related cost and complexity. Yet another occurrence of branch consolidation is taking place this very month within our market, which will force customers of that bank to travel more than twenty (20) miles to the next closest bank branch.

At MCS Bank, we now have six (6) of forty-two (42) employees who devote significant amounts of their routine workdays to compliance; from our Compliance Officer down to lenders and loan processors.

I argue that a great deal of time and resources we are devoting toward our efforts to comply with the letter of the laws and regulations, their complexities and many inconsistencies, have had a detrimental impact on our ability to serve our customers with both products and service delivery.

Has Dodd-Frank impacted the products our bank offers? Yes. Since the introduction of QM and Ability-To-Repay, MCS Bank has discontinued offering balloon loans. For us, the decision wasn't a matter of whether or not we have the latitude within the new rules to continue to offer this product, but rather it boiled down to a matter of resource allocation. With the volume of rules to interpret and implement, we simply had to decide on which products we were going to focus our attention. Because we historically originate fewer balloon loans in comparison to our other mortgage products, we opted to not create a new note and disclosures, under the new rules. Secondarily, we were concerned about the potential higher level of examination scrutiny.

The required escalation of our compliance focus negatively impacts bank stakeholders such as community organizations, charities, etc., which have historically been the beneficiaries of our philanthropic efforts, both monetarily and otherwise. The more time our people must devote to compliance matters is less time available for them to spend on volunteer and charitable endeavors. Increased regulatory costs also negatively impact the community by way of diverting financial resources away from community investment. As increased costs and other pressures work collectively to incentivize further consolidation, larger organizations with distant headquarters locations lack the appreciation and commitment to local needs in rural areas. I know from personal experience of such situations in our market. In a community into which we are contributing thousands of dollars annually in charitable donations and other types of community giving, a large regional bank, by comparison, is contributing very little. We have a branch manager in our community office who previously worked in the same capacity for the regional bank, whose office was allocated only $100.00 annually for community support.

Are theories behind the consumer-focused regulations well intended? Absolutely! The notion of "ability-to-repay", as generally defined, has long been an underwriting practice of prudent community lenders, but the codification of such concepts into regulation is fraught with complexity, inconsistencies, and in some cases lacks logic. The unintended consequence is confusion for our people as they attempt to implement and administer new rules, which ultimately leads to human error, additional cost and potential examiner criticism, despite best efforts to do the right thing. I argue there are elements that have no meaningful benefit to consumers, and in fact create greater consumer confusion.

To the issue of human error, consider the following example we experienced in a purchase-mortgage transaction:

- In the sale negotiation, the buyer agreed to pay the full transfer tax to the county authority. The loan processor, when preparing the early disclosures, overlooked this detail when reviewing the Sales Contract. As a result, the early disclosure was prepared, as is customary, with the buyer and seller paying one-half each of the transfer tax. This error, when discovered, was not a redisclosable event under (RESPA Reform of 2010); therefore we could not reissue a revised early disclose to correct the error. Consequently, we absorbed the cost of one-half of the transfer tax by compensating the buyer for an expense he fully intended pay as a part of the negotiated transaction. Under the new TILA–RESPA Integrated Disclosure (TRID) rules, there remains no latitude for us to rectify this type of mistake, thus forcing cost onto the bank as a result of simple human error.

Because the timing of today's hearing coincides with our ongoing work to fully implement the rules promulgated by the TILA–RESPA Integrated Disclosure (TRID), which had an effective date of October 3, 2015, I have included a TRID related example in my testimony:

- One (1) of two (2) definitions of a Business Day apply for disclosure purposes depending upon the nature of the disclosure (Initial or Revised Loan Estimate, or Closing Disclosure).
- Formatting differences exist between the Loan Estimate and Closing Disclosure documents.
  - Estimated fees costs are required to be truncated on the Loan Estimate while they are required to be taken out to two (2) decimals on the Closing Disclosure (i.e., Estimated Taxes and Insurance must be disclosed as $xxx. on the Loan Estimate and as $xxx.xx on the Closing Disclosure, even when the estimates do not change from the time the Loan Estimate and Closing Disclosures are prepared and provided to the customer).

The complexity involved in implementing TRID is taxing all parties involved. In our case, our third-party Loan Origination Software (LOS) provider's applications were not ready to go on October 3rd; therefore our testing protocols were delayed. If fact, as of Friday of last week, our loan origination software is on its fifth (5th) update, post October 3rd, to correct a host of technical issues. Despite the amount of training our lending and compliance staff has attended to be ready for the changes, we were still not fully prepared to go on day one, which in my estimation is a function of over complexity of, and inconsistencies within, the rules. Director Cordray acknowledged the delays some of the vendors are experiencing in readying their platforms to handle the new TRID rules. [1]

As things stand now, in terms of product delivery, we are wrestling with whether or not the new rules will allow us to continue to offer single-closing construction loans when the customer chooses and adjustable-rate mortgage (ARM). Our compliance consultant with thirty (30) years of experience is of the opinion that the new disclosure rules do not accommodate a single-close construction loan that has a variable-rate during the construction period then converts to an ARM loan when the loan enters the postconstruction repayment phase. Single-close construction loans benefit consumers in terms of both time and cost. This inability to originate an ARM loan in this situation also reduces our ability to manage interest rate risk. In today's low-rate environment, this is most critical.

As a small institution, not only do we rely on software vendors, but we also must rely on consultants for guidance and interpretations of the application of the rules. While working through TRID implementation and training, our compliance consultant cited instances in which requests to the CFPB staff for clarification have been met by being pointed back to the guidance. An example of this instance being the construction loan disclosure illustration previously cited.

[1] "ICBA Opposes CFPB Overdraft Data Request" (2015, October). *ICBA Independent Banker*, p.11.

The CFPB order, issued in 2014, to financial institution data processors to provide client bank overdraft program system settings and overdraft activity, for analytical purposes, imposes a real cost to community banks. Our data processor, Fiserv Inc., responded to this order by stating, "The request will impose significant expenses that will have to be passed to its bank clients."[2] The financial institution themselves, not CFPB, bear the cost of the data processors efforts to comply with the CFPB request in order that the Bureau may ferret out practices tied to "overdraft privilege programs" that it perceives as wholly bad for consumers.

At MCS Bank we've long held to a traditional approach to consumer overdrafts. Long ago our board and management team took a philosophical stance against "overdraft privilege programs" because we didn't want to create the perception with either regulators or customers that we encourage overdraft behavior for the sole sake of generating overdraft revenues. Our approach is simple: we work one-on-one with customers exhibiting overdraft behavior. We counsel those experiencing financial difficulty and attempt to provide assistance to redress the underlying issue. When we believe circumstances warrant closing an account and moving a customer to a more suitable account, we will do so.

There are several important issues related to the CFPB's order to the financial services third-party core processors to provide the requested data, such issues as authority and due process under §1022 of Dodd-Frank. For our bank, the more basic issue is who ultimately bears the cost of compliance. Our data processor clearly has signaled it will pass the cost onto us; a cost that we will be forced to absorb. Unfortunately, we as an institution, and few other community bank institutions I know of, have never engaged in the type of behavior that gives the CFPB such concern.

Flood map "creep" in recent years has exposed MCS Bank to reputation damage, an instance of a formal consumer complaint being lodged with the Pennsylvania Department of Banking and Securities and ultimately a lost customer.

In 2013, a customer disputed a Flood Redetermination and refused to purchase flood insurance. The bank advised the customer of their need to obtain an elevation determination in order to potentially avoid the need for flood insurance. In the interim, the bank forced placed insurance on the property to ensure coverage is in-place within 45-days of our receipt of the redetermination notice. The subsequent elevation determination concluded that the customer's home was not in a flood zone and thus flood insurance was not required. The bank promptly canceled the force-placed flood insurance and refunded the unearned premiums returned by the insurer. The customer then demanded a refund of the entire premium because of the elevation-determination results. Not being satisfied with the reason for a partial refund, the customer filed a complaint against the bank with the Pennsylvania Department of Banking and Securities. A review by the Department concluded that the bank acted properly. As you might imagine, this borrower no longer does business with MCS Bank.

Recommendations

A number of bills have been introduced in the House and Senate that would provide significant relief from many of the concerns noted above:

- *S.1711*, introduced by Senators Tim Scott and Joe Donnelly, would provide a critical safe harbor from enforcement actions and private law suits for compliance errors arising from the implementation of the TRID rule, provided the lender has acted in good faith to implement and comply with the new rule. As with any new rule of this magnitude and complexity, before it went "live" on October 3, it was impossible for community banks and other stake holders to begin to identify problems and develop and implement solutions. This is particularly true because there was no opportunity under the new rule to comply early, testing systems in real time and under real circumstances. A safe harbor will allow mortgage closings to proceed apace without fear of enforcement and liability for minor errors.
- *The Financial Regulatory Improvement Act (S.1484)*, introduced by Chairman Richard Shelby and marked up by this Committee in May, contains a number of provisions that would help community banks like mine better focus our resources on the communities we serve. For example, S.1484 would provide that any mortgage held in portfolio, including the balloon loans that play an important role in our local market, would be a "qualified mortgage" (QM), under the CFPB's ability-to-repay rule. The bill would also create an 18-month exam cycle and streamlined call reports for well-rated community banks with assets of less

[2] Swanson, J. (2015, October 20). "CFPB Warning: Cordray 'Disturbed by Reports' of TRID Implementation", (*mortgagenewsdaily.com*).

than $1 billion. These provisions would better reflect the significantly lower risk profile of community banks. S.1484 would require the Federal Housing Finance Agency to withdraw a proposed rule that would impose a mortgage lending test on Federal Home Loan Bank (FHLB) members. The FHFA proposal cuts against the grain of Congress' clearly expressed intention of expanding the mission and role of FHLBs beyond residential housing finance to supporting small and medium-sized businesses and other critical community needs. These are just a few of the more significant regulatory relief provisions of S.1848.

- *S.970*, introduced by Chairman Pat Toomey and Senator Joe Donnelly, would allow a highly rated bank (CAMELS 1 or 2) with assets of less than $1 billion to be examined on an 18-month rather than a 12-month cycle. S.970, which is identical to a provision of S.1484 noted above, would allow examiners to better target their resources at the true sources of systemic risk.
- *The Community Lending Enhancement and Regulatory Relief Act of 2015 (the "CLEAR Act", S.812),* introduced by Senators Jerry Moran and Jon Tester, would provide QM status for any mortgage held in portfolio and an exemption for loans held in portfolio from new escrow requirements for higher priced mortgages for any lender with less than $10 billion in assets. S.812 would also provide an exemption from internal control attestation requirements for community banks with assets of less than $1 billion.
- *The Privacy Notice Modernization Act (S.423),* introduced by Senators Jerry Moran and Heidi Heitkamp, would eliminate annual privacy notice mailings when an institution has not changed its privacy policies. These notices are costly, redundant, and a source of confusion to many customers.

This is just a sampling of the legislation before this Committee that would provide meaningful regulatory relief for community banks, help stave off further industry consolidation, and ultimately benefit consumers, particularly in rural communities such as the ones that I serve.

I thank you again for the opportunity to testify today and I hope that my comments are beneficial to the work of the Subcommittee.

I am happy to answer any questions you may have.

PREPARED STATEMENT OF ROGER A. PORCH

VICE PRESIDENT, FIRST NATIONAL BANK, PHILIP, SOUTH DAKOTA

OCTOBER 28, 2015

Chairman Toomey, Ranking Member Merkley, and Members of the Subcommittee, my name is Roger Porch and I am a Vice President at First National Bank in Philip, South Dakota. I would like to thank you for affording me the opportunity to appear before you to share some information about regulatory challenges faced by rural banks. My hope is we can find some regulatory relief that will help community banks across the country. More importantly, however, we hope we can—by making credit more readily available to those who live in rural areas—sustain our lifestyles and expand local economies. The area in which I live—western South Dakota—is highly reliant on agriculture and tourism, and we are doing well for the time being with some notable exceptions which I will touch upon later. But, we take nothing for granted and are pleased to be here this morning.

My bank is headquartered in Philip, South Dakota, and we have one branch in Faith, South Dakota, located 85 miles to the north. You can see by that distance that our environment is one of sprawling prairies with miles between towns. We are a $250 million bank, and serve a large area of western South Dakota. We have customers as far west as Wyoming and south to Nebraska. First National Bank is privately owned, and has successfully served the needs of our trade area for over 100 years. We live by our motto, "Partners in Banking". Our principal scope of business is the financing of farmers and ranchers with lines of credit and real estate and machinery loans. Our bank is, and has been, well-managed. Perhaps this is presumptuous of me to say, but we like to think we know what we are doing. However, excessive, unfocused regulations are changing the way we do business.

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 nonprofits—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.

The ability to meet local needs has not been easy with the increased regulatory costs and second-guessing by bank examiners. During the last decade, the regulatory burden for community banks has increased dramatically and it is no surprise that nearly 18 percent of community banks disappeared in that period.

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 urge Congress to work together—Senate and House—to pass bipartisan legislation that will enhance the ability of community banks to serve our customers.

In my testimony today I would like to make the following three points:

- Unnecessary regulatory burden limits banks' ability to serve their customers,
- These challenges have real costs for our banks and the communities they serve, and
- Commonsense solutions would help alleviate this burden.

Unnecessary Regulatory Burden Limits Banks' Ability To Serve Their Communities

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.

Make no mistake about it, this burden is keenly felt by all banks, but particularly small banks that do not have as many resources to manage all the new regulations and the changes in existing ones. The role of community banks serving their rural communities has been placed in jeopardy by the broad array of new regulations. The Dodd-Frank Act alone has charged Federal financial regulators with writing and enforcing 398 new rules, resulting in at least 22,534 pages of proposed and final regulations, and that's with regulators only two-thirds of the way through the rulemaking process. Community banks are disproportionately affected by regulatory overkill since there is a small asset base over which to spread the costs. First National Bank spent $222,000 on regulatory expense which is 19 percent of overhead. Importantly, that doesn't include salaries. One could argue our total financial burden is 30 percent of overhead. We epitomize the rural community bank and our burden is noticeable. Regulation comes at a cost, most often to local economic growth, job creation, and community well-being.

Overly Burdensome Mortgage Regulations Leave Customers Unserved

National Bank does not make home loans. The avalanche of mortgage regulations is too complex and costly to comply with. The added cost and risk of making these loans is not something our bank can justify changing our long-standing policy. The economic life of rural America depends upon financial products and services only community banks provide. By forcing many community banks out of mortgage lending, there will be significant harm to the rural communities bankers are trying to serve.

Examiner Understanding of Farm Lending Is Limited

Our main scope of business is lending operating money to ranchers and farmers. Although we do use projected cash flows in our annual credit analyses, we consider ourselves equity lenders. We measure equity for each customer once a year. The problem is our examiners are accustomed to analyzing commercial businesses which are more reliant upon cash flow. Agriculture income is projected to fall by 36 percent this year, and we are already seeing livestock prices down by 24 percent from last year. Our ag customers could see some erosion of equity and problems with cash flow. If we are required to rely on cash flow analysis, we could possibly find ourselves in the situation of not being able to loan operating money to a rancher even though the rancher may have equity in the millions simply because the cash flow is fluctuating due to dropping commodity prices. In the past, these loans have been made safely and successfully

Uniform Overdraft Requirements Will Harm Rural Customers

The Consumer Financial Protection Bureau (CFPB) is inquiring into overdraft procedures to determine how those practices are impacting consumers. First National Bank considers itself an "ad hoc" meaning we generally cover overdrafts rather than return checks. We are willing to assume that risk in most cases. However, we are being told that we should counsel those account holders that are routinely overdrawn. But, we don't know what counseling means and we don't know at what level counseling begins. Statistics show that 8 percent of account holders pay 75 percent of the charges, and the burden falls disproportionally on those between 18 and 25 years of age. Should regulations force us to close accounts, there would be many who wouldn't be able to own an account at a bank. First National Bank in Philip has voluntarily limited overdraft charges to five items per day in the hope that impact upon account holders be minimized. We don't want to close accounts and force people to pawn shops and pay day lenders. This is a perfect example of unintended consequences.

The Bank Call Report Is Unnecessarily Burdensome

Twenty-five years ago, the call report required by FFIEC was less than 10 pages long. Today, for our bank, it is 86 pages. Ironically, many of the pages are not applicable to us or other rural community banks.

Nonbank Lenders Compete With Unjustified Competitive Advantages

Competition from nonbank lenders is an ongoing problem. Farm Credit System (FCS) and credit unions enjoy special tax treatments giving these institutions a competitive advantage over banks. The special tax treatments were gifted to these nonbank lenders in order to encourage lending to certain groups of individuals. The advantages afforded to these institutions need to be reexamined and reduced in terms of tax exemptions and regulatory burden. For example, the FCS paid only 4.5 percent tax rate last year while earning approximately $5 billion in net income. Why should multibillion dollar GSE lenders be exempted from taxation earned on their real estate and mortgage lending when competing to serve the same borrowers as much smaller community banks? Why were FCS institutions exempted from the burdens of the Dodd-Frank Act since the FCS also has authority to make residential mortgage loans in small rural towns to the same types of borrows community banks serve? Of great concern, we see the FCS's regulator allowing FCS institutions to venture into non-farm lending, although they were not created to serve both farm and non-farm customers.

We are also very concerned about a new regulatory proposal to allow credit unions to dramatically increase their business lending.

The increased business lending activity by both the credit unions and the FCS institutions will come at the expense of community banks which will lose loans to these institutions due to their tax exemptions. These institutions are all too happy to siphon away loans from community banks, but they strenuously refuse to pay taxes that are used to finance schools and other services necessary to keep America's communities viable.

These Challenges Have Costs for Banks and the Communities They Serve

While the situation is different for every bank, it should be helpful to examine specific financial burdens to our bank. The staff at First National Bank reviewed our records to determine the actual cost of regulation. Specifically, we have found that we spend over $222,000 on compliance costs every year. This amounts to over 18 percent of our total overhead.

Be mindful, this analysis doesn't include any personnel expense. We have 33 FTE's, and we assume that one could conclude four of them spend their time on studying, enforcing and analyzing regulations. The financial burden of unnecessary regulations is a struggle for all community banks.

First National Bank

Regulatory Compliance Costs

Regulatory Software:	$	56,093
Compliance Educ:	$	19,916
Accounting Audits:	$	13,676
Misc. Audits:	$	5,354
Banker's Comp:	$	34,407
Examiners-OCC:	$	92,685
Total:	$	222,131

Overhead Expense: $ 1,189,994

Regulation as a Per Cent of Overhead: 18.7%

Ultimately our customers and communities are the ones who feel the true cost of this burden. They feel it in the form of more expensive financial services and fewer options. For example 58 percent of banks have held off or canceled the launch of new products—designed to meet consumer demand—due to expected increases in regulatory costs or risks. Additionally, 44 percent of banks have been forced to reduce existing consumer products or services due to compliance or regulatory burden. This means less credit in our communities. Less credit means fewer jobs, lower income for workers, and less economic growth.

Commonsense Solutions Would Help Banks Alleviate This Burden

I believe my time in front of this Subcommittee would be wasted if some possible solutions weren't offered. However, I know enough about the legislative process to also know that if I suggested that CFPB be repealed entirely, my time would also be wasted. The current regulatory environment in which we live was created with good intentions. But, as with many good intentions, there are always unintended consequences. That, I believe, is the case we find ourselves in today. Below I note selected bills that would provide viable and effective solutions to many of the concerns I have noted in this testimony.

The Community Lending Enhancement and Regulatory Relief Act of 2015 (the "CLEAR Act", S.812), introduced by Senators Jerry Moran and Jon Tester, would provide qualified mortgage status for any mortgage held in portfolio and an exemption for loans held in portfolio from new escrow requirements for higher priced mortgages for any lender with less than $10 billion in assets. Like S.1816 (noted above), S.812 would provide an exemption from internal control attestation requirements for community banks with assets of less than $1 billion.

Chairman Pat Toomey and Senator Joe Donnelly have introduced legislation (S.970) which would allow a highly rated bank (CAMELS 1 or 2) with assets of less than $1 billion to be examined on an 18-month cycle. Under current statute and agency guidance, only a highly rated bank with assets of less than $500 million is allowed to use an 18-month exam cycle; all others are on a 12-month cycle. Preparations for bank exams, and the exams themselves, distract bank management from serving their communities to their full potential. S.970 is identical to a provision of S.1484 noted above.

In addition to a longer exam cycle, we would request there be some directive given to bank examiners in the area of cash flow lending vs. equity and collateral based lending. As previously stated, First National Bank in Philip is an equity lender, and over our history, we have experienced few losses. At least, we would ask that examiners understand the uniqueness of farming and ranching and the difficulty in cash flowing with fluctuating grain and livestock prices.

In addition to these bills, we hope that account overdrafts can be managed internally, especially for rural community banks. We know our customers' needs and don't want to be forced to close accounts because of excessive oversight.

Call reports could be simplified to reflect a bank's business model and size. It seems unreasonable to assume that the same call report is needed for a $10 billion bank as a $250 million bank. One size does not fit all.

This hearing is most likely not the time or place to take up the issue of Farm Credit System and credit unions, but the issue needs to be noted.

Conclusion

Credit will only remain available in rural America as long as local financial institutions remain healthy and viable. Local banks, many of which have been in business for generations, understand the risks associated with lending in rural areas. They are good at what they do. Now, many of them feel under assault by excessive regulations. Regulations that take the "one size fits all" approach don't understand the unique relation rural banks play in individuals' lives and communities.

First National Bank in Philip recently hired a team of auditors to complete a Directors' exam. At the exit interview, the auditor stated that banks are more highly regulated than hospitals. I sit on the local hospital board and understand all too well how highly regulated hospitals are. To have someone who examines both state that banks are more regulated was an eye opener.

We ask for regulation and oversight that is truly beneficial to rural consumers who rely on local banks for credit. The focus should be on enforcing existing laws rather than creating new rules and regulations that threaten banks' future existence. Rural banks can compete, but they can't compete while burdened with red tape and unnecessary, unfocused regulations. It's not fair to local banks and the communities that rely on them.

At the end of the day, this isn't about banks. It's not about First National Bank in Philip. It is about people. It is about communities and lifestyles of those who populate rural America. We have a unique opportunity this morning to begin the process of effecting change which will truly help the residents of rural America.

Thank you and I look forward to your questions.

PREPARED STATEMENT OF CARRIE WOOD

President and Chief Executive Officer, Timberland Federal Credit Union, DuBois, Pennsylvania

October 28, 2015

Chairman Toomey, Ranking Member Merkley, Members of the Subcommittee: Thank you for the opportunity to testify at today's hearing. The Committee's continued focus on the regulatory burden facing small community financial institutions is critical.

My name is Carrie Wood, and I am president and chief executive officer of Timberland FCU, a $60 million credit union located in DuBois, Pennsylvania. We serve 9,800 members, over three-quarters of which are low-income. The 15 full-time members of my staff and I work hard every day to help meet their financial service needs.

As a CEO of a credit union serving a rural area, I am faced with the mile-wide, inch-deep dilemma that other credit unions and small banks face: I am forced to comply with many of the same regulations as the largest financial institutions, but with far fewer resources than the too-big-to-fail banks.

While my title is CEO, I am also the security administrator, human resources department, compliance officer, marketing and business development department, backup IT person and NMLS administrator. To help me keep up with the changes in rules coming out of Washington, I have assigned a team of five staff, a full third of my total, from various departments across the credit union.

When these team members are working on compliance issues, they are not serving our members. They're not helping them get loans. They're not providing financial counseling. They're not helping improve our processes and how we offer our services.

The time and resources we spend complying with rules designed for bad actors and large institutions are unnecessary costs that rob our members of the services we could have provided them.

Since the beginning of the financial crisis, credit unions have been subjected to at least 202 regulatory changes from nearly two dozen Federal agencies totaling more than 6,000 Federal Register pages. These numbers do not take into account regulatory changes that may emanate from State regulators. Every time a rule is changed credit unions and members incur costs—even if we are not ultimately required to comply with the rule. The credit union staff and board must make the time to understand the new requirement, modify our computer systems, update our internal processes, properly train staff on the compliance liability and new policies, design and print new forms and produce materials to help the credit union member understand the new requirement. Even simple changes in regulation cost credit unions thousands of dollars and many hours: time and resources that could be more appropriately spent on serving the needs of credit union members.

Rules are often changed in the name of consumer protection, but when they make it harder or more expensive for me to serve my members, that's not consumer protection. Sometimes the new rules are difficult for us to decipher, and more so to explain and educate our members on the changes we are forced to make.

Since the passage of the Dodd-Frank Act the sheer volume and complexity of the rules that we must comply have increased substantially, which means that I need to hire specialists in order to comply and keep the regulators from citing me for violations. One of the most recent demands is that NCUA would like me to have two technology specialists on staff to comply with cyber security requirements. As CEO, I above anyone, understand the importance of protecting my members, however, it can be very expensive and difficult to attract high quality personnel with the necessary experience because they are not always found locally, and they don't often want to give up urban life for rural living. A real-world issue that is not considered by my regulator.

The constant churn of new regulatory requirements not only takes a hit on our bottom line—which for a not-for-profit institution directly affects our members and service—it also has kept us from entering new markets.

Our members want us to offer small business loans, but we are hesitant because of the regulatory and statutory restrictions in place today.

We also delayed our entry into indirect auto lending because the ongoing dilemma of who is going to oversee the program and administer the day-to-day, what compliance issues are there, when are we going to train for it, what procedures do we need, who will audit, what is NCUA going to be require in our policy and for a compliant program. We know these programs are on the regulators radar and have proceeded with caution. As a result, we find ourselves behind on meeting member demands, perhaps to the detriment of their credit, in the name of convenience.

On top of that, the CFPB has added an entire new level of regulatory anxiety for my credit union and others like us. In the interest of time, I will raise an immediate issue we are facing related to the implementation of the TILA–RESPA Integrated Disclosure (TRID) forms. But rest assured there are many others.

We have known TRID is coming down the pipe for some time and we have worked with our vendors to comply. TRID is a complicated rule and the CFPB provided us absolutely no transition time. One day we have to do things the way we've always done them; the next day, we were required to abruptly change and do things differently. No transition period. No enforcement delay. No protection from legal liability if we made a mistake. As a small institution, we rely on outside vendors on many things. With this particular change, we are vendor-dependent to ensure our data processing system pulls all the right information into the correct fields on the forms. When we ran into an unanticipated problem after we flipped the switch to the new form, we were forced to manually input information into the new forms, slowing down the process for our members and potentially exposing us to errors.

I know the NCUA, which will supervise our compliance, has said that their examiners are going to exercise tolerance for a reasonable amount of time. But what I don't understand is why Congress will not protect us from legal liability as we work out the kinks in the system. We're trying to comply as we continue to serve our members, but I don't want to see our credit union hit with a lawsuit 3 or 5 years down the road because we made a mistake in the first few months of this new system.

Despite the ever increasing regulatory burden, we continue to do what we can to help our members. And, in closing, let me tell you about a few of those services.

When members open an account, we offer a free credit review. We are also working on having three current staff members receive their Certified Financial Counselor designation to have free, in-house credit counseling for our members.

We participate in our State program called "Better Choice", which allows us to offer an alternative to pay day lending. For members to take advantage of this program, we require financial counseling and partner with our local Community Action to provide that counseling. Timberland FCU makes absolutely no money on this program; we offer it as a member service.

Additionally, small, underwritten loans are pretty common here. Members request small loans to get fuel, payoff pay day lenders, buy an Amish mattress, among other things. I once did a loan for a man who just had his 5 granddaughters move back in with him because his daughter lost her job. He needed $200 because the girls had contracted a medical condition at school. He couldn't afford the treatments until his next social security check, and the girls couldn't go back to school until he took care of them. I've written car loans for members who've totaled their cars due to hitting a deer, and once, for a member who hit a horse. Public transportation is a struggle because we are so spread out. I drive 23 miles one way to work every day, but it only takes me ½ hour. My members need a car, which makes expediency of these types of loans a must. The work we do at Timberland FCU—like the work credit unions across the country do—helps families stay in their homes, members hold their jobs, and children stay in school. We're a lifeline for our members.

My members need their credit union to be in a position to help them in these situations. Unfortunately, every time a rule is created or modified it makes it much more difficult for us to be there when they need us.

There is a reason that we are losing a credit union a day—and it's coming out of Washington in the form of ever-changing and ever-increasing regulatory burden. Again, your focus on the crisis facing small community financial institutions is critical, and I applaud your efforts.

Thank you for the opportunity to testify.

PREPARED STATEMENT OF SARAH EDELMAN

DIRECTOR, HOUSING POLICY, CENTER FOR AMERICAN PROGRESS

OCTOBER 28, 2015

Introduction

Thank you, Chairman Toomey, Ranking Member Merkley, and Members of the Subcommittee for the invitation to appear before you today. My name is Sarah Edelman, and I am the Director of Housing Policy at the Center for American Progress. Thank you for holding a hearing on this important topic.*

Consumers living in rural areas rely on community banks to meet their credit needs. These banks provide vital support to the small businesses, farmers, and homeowners that make rural economies function. However, for decades, the number of community banks serving these areas has been declining. [1]

This decline long precedes the financial reform measures put into place after the 2007 financial crisis. [2] There are many reasons for this trend including slowing population growth in rural areas, changes in the financial market, and changes to interstate banking rules that made it easier for banks to consolidate.

I plan to make the following points in my testimony today:

- Many rural economies are in trouble. Community banks can, and should be, an important partner in revitalizing rural economies.
- Rolling back financial regulation is not the right approach to support community banks. Deregulation of the banking sector increases risk to the broader economy and to community banks.
- A comprehensive approach is needed to support rural communities and the banks that serve them.

Community Banks Provide a Vital Source of Credit for Consumers Living in Rural Areas

For many families living in rural areas, access to lending is severely limited. For generations, community banks have served as important partners to small businesses, family farms, and families seeking to buy or refinance a home. Often, the

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*This testimony is based primarily on an issue brief published earlier this year by the Center for American Progress about financial reform and community banking and recent testimony provided by the Center to the House Subcommittee on Economic Growth, Tax, and Capital Access. The full issue brief is attached: David Sanchez, Sarah Edelman, and Julia Gordon, "Do Not Gut Financial Reform in the Name of Helping Small Banks", Center for American Progress: July, 2015, available at *https://www.americanprogress.org/issues/housing/report/2015/07/07/113119/do-not-gut-financial-reform-in-the-name-of-helping-small-banks/*. For the testimony, see: Julia Gordon, Testimony before the U.S. House Committee on Small Business Subcommittee on Economic Growth, Tax, and Capital Access, "Financing Main Street: How Dodd-Frank Is Crippling Small Lenders and Access to Capital", September 17, 2015, available at *http://smbiz.house.gov/uploadedfiles/9-17-2015_gordon_testimony.pdf.*

[1] David Sanchez, Sarah Edelman, and Julia Gordon, "Do Not Gut Financial Reform in the Name of Helping Small Banks", Center for American Progress: July, 2015, available at *https://www.americanprogress.org/issues/housing/report/2015/07/07/113119/do-not-gut-financial-reform-in-the-name-of-helping-small-banks/*.

[2] Ibid.

only source of credit for rural consumers is their local community bank.[3] Approximately one out of every five counties in the United States is served exclusively by community banks—and three quarters of these counties are located in rural areas.[4]

While community banks hold a diminishing share of the banking sector's total assets—14 percent in 2011, according to the FDIC—they continue to make nearly half of all small business and agricultural loans.[5] Lending to small businesses and farmers remains a core part of the community bank business model, even as larger banks have shifted away from this type of lending.

In the wake of the recession, there is a great need for capital in rural communities. The small business and mortgage loans community lenders offer in rural communities will play an important role in supporting economic recovery and a recovery in the housing market.[6] Even as the broader housing market is recovering, some rural housing markets are seeing conditions further deteriorate. The percentage of mortgaged homes with negative equity in nonmetropolitan rural counties increased from an average of 11 percent in the second quarter of 2011 to 20 percent in the first quarter of 2015.[7]

Without home equity, small business owners and entrepreneurs have fewer reserves to draw upon to make investments in their existing business or to start a new one. Through investing in local businesses, community banks can help to stimulate economic recovery in rural areas.

Financial Reform Legislation Is Not Responsible for the Decline in the Number of Community Banks

Despite the important role community banks[8] play in counties across the country, the number of them has declined precipitously for over a generation.[9] This 30-year decline has very little to do with postcrisis financial regulation. Factors causing the decline include an increasingly complex financial services sector where the size of the banking institution matters for profitability, economic challenges in the communities these banks tend to serve, and changes in interstate banking laws that make it easier for bank mergers and consolidation to take place.

The number of community banks has declined at a rate of about 300 per year over the past 30 years, mostly through consolidation with other banks, according to the FDIC.[10] This decline began far before the 2007 financial crisis and the subsequent Dodd-Frank Wall Street Reform and Consumer Protection Act. The decline has continued at about the same pace since regulators began implementing the law.[11]

[3] Federal Deposit Insurance Corporation, "FDIC Community Banking Study", December 2012, pp.3–5, available at *https://www.fdic.gov/regulations/resources/cbi/report/cbi-full.pdf.*

[4] Ibid, p.I.

[5] Ibid.

[6] Forthcoming, Michela Zonta and Sarah Edelman, "The Uneven Housing Recovery", Center for American Progress: October, 2015.

[7] Ibid.

[8] There is no one definition for a small or community bank, but many analysts use asset size, such as a threshold of $1 billion or less, to characterize such a bank. The FDIC uses a definition that takes into account a bank's lending and deposit-taking activities, as well as the geographic location of its branches. Through its definition, the FDIC eliminates certain specialty institutions and institutions that operate on more of a national scale. Source: David Sanchez, Sarah Edelman, and Julia Gordon, "Do Not Gut Financial Reform in the Name of Helping Small Banks", See also: Federal Deposit Insurance Corporation, "FDIC Community Banking Study".

[9] Federal Deposit Insurance Corporation, "FDIC Community Banking Study".

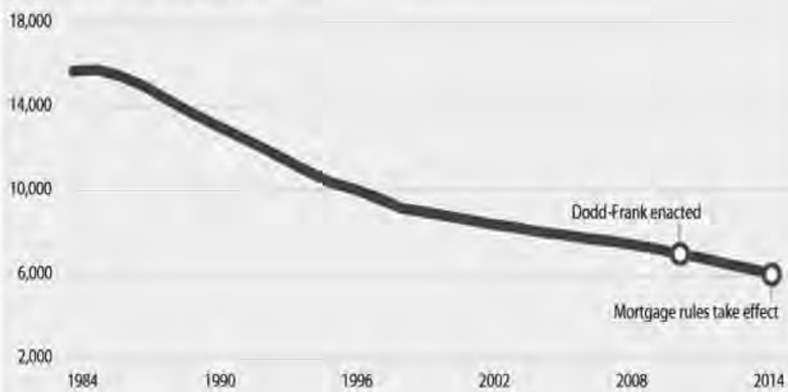
[10] David Sanchez, Sarah Edelman, and Julia Gordon, "Do Not Gut Financial Reform in the Name of Helping Small Banks".

[11] Ibid.

FIGURE 2

Financial reform is not causing the declining number of community banks

Number of U.S. community banks



Source: Federal Deposit Insurance Corporation, "Historical Community Banking Reference Data," available at https://www.fdic.gov/regulations/resources/cbi/data.html (last accessed May 2015).

The number of locally owned community banks has also declined, particularly in rural areas from approximately 80 percent in 1976 to approximately 20 percent in 2007.[12]

While the number of bank offices operating outside of metropolitan areas appears to have been stable during the same period, the offices are typically owned by out-of-county or out-of-State banks which may be less likely to consider "soft data" when making loans, such as the applicant's reputation for financial responsibility within the community.[13]

Over the past 30 years, more than 80 percent of banks that have exited the market have not failed, but rather, have merged with an unaffiliated bank or consolidated with another chartered bank, sometimes within the same organization.[14] Many banks took advantage of changes in interstate banking rules in the 1980s and 1990s to expand their scale and geographic footprint through mergers and consolidations. Others consolidated because they were at risk of failure.[15]

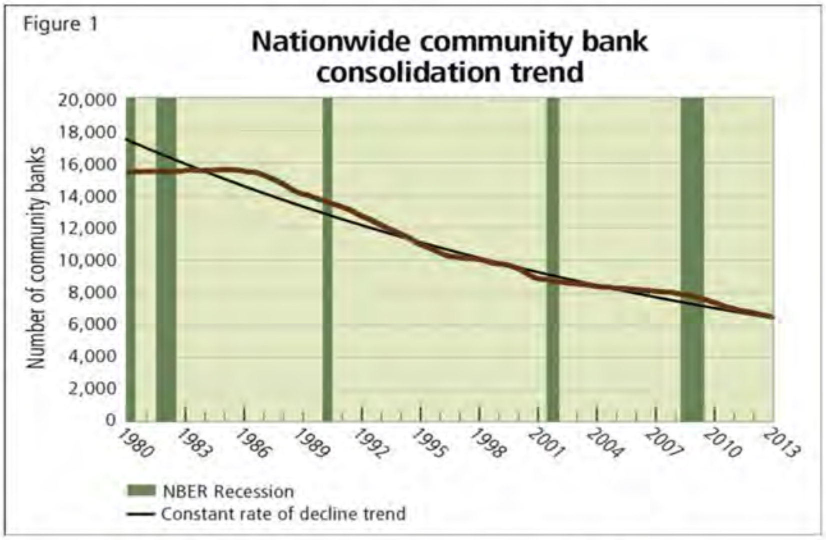
[12] C. M. Tolbert, "Restructuring of Financial Industry: Disappearance of Locally Owned Traditional Financial Services in Rural America", *Rural Sociology* 2014.

[13] Ibid.

[14] David Sanchez, Sarah Edelman, and Julia Gordon, "Do Not Gut Financial Reform in the Name of Helping Small Banks".

[15] Federal Deposit Insurance Corporation, "FDIC Community Banking Study", pp.I–II.

Figure 1



Source: Minneapolis Federal Reserve "Assessing Community Bank Consolidation."[16]

Why are there fewer community banks now than there were in the 1980s? First, the financial market has become more complex in recent decades. Large banks can benefit from the economies of scale that make certain operations more efficient, while small banks cannot. The Government Accountability Office, or GAO, has concluded that, "larger banks generally are more profitable and efficient than smaller banks, which may reflect increasing returns to scale." [17] These advantages are particularly evident in mortgage lending, where technology can make it much easier for a bank to make and service a loan. [18]

Community banks are also victim to the population loss and economic challenges afflicting rural communities. For example, 86 percent of rural counties in the Great Plains experienced population loss between 1980 and 2010. [19] As jobs become more concentrated in metropolitan areas, many young people are leaving rural areas for these job centers. [20] Further, employment in urban centers has generally recovered more quickly than in rural areas, and rural workers earn about 20 percent less than those in urban areas. [21] Unlike a larger bank that may have branches across many types of geographies, a community bank may be more vulnerable in the case of a local economic downturn or if its local customer base declines.

[16] Ron J. Feldman and Paul Schreck, "Assessing Community Bank Consolidation", Federal Reserve Bank of Minneapolis, February 6, 2014, available at *https://www.minneapolisfed.org/research/economic-policy-papers/assessing-community-bank-consolidation.*

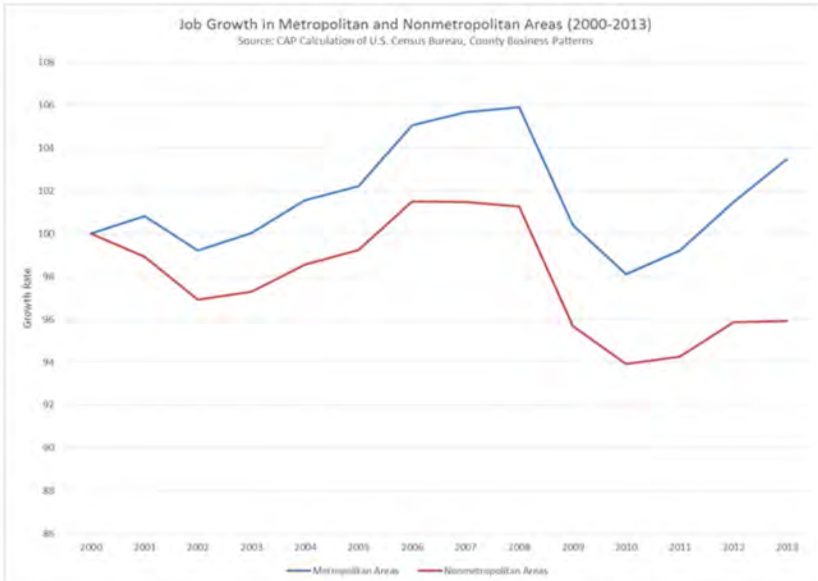
[17] U.S. Government and Accountability Office, "Community Banks and Credit Unions: Impact of the Dodd-Frank Act Depends Largely on Future Rule Makings", September 2012, p.10, available at *http://www.gao.gov/assets/650/648210.pdf.*

[18] Dr. Adam J. Levitin, Testimony before the U.S. House Committee on Financial Services, "Preserving Consumer Choice and Financial Independence", March 18, 2015, available at *http://financialservices.house.gov/uploadedfiles/hhrg-114-ba00-wstate-alevitin-20150318.pdf.*

[19] Federal Deposit Insurance Corporation, "FDIC Community Banking Study", pp.3–8.

[20] CAP calculation of U.S. Census Bureau 2000–2010, "County Business Patterns"; and, "Federal Deposit Insurance Corporation", "FDIC Community Banking Study", pp.3–8.

[21] U.S. Department of Agriculture Economic Research Service, "Employment & Education", available at *http://www.ers.usda.gov/topics/rural-economy-population/employment-education.aspx.*



Finally, it is true that smaller institutions may have a more difficult time managing the cost of complying with regulation, as the resources required to report to State and Federal regulators require a greater share of the bank's resources. However, many of these compliance costs long precede the Dodd-Frank Wall Street Reform Act. As described in greater detail below, regulators have been very careful to make sure community banks have the flexibility they need to meet the new financial regulatory requirements.

Despite all of the challenges described above, community banks have performed relatively well in recent years. Both smaller and larger community banks originated a larger share and number of home purchase mortgages today than they did in 2010. [22] Last year, community banks increased their lending volume at almost twice the rate of larger banks. [23] Data from the FDIC also show that the performance and financial health of community banks has experienced consistent improvement over the past 5 years. [24]

Gutting Financial Reform Would Do Little To Help Community Banks and May Further Undermine Community Banks

Policymakers should continue to monitor the implementation of financial regulatory requirements to ensure that compliance is as simple as possible. However, undermining financial reform in the name of helping small banks in rural areas is not the right approach. Returning to precrisis regulatory standards would ultimately put more banks at risk of failure.

Most of the bank failures that have occurred over the past 30 years have occurred during a financial or economic crisis. [25] Community banks are no exception to this

[22] Center for American Progress analysis of Home Mortgage Disclosure Act, or HMDA, data for owner-occupied, 1–4 unit home purchase mortgages for 2010 and 2013. Community banks are identified using the FDIC's definition; smaller community banks are those with less than $1 billion in assets. See Consumer Financial Protection Bureau, "The Home Mortgage Disclosure Act", available at *http://www.consumerfinance.gov/hmda/explore* (last accessed May 2015); Federal Deposit Insurance Corporation, "Community Banking Reference Data", available at *https://www.fdic.gov/regulations/resources/cbi/data.html* (last accessed June 2015).

[23] Kate Davidson, "Dodd-Frank's Effect on Small Banks Is Muted", *The Wall Street Journal*, October 4, 2015, available at *http://www.wsj.com/articles/dodd-franks-effect-on-small-banks-is-muted-1443993212*.

[24] Federal Deposit Insurance Corporation, "Quarterly Banking Profile: Second Quarter 2015", available at *https://www.fdic.gov/bank/analytical/quarterly/2015_vol9_3/FDIC_2Q2015_v9n3.pdf*.

[25] Richard Brown, Testimony to the U.S. Senate Committee on Banking, Housing, and Urban Affairs, "Lessons Learned From the Financial Crisis Regarding Community Banks", June, 13,

trend and have had failure rates comparable to other types of banks.[26] According to Richard Brown, the former chief economist of the FDIC, “To the extent that future crises can be avoided or mitigated, bank failures should contribute much less to future consolidation.”[27]

The Great Recession negatively impacted the community banking sector. While generally community banks did not engage in the type of predatory residential mortgage lending that brought down larger banks, many community banks also failed in the wake of the financial crisis. During the bubble years, some community banks aggressively expanded their commercial lending, often in the form of construction loans. When the financial crisis and subsequent recession caused home prices to decline, these banks suffered crippling losses and many failed.[28] Between 2008 and 2011, 419 of the 481 depository banks that failed were small banks.[29]

The long-term health of community banking depends on a healthy economy and a stable financial market. Strong regulation helps banks of all sizes establish a sturdy foundation and will help prevent future financial crises, and the loss of more community banks.

Moreover, regulators have already taken steps to ensure that community banks are able to continue lending in a safe way. Recognizing that community banks may need more flexibility to serve rural and nonmetropolitan markets, regulators have already provided small banks with a series of exemptions from the new mortgage rules:

- Small banks have greater underwriting flexibility when making Qualified Mortgage, or QM, loans—those that are eligible for the highest level of protection from legal challenges—because if small banks hold the loans on portfolio, they are not bound to the fixed debt-to-income ratio limit that applies to larger lenders.[30]
- Small institutions serving rural or underserved areas can get QM protection for loans that require a balloon payment, although the general QM definition bans balloon loans.[31]
- The CFPB recently expanded the definition of small institutions, as well as the rural definition, so that more banks now qualify for a variety of mortgage rule exemptions, including more flexibility to make QM loans.[32] Under the new definitions, roughly 93 percent of all institutions engaged in mortgage lending are eligible for these exemptions.[33]
- Small institutions serving rural or underserved areas are exempt from requirements that they maintain escrow accounts for higher-cost loans.[34]
- Small creditors are exempt from most mortgage-servicing rules.[35]

2013, available at *http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=9a223606-f64b-4a72-9874-b4886f2f9f2b.*

[26] The FDIC Community Banking Research Project, “Community Banking by the Numbers”, presentation at the FDIC Future of Community Banking Conference, February 12, 2012, slide 15, available at *https://www.fdic.gov/news/conferences/communitybanking/community_banking_by_the_numbers_clean.pdf.*

[27] Richard Brown, Testimony to the U.S. Senate Committee on Banking, Housing, and Urban Affairs, p.4.

[28] Federal Deposit Insurance Corporation, “FDIC Community Banking Study”.

[29] Richard Brown, Testimony to the U.S. Senate Committee on Banking, Housing, and Urban Affairs, p.1.

[30] Consumer Financial Protection Bureau, “Ability-To-Repay and Qualified Mortgage Rule: Small Entity Compliance Guide” (2013), Section 4.3, available at *http://files.consumerfinance.gov/f/201308_cfpb_atr-qm-implementation-guide_final.pdf.*

[31] Consumer Financial Protection Bureau, “Ability-To-Repay and Qualified Mortgage Rule: Small Entity Compliance Guide”, Section 4.6.2.

[32] Consumer Financial Protection Bureau, “CFPB Issues Proposal To Facilitate Access To Credit in Rural and Underserved Areas”, Press release, January 29, 2015, available at *http://www.consumerfinance.gov/newsroom/cfpb-issues-proposal-to-facilitate-access-to-credit-in-rural-and-underserved-areas/.*

[33] Consumer Financial Protection Bureau, “Amendments Relating to Small Creditors and Rural or Underserved Areas Under the Truth in Lending Act (Regulation Z)” (2015), available at *http://files.consumerfinance.gov/f/201501_cfpb_amendments-relating-to-small-creditors-and-rural-or-underserved-areas.pdf.*

[34] Consumer Financial Protection Bureau, “TILA Higher Priced Mortgage Loans (HPML) Escrow Rule: Small Entity Compliance Guide” (2014), Section 4, available at *http://files.consumerfinance.gov/f/201401_cfpb_tila-hpml-escrow_compliance-guide.pdf.*

[35] Consumer Financial Protection Bureau, “2013 Real Estate Settlement Procedures Act (Regulation X) and Truth in Lending Act (Regulation Z) Mortgage Servicing Final Rules: Small Entity Compliance Guide” (2013), Section 3, available at *http://files.consumerfinance.gov/f/201306_cfpb_compliance-guide_2013-mortgage-servicing-rules.pdf.*

- An array of mission-oriented lenders, such as Community Development Financial Institutions and State housing finance agencies, are fully exempt from the entire CFPB Ability-To-Repay requirement.[36]

There are also various opportunities for small banks to weigh in with regulators about the regulatory process. The CFPB, the FDIC and the Federal Reserve have all formed community bank advisory councils since the financial crisis. Moreover, the CFPB has to permit small businesses, including community banks, to weigh in on rulemaking efforts before proposed rules are released for public comment. The voices of community banks are well represented and regulators continue to be responsive to their concerns.

These exemptions may actually help to make community banks more competitive relative to larger banks serving the same communities. Rolling back regulations for bigger institutions in the name of helping small banks may erode this competitive advantage while exposing all banks to greater risk of failure.

A More Sensible Approach

Instead of pursuing sweeping deregulatory legislation that will do little to help small banks, policymakers should take a more comprehensive approach.

First, regulators are the best positioned to work with community banks to help ensure that regulatory compliance is as simple and straightforward as possible. As new regulations are fully implemented, the CFPB, FDIC, and other regulators should continue to communicate with small banks and to monitor for any challenges that may arise. To the extent the data suggest specific policy changes that can help community banks address compliance costs without weakening consumer protections or endangering their safety and soundness, policymakers should pursue these reforms in a targeted and careful way. Otherwise, rolling back financial regulation will simply expose consumers, communities, or our banking system to greater risk.

More attention should also be directed toward helping community banks upgrade technological systems. Improved technology could help bring down compliance costs and reduce the cost of lending in the long run. The recent CFPB e-closing pilot provided helpful learning about ways technology can be used to improve efficiency and generate savings for consumers and banks alike.[37] More research is needed to identify best practices among community banks and ways the Government may be able to support technological innovation among community banks.

Finally, the Federal Government has served as an important partner to rural communities and community banks over the years. Lending programs through the United States Department of Agriculture, or USDA, and Small Business Administration, or SBA, help to ensure that the credit needs of rural businesses and homeowners are met.[38] In addition to these lending programs, both agencies can partner with community banks to help them serve their communities. While Congress has said it will fully fund critical lending programs in the coming year, lawmakers have proposed serious cuts to the agencies responsible for administering them.[39] Undermining the capacity of USDA and SBA to manage these programs is a bad idea for consumers in rural areas as well as for taxpayers. These agencies should be fully funded to help ensure that lending programs are available for prospective homeowners and small businesses in rural communities.

The Federal Housing Finance Agency can also take steps to support more lending in rural areas. The FHFA is currently working to finalize the proposed duty to serve rule, a rule mandated by the Housing and Economic Recovery Act of 2008 that re-

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[36] Consumer Financial Protection Bureau, “Ability-To-Repay and Qualified Mortgage Rule: Small Entity Compliance Guide”, Section 3.13.

[37] Consumer Financial Protection Bureau, “CFPB Study Finds Electronic Mortgage Closings Can Benefit Customers”, Press release, August 5, 2015, available at *http://www.consumerfinance.gov/newsroom/cfpb-study-finds-electronic-mortgage-closings-can-benefit-consumers/*.

[38] The White House Council of Economic Advisors, “Strengthening the Rural Economy—Growing New Businesses in Rural America”, available at *https://www.whitehouse.gov/administration/eop/cea/factsheets-reports/strengthening-the-rural-economy/growing-new-businesses-in-rural-america*.

[39] Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Bill, 2016, H. Rept. 205, 114 Cong. 1 Sess. June 14, 2015, available at *https://www.congress.gov/114/crpt/hrpt205/CRPT-114hrpt205.pdf*; Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Bill, 2016, S. Rept. 82, 114 Cong. 1 Sess. July 16, 2015, available at *https://www.congress.gov/114/crpt/srpt82/CRPT-114srpt82.pdf*; Financial Services and General Government Appropriations Bill, 2016, H. Rept. 194. 114 Cong. 1 Sess. July 9, 2015, available at *https://www.congress.gov/114/crpt/hrpt194/CRPT-114hrpt194.pdf*; and, Financial Services and General Government Appropriations Bill, 2016, S. Rept. 97. 114 Cong. 1 Sess. July 30, 2015, available at *https://www.congress.gov/114/crpt/srpt97/CRPT-114srpt97.pdf*.

quires Fannie Mae and Freddie Mac to help ensure that the credit needs of underserved and rural markets are met.[40] FHFA should encourage Fannie Mae and Freddie Mac to work more with community lenders in rural areas and to help design products that meet the needs of consumers in rural communities.

Conclusion

Community banks play an important role in rural communities. Over the last generation, there has been a significant decline in the number of these banks. Changes in the underlying market are largely responsible for their decline. However, in recent years the community banks that are serving rural communities have become stronger and are doing more consumer lending. Going forward, regulators and Federal agencies should continue to partner with community banks to help them revitalize local economies.

[40] "Duty To Serve Underserved Markets for Enterprises", Advanced Notice of Proposed Rulemaking, Federal Housing Finance Agency, 12 CFR. Part 1282, available at *http://www.gpo.gov/fdsys/pkg/FR-2009-08-04/pdf/E9-18515.pdf.*

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM TERRY FOSTER

Q.1. In the Dodd-Frank Act, Congress directed the Federal Deposit Insurance Corporation (FDIC) to change how it calculates deposit insurance assessments. At the time, the Independent Community Bankers of America (ICBA) estimated that the change would save community banks $4.5 billion in just the first 3 years the change was in effect. Could you estimate how much your institution has saved in total assessments because of this change?

A.1. For assessment periods September 30, 2011, through June 30, 2015, MCS Bank paid BIF premiums of $340,000. In comparison, using an assumed* premium rate for future periods had the Domestic Deposit basis for premium assessments remained in place, estimated premiums would have been $522,000, or $182,000 higher than what they are under the current assessment model.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR WARREN FROM ROGER A. PORCH

Q.1. In the Dodd-Frank Act, Congress directed the Federal Deposit Insurance Corporation (FDIC) to change how it calculates deposit insurance assessments. At the time, the Independent Community Bankers of America (ICBA) estimated that the change would save community banks $4.5 billion in just the first 3 years the change was in effect.[1] Could you estimate how much your institution has saved in total assessments because of this change?

A.1.

Year	Avg Assets	FDIC Ins	Avg Deposits	FDIC Ins as % of Avg Assets	FDIC Ins as % of Avg Deposits
2002	$ 107,334,825.00	$ 14,419.00	$ 86,803,000.00	0.013%	0.017%
2003	$ 114,540,462.00	$ 13,804.00	$ 89,346,000.00	0.012%	0.015%
2004	$ 116,708,074.00	$ 13,224.00	$ 93,787,000.00	0.011%	0.014%
2005	$ 115,703,801.00	$ 12,474.00	$ 93,038,000.00	0.011%	0.013%
2006	$ 119,440,917.00	$ 11,382.00	$ 94,036,000.00	0.010%	0.012%
2007	$ 122,016,706.00	$ 11,340.00	$ 98,221,000.00	0.009%	0.012%
2008	$ 136,828,411.00	$ 13,691.00	$ 99,212,000.00	0.010%	0.014%
2009	$ 149,858,888.00	$ 202,884.00	$ 116,068,000.00	0.135%	0.175%
2010	$ 160,456,138.00	$ 154,201.00	$ 126,912,000.00	0.096%	0.122%
2011	$ 166,597,868.00	$ 111,946.00	$ 135,599,000.00	0.067%	0.083%
2012	$ 178,255,953.00	$ 80,225.00	$ 141,710,000.00	0.045%	0.057%
2013	$ 220,020,231.00	$ 106,811.00	$ 191,534,000.00	0.049%	0.056%
2014	$ 243,258,811.00	$ 123,533.00	$ 216,194,000.00	0.051%	0.057%
2015	$ 252,332,797.00	$ 127,991.00	$ 220,851,000.00	0.051%	0.058%

Note: For 2015, we only have the actual number through October, so the number shown is annualized.

* The "assumed" premium rate is MCS Bank's average BIF assessment rate for the prior thirteen (13) quarters (beginning with the 3/31/2008 assessment period) during which the Bank paid BIF premiums.

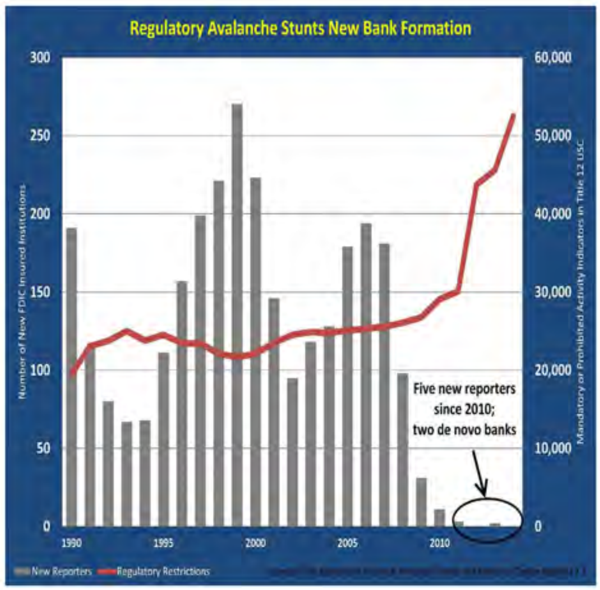
Prior to 3/31/2008, MCS Bank, based upon its risk profile, was only subject to the FICO Assessment and thus did NOT pay BIF premiums.

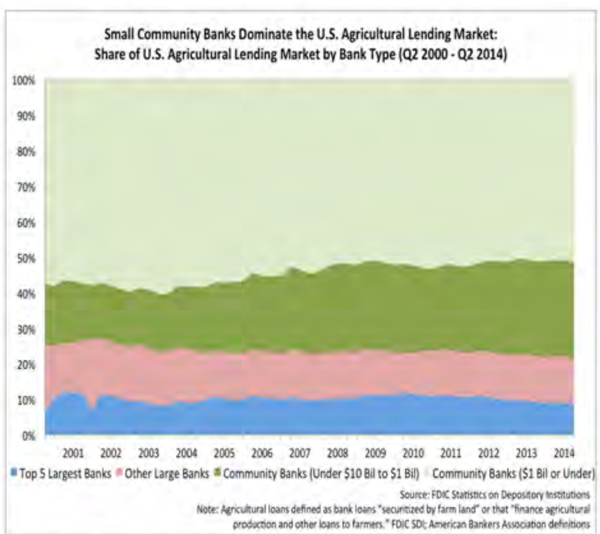
Despite the "reduction" of premiums which resulted from the Dodd-Frank Act, BIF premiums remain high from a historical perspective, representing eight basis points of pretax earnings/average assets.

[1] *http://www.icba.org/files/ICBASites/PDFs/FinalBillDepositInsurance.pdf*

Additional Material Supplied for the Record

CHARTS SUBMITTED BY CHAIRMAN TOOMEY





Source: Lux, Marshall and Robert Greene. "The State and Fate of Community Banking," Mossavar-Rahmani Center for Business and Government: http://www.hks.harvard.edu/centers/mrcbg/publications/awp/awp37

SUMMARY OF THE DEMOCRATIC ALTERNATIVE TO THE "FINANCIAL REGULATORY IMPROVEMENT ACT OF 2015" SUBMITTED BY SENATOR MERKLEY

SUMMARY OF THE DEMOCRATIC ALTERNATIVE TO THE "FINANCIAL REGULATORY IMPROVEMENT ACT OF 2015"

TITLE I. HELPING COMMUNITY LENDERS

Section 101. Community Bank and Credit Union Portfolio Lending

- This section provides qualified mortgage (QM) liability protection for certain loans, as long as they are held in portfolio by depository institutions under $10 billion in total consolidated assets.
- Products that do not maintain consumer protections, such as no-doc loans and loans with excessive fees or interest rates – all of which played a role in the financial crisis – would be ineligible.
- It would provide more flexibility for relationship lending by community banks and credit unions by removing the 43 percent debt-to-income cap for loans held on portfolio.

Section 102. Streamlining Privacy Notifications

- Financial institutions – including banks and credit unions – must send consumers an annual privacy notice.
- Unfortunately, these annual privacy notices have become so routine that most consumers are either confused by them, or simply do not read them at all.
- The requirement is costly for small institutions like community banks and credit unions.
- Under this provision, a financial institution will be required to send a consumer an annual privacy notice only when there has been a change in the bank's privacy policy. This will make the notices more meaningful to consumers and reduce the unnecessary red tape on community banks and credit unions. An institution's privacy policy will still be available to consumers through other means.
- The provision mirrors legislation Sens. Jerry Moran (R-KS) and Heidi Heitkamp (D-N.D.) introduced this Congress. The bill had 75 cosponsors last Congress.

Section 103. Tailored Exam Cycles

- This provision lengthens the exam cycle to 18 months for well-capitalized banks under $1 billion in total assets. Regulators may continue to examine more frequently under certain circumstances, such as potential or actual deterioration or a change in control.
- Current law requires a full-scope exam every 12 months for banks above $500 million in total assets.
- Approximately 600 institutions would benefit from this change.
- This section mirrors legislation Sens. Pat Toomey (R-PA) and Joe Donnelly (D-IN) introduced this Congress.

Section 104. Parity for Credit Unions

- The Federal Home Loan Bank System's (FHLB) approximately 7,600 member institutions are commercial banks, thrifts, credit unions, and insurance companies. The membership definition currently excludes privately-insured credit unions from joining the FHLB system.
- There are currently about 150 privately insured credit unions in nine states – California, Idaho, Illinois, Indiana, Maryland, Mississippi, Nevada, Ohio, and Texas – most of which are under $70 million in assets. By contrast, there are 6,429 federally insured credit unions, about 1,100 of which are FHLB members. Total assets of privately insured credit unions are about $11 billion.
- This provision allows privately-insured credit unions to become members of the FHLB if a state regulator determines that the privately-insured credit union meets all eligibility requirements of the FHLBs, and that the private insurer has sufficient reserves for losses, and has adequate capital.

Section 105. Parity for Thrifts

- This provision changes the Securities and Exchange Commission's registration and deregistration thresholds for Savings and Loan Holding Companies to provide them parity with Bank Holding Companies.
- The JOBS Act raised the 500-shareholder of record threshold to 2,000 for Bank Holding Companies before they are required to register with the SEC, and raised the threshold at which a bank holding company can deregister to 1,200 shareholders of record from 300.
- Savings and loan holding companies were not included in the JOBS Act provision.
- This section mirrors legislation Sens. Moran and Jon Tester (D-MT) introduced this Congress.

Section 106. Transitional Licenses

- This section amends the Secure and Fair Enforcement for Mortgage Licensing Act of 2008 (SAFE Act) to make it easier for mortgage loan originators who work for banks to transition to jobs with non-bank firms. It allows a 120-day transitional period for mortgage loan originators who works at banks to comply with the education and testing requirements under the SAFE Act that apply to non-bank firms.
- Similar legislation was introduced by Rep. Spencer Bachus (R-AL) last Congress and cosponsored by Senators Shelly Moore Capito (R-WV) and Gary Peters (D-MI) when they served in the House.

TITLE II. PROTECTING CONSUMERS

Section 201. Enhanced Consumer Protections for Servicemembers

- This section allows the CFPB to ensure that members of the armed forces are protected under certain existing provisions of the Servicemember Civil Relief Act (SCRA). The SCRA protects servicemembers in the event that their military service impedes their ability to meet financial obligations incurred before entry into active military service.
- The CFPB's Office of Servicemember Affairs has been very active: nearly 30,000 servicemembers have submitted complaints since the CFPB opened its doors and recovered more than $1.6 million.
- Servicemembers continue to be vulnerable to financial abuse. Since 2012, lenders have been fined over $150 million for SCRA violations related to student loans, credit cards, foreclosures, and vehicle repossessions, as well as $100 million for other violations including deceptive marketing and abusive debt collection. Earlier record settlements stemming from the financial crisis revealed that a significant number of servicemembers were illegally foreclosed upon while serving their country overseas.
- This section does not change the SCRA statute itself. It simply enables the CFPB, already active through its Office of Servicemember Affairs, to enforce the SCRA.

Section 202. Tenant Fairness

- This section permanently extends the provisions of the Protecting Tenants at Foreclosure Act that expired at the end of 2014.
- In the case of a foreclosure on a property being rented, the new landlord would be required to abide by the terms of any lease and provide a notice to vacate the property 90 days before a tenant was required to vacate the property.

Section 203. Regulatory Access

- This section amends the SAFE Act to allow federal and state financial services regulators access to the Nationwide Mortgage Licensing System database while maintaining the confidentiality of information shared between the regulators.
- This provision mirrors legislation, introduced by then-Sen. Kay Hagan (D-NC), that the Senate passed in the last Congress. Also in the last Congress, Sen. Capito introduced the bill while she served in the House, where it also passed. Unfortunately, the bill did not become law.

LETTER SUBMITTED BY JIM NUSSLE, PRESIDENT AND CEO, CREDIT UNION NATIONAL ASSOCIATION

CUNA
Credit Union National Association

Jim Nussle
President & CEO

October 28, 2015

The Honorable Pat Toomey
Chairman
Subcommittee on Financial Institutions and Consumer Protection
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Jeff Merkley
Ranking Member
Subcommittee on Financial Institutions and Consumer Protection
Committee on Banking, Housing and Urban Affairs
United States Senate
Washington, DC 20510

Chairman Toomey and Ranking Member Merkley:

On behalf of the Credit Union National Association (CUNA), the national trade association for America's state and federally chartered credit unions, thank you for holding this hearing on the State of Rural Banking: Challenges and Consequences. CUNA represents America's credit unions and their more than 100 million memberships.

I appreciate your inviting CUNA member Carrie Wood, president and CEO of Timberland FCU in Dubois, Pennsylvania to testify at this hearing. I am confident that Ms. Wood's experience as the CEO of a small credit union in a rural area will contribute greatly to the subcommittee's understanding of the crisis of creeping complexity facing credit unions and small banks.

Credit unions' statutory mission is to promote thrift and provide access to credit for provident purposes to credit union members. This is the mission that credit unions have fulfilled since their inception in the United States more than 100 years ago. Our vision is that Americans choose credit unions as their best financial partner. The system's size and growth in terms of membership, loans and deposits, and its consistent soundness are indicators that credit unions succeed in fulfilling their mission and are well on their way to achieving their vision.

The credit union system is very sound, with a system wide capital ratio of 10.9%, and a history of being there for credit union members in good times and bad. As safe and affordable member-owned financial services institutions credit unions continue to deliver tremendous benefits to their members in terms of lower-interest rate loans, and lower-fee or no-fee products and services. When the financial crisis threatened the economy and the financial livelihood of many Americans, credit unions were a safe harbor for consumers and small businesses that could not access credit elsewhere; they continued to lend when others were forced to pull back.

Credit union employees and volunteers work every day to deliver service excellence to their members, but there are several statutory and regulatory barriers that keep credit unions from more fully serving the savings and credit needs of their members. We want to work with the Committee to remove these barriers. If these barriers are removed, the impact that credit unions could have on the financial lives of their members would be that much more significant and the economic contribution credit unions and their members make would be that much greater.

The Consequences of Doing Nothing

Credit unions, particularly those in rural areas, face a crisis of creeping complexity with respect to regulatory burden, and American consumers cannot afford for Congress to do nothing to address this crisis. Since the beginning of the financial crisis, credit unions have been subjected to more than 202 regulatory changes from nearly two dozen Federal agencies totaling more than 6,000 *Federal Register* pages.[1] These numbers do not take into account regulatory changes that may emanate from state regulators. Every time a rule is changed credit unions and their members incur costs. They must take time to understand the new requirement, modify their computer systems, update their internal processes and controls, train their staff, design and print new forms and produce material to help their members understand each new requirement. Even simple changes in regulation cost credit unions thousands of dollars and many hours: time and resources that could be more appropriately spent on serving the needs of credit union members.

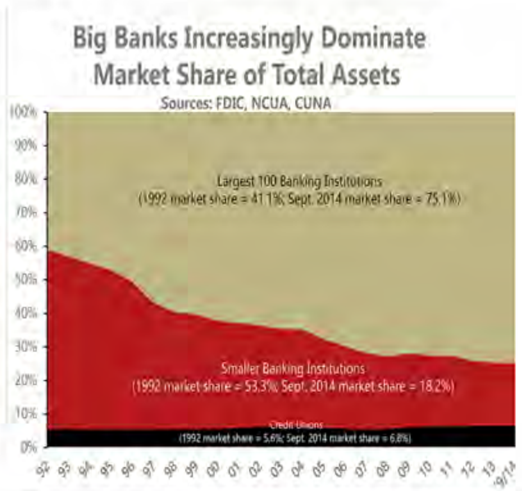
Regulatory change presents a particularly difficult challenge for small and rural depository institutions because the fixed costs of compliance are proportionately higher for smaller-sized credit unions and banks than for behemoth banks. Congress and regulators ask a lot of small, not-for-profit, financial institutions in rural America when they tell them to comply with the same rules as J.P. Morgan, Bank of America and Citibank. Almost half of the credit unions in the United States operate with five or fewer full-time equivalent employees; the largest banks likely have compliance departments that exceed that number by multiples of a hundred or more. To put the question of size in further perspective, consider that each of the four largest banks in the United States has total assets greater than the combined assets of the entire credit union system.

The rules that the Consumer Financial Protection Bureau (CFPB) have promulgated so far do not take the disparity of size -- and disproportionate burden -- into consideration as much as we feel it can or should under the law. When the CFPB does try to tailor its regulations, the tiered approach often restricts small credit unions ability to serve their members by encouraging them to stay under the thresholds established. For example, if a rule applies to credit unions that originate more than 200 mortgages in a year, a small credit union is likely to reduce mortgage lending as it approaches the threshold and stop originating mortgages

[1] See Attachment I for a list of these regulations, the agency which promulgated them, and the number of pages in the *Federal Register*.

altogether after their 200th, turning away and alienating otherwise credit worthy members. This is one of the reasons we have consistently urged the CFPB to fully exercise its authority to exempt "any class of covered person" from its regulations. We strongly believe they have the authority to exempt credit unions from its regulations [2] and we continue to be deeply disappointed they have failed to do so.

Regulatory burden is one of the primary reasons that Main Street and rural financial institutions are disappearing at an alarming rate. The number of credit unions has been halved in the last 20 years – from more than 12,500 in 1995 to a little less than 6,300 today. A similar phenomenon is happening in the banking industry. This consolidation of small financial institutions, much like the pre-crisis trend, is being led by an ever-increasing, never-decreasing, regulatory burden that frankly forces some credit unions simply to give up and find other larger credit unions with which to merge. And when small financial institutions disappear, large banks gobble up ever more market share.



If Congress does nothing to protect small and rural depository institutions from, and relieve them of, the unnecessary and poorly focused regulatory burden, the trend of consolidation will continue; consumers in rural communities will have fewer options in the financial marketplace; and the cost of accessing mainstream financial services will increase. This outcome is unacceptable, and Congress can do something about it.

[2] See Attachment II for a legal opinion outlining the CFPB's exemption authority.

Congress Should Consider Several Measures to Remove Barriers for Credit Unions to More Fully Serve Their Member

In testimony before the full committee earlier this year, we outlined the statutory and regulatory barriers credit unions face as they work to fulfill their mission and fully serve their members; we also discussed more than two dozen proposals to address these barriers.[3]

As we indicated in our previous testimony, Congress should make several improvements to the *Federal Credit Union Act*, including enacting legislation to improve credit union capital requirements and restoring credit union business lending authority to pre-1998 levels. Further, Congress should consider modernizing credit unions' loan maturity restrictions, investment authority and federal credit union by-laws.

Credit unions face barriers with respect to membership eligibility in Federal Home Loan Bank System. We ask Congress to ensure that the eligibility rules for small credit unions are the same as they are for small banks, and to permit privately insured credit unions to join the FHLB system.

We encourage Congress to address issues related to examination fairness by enacting legislation that creates an independent ombudsman and independent appeals process.

Consumers and financial institutions would benefit if Congress enacted legislation to modernize privacy notification requirements, and to improve merchant data security standards.

In addition, we encourage Congress to recognize that the Dodd-Frank Act is not and should not be considered sacrosanct. There are several improvements that should be made to the law that, in the long run, would enhance consumer protection by ensuring credit unions are around to serve them. We encourage Congress to consider structural reforms to the Bureau that enhance the stability, so that over the long run credit unions and other small lenders experience stability from the Bureau as opposed to the uncertainty brought on by constantly changing rules. While we know there are significant differences of opinion on this, we believe a commission could bring about the stability we seek. There are other proposals, as well, which would protect the marketplace participants, including consumers, from the peril associated with frequently changing regulatory requirements. Legislation has also been introduced to address the unintended consequences of the Dodd-Frank Act mortgage rules; we encourage Congress to enact these bills as well.

[3] Testimony of Wally Murray, President and Chief Executive Officer, Greater Nevada Credit Union, on behalf of the Credit Union National Association. "Regulatory Relief for Community Banks and Credit Unions." Committee on Banking, Housing and Urban Affairs. United States Senate. February 12, 2015. http://www.banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=e64a546e-3ea0-4094-bd56-ac5765417e60

Finally, we encourage Congress not to impose any new burdens on credit unions, noting that the National Credit Union Administration (NCUA) has petitioned Congress for authority to supervise third-party vendors. We believe NCUA has sufficient authority to obtain the information it requires from these vendors, most of which are either owned by credit unions subject to supervision by NCUA or supervised by other banking regulators. Conveying additional authority to NCUA would increase costs to credit unions and their members without significantly enhancing safety and soundness.

Many, but not all, of the proposals that would help credit unions more fully serve their members can be found in Title I of S. 1484; several are also in Senator Brown's alternative. We encourage the Committee and the Senate to find a way to enact these provisions, which we believe enjoy broad bipartisan support, before the end of the year.

Conclusion

We greatly appreciate your holding today's hearing and maintaining the focus on regulatory burden facing small financial institutions. We are confident that if barriers are removed, credit union members will be better off than they are today, because their credit unions will be spending less resources on complying with outdated, poorly focused and unreasonably burdensome regulation, and more on meeting the financial services needs of their members. We stand ready to work with you to remove these barriers.

On behalf of America's credit unions and their more than 100 million members, thank you very much for the opportunity to share our thoughts.

Sincerely,

Jim Nussle
President & CEO

ATTACHMENT I

FINALIZED FEDERAL REGULATORY CHANGES APPLICABLE TO CREDIT UNIONS
(Effective Dates on or after January 1, 2008)[4]

Effective Date	Agency	Title of Final Rule	Pages in Federal Register
1/1/2008	FEMA	FEMA Flood Map Changes	2
1/1/2008	IRS	Annual Electronic Filing Requirement For Small Tax Exempt Organizations – Form 990-N	1
1/1/2008	IRS	IRS Form 990 Instructions - New Reporting Form	79
1/1/2008	IRS	IRS Redesign Form 990	28
5/29/2008	NCUA	Disclosures for Subprime Mortgage Loans	9
7/7/2008	FTC	CAN-SPAM Act Rules	27
10/1/2008	FHA	Hope for Homeowners Program for Subordinate Lienholders	6
10/10/2008	FASB	Use of Fair Value in an Inactive Market	7
10/22/2008	NCUA	Share Insurance Signs to Reflect Increased Limits	2

[4] Last updated: October 2015

10/31/2008	NCUA	Official Advertising Statement	2
11/21/2008	NCUA	Incidental Powers	7
12/15/2008	FASB	Amendments to the Impairment Guidance No. 99-20	44
12/31/2008	NCUA	PCA: Amended Definition of Post-Merger Net Worth	4
1/2/2009	NCUA	Criteria to Approve Service to Underserved Areas	5
1/7/2009	FHA	Interim Final Rule on Hope for Homeowners Program	6
1/16/2009	HUD	Final RESPA Rule	85
1/19/2009	FED	Unlawful Internet Gambling	31
4/3/2009	NCUA	Share Insurance Signs for Shared Branching	3
4/27/2009	NCUA	RegFlex Changes for Unimproved Land	1
5/14/2009	NCUA	Technical Changes to the FACT Act "Red Flags"	8
6/15/2009	FASB	Fair Value: Decrease in Market Activity/Transactions That Are Not Orderly	27
6/15/2009	FASB	Recognition and Presentation of Other-Than-Temporary Impairments	64

6/20/2009	FED	Restructuring of Fed's Check Processing : Districts 10, 11, and 12	2
7/2/2009	FED	Fed Rule Authorizing Excess Balance Accounts and Earnings on Balances	10
7/2/2009	FED	Fed Rule Authorizing Pass-through Accounts and Adjusting the Limitation on Savings Account Transfers	11
7/19/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 6 and 8	2
7/25/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 4 and 9	2
7/30/2009	FED	Revisions to Regulation Z Mortgage Loan Disclosures	17
9/1/2009	NCUA	Credit Union Reporting	3
9/12/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 4 and 7	2
9/14/2009	FED	Regulation Z Disclosures for Private Student Loans	63
9/21/2009	FED	Regulation Z Rule Implementing the CARD Act	26
10/1/2009	FED	Amendments to the Home Mortgage Provisions of Regulation Z	93
10/17/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 11 and 12	3
10/18/2009	FED	Restructuring of Federal Reserve's Check Processing : District 4	3

10/18/2009	FED	Restructuring of Federal Reserve's Check Processing : District 6	3
11/6/2009	FHFA	Election of Federal Home Loan Bank Directors	13
11/14/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 11 and 12	3
11/30/2009	NCUA	Share Insurance Coverage for Revocable Trust Accounts	9
11/30/2009	NCUA	Temporary Increase in SMSIA; Display of Official Sign; Coverage for Mortgage Servicing Accounts	10
12/12/2009	FED	Restructuring of Federal Reserve's Check Processing : District 3	2
12/24/2009	NCUA	Exceptions to the Maturity Limit on Second Mortgages	2
1/1/2010	FED	Overdraft Protection Disclosures	11
1/1/2010	FED	Revisions to Regulation S	4
1/1/2010	NCUA	Operating Fees	3
1/1/2010	NCUA	Truth in Savings Rule for Overdraft Protection and Electronic Disclosures	5
1/4/2010	NCUA	NCUSIF Premium and One Percent Deposit	7
2/4/2010	FHFA	Federal Home Loan Bank Membership to Include Non-Federally Insured CDFI Credit Unions	27

2/10/2010	FinCEN	Expansion of Special Information Sharing Procedures To Deter Money Laundering and Terrorist Activity	11
2/14/2010	FED	Regulation Z Disclosures for Private Student Loans	63
2/22/2010	FED	Regulation Z Rule Implementing the CARD Act	268
2/27/2010	FED	Consolidation of Federal Reserve's Check-Processing	2
5/21/2010	NCUA	Interagency Policy Statement on Funding & Liquidity Risk Management	11
6/4/2010	FED	Establishment of Term Deposits at Federal Reserve Bank	6
6/18/2010	NACHA	Direct Access Registration Requirement	6
6/18/2010	NACHA	Risk Management and Assessment	4
7/1/2010	ED	Final Rules for Student Loans	35
7/1/2010	FED	Regulation Z Open-end Credit Final Rule	255
7/1/2010	FED	Regulation E Final Rule for Overdraft Protection Plans	8
7/1/2010	FTC	FACT Act Rules and Guidelines on the Accuracy of Credit Information	87
7/1/2010	NCUA	FACT Act Rules and Guidelines on the Accuracy of Credit Information	45

7/1/2010	NCUA	NCUA Final Rule on Unfair and Deceptive Practices for Credit Cards	3
7/6/2010	FTC	Disclosures for Non-federally Insured Credit Unions	7
7/26/2010	NCUA	Chartering and Field of Membership (FOM): Federal Credit Unions	9
8/2/2010	FED	FedACH SameDay Service	3
8/5/2010	NCUA	Low-Income Definition	2
8/16/2010	IRS	Payments Made in Settlement of Payment Card and Third-Party Network Transactions	16
8/22/2010	FED	Final Rule Implementing the CARD Act Provisions for Penalty Fees and Rate Reviews	68
8/22/2010	FED	Regulation E Rules for Gift Cards	43
9/2/2010	NCUA	Display of Official Sign; Permanent Increase in Standard Maximum Share Insurance Amount	3
9/7/2010	FED	Clarifications of Reg E and Reg DD Overdraft Rules	4
9/7/2010	NCUA	Clarifications on Reg DD Overdraft Protection Rules	4
10/1/2010	NCUA	SAFE Act	54
10/4/2010	HUD	FHA Risk Reduction Final Rule	4

10/18/2010	NCUA	Reverse Mortgage Guidance	12
10/25/2010	NCUA	Short-Term, Small Amount Loans	6
11/29/2010	NCUA	RegFlex Program Changes	4
11/29/2010	FED	Extension of CARD Act Effective Date for Gift Cards	5
12/23/2010	NCUA	Conversions of Insured CUs: Definition of Regional Director	2
12/31/2010	NCUA	Model Privacy Notices	105
1/1/2011	FED	FACT Act Risk-Based Notice Rule	61
1/1/2011	FED	Consumer Notification of Mortgage Loan Sales or Transfers	16
1/1/2011	FTC	Notice Regarding Charges Permitted Under the FCRA	1
1/1/2011	NACHA	Mobile ACH Payments	1
1/3/2011	FinCEN	Confidentiality of Suspicious Activity Reports	15
1/18/2011	NCUA	Corporate Credit Union Rule	4
1/20/2011	NCUA	IRPS 11-1 Supervisory Review Committee	4

1/27/2011	NCUA	Fiduciary Duties at Federal Credit Unions, and Mergers and Conversions of Insured Credit Unions	18
1/30/2011	FED	Interim Final Rule on Disclosures Required under the Mortgage Disclosure Improvement Act	8
1/31/2011	FED	Extension of CARD Act Gift Card Rules	1
3/14/2011	NCUA	Conversions of Insured Credit Unions: Definition of Regional Director	1
3/23/2011	NCUA	Corporate Credit Unions: Technical Corrections	1
3/23/2011	NCUA	PCA: Amended Definition of "Low-Risk Assets	2
3/24/2011	Treasury	Garnishment of Accounts Containing Federal Benefit Payments	24
3/28/2011	FinCEN	Amendment to BSA Regulations: Reports of Foreign Financial Accounts	1
3/28/2011	NCUA	IRPS: Chartering Corporate Federal Credit Unions	4
4/1/2011	FED	Interim Final Rule on Appraisal Independence	35
4/1/2011	FED	Loan Compensation and "Steering" of Loans	30
4/4/2011	FHA	Temporary Minimum Capital Increase for FHFA Regulated Entities	7
6/24/2011	NCUA	Technical Correction - Golden Parachute and Indemnification Payments	2

6/24/2011	NCUA	Temporary Unlimited Share Insurance for Noninterest-bearing Transaction Accounts	3
6/27/2011	NCUA	Golden Parachute and Indemnification Payments	12
7/21/2011	CFPB	Consumer Financial Rules to be Enforced by the CFPB	2
7/22/2011	CFPB	Regulation D Interim-Final Rule Implementing the Alternative Mortgage Transaction Parity Act	19
7/25/2011	NCUA	Sample Income Data to Meet the Low-income Definition	3
7/27/2011	NCUA	Remittance Transfers Interim Final Rule	2
8/10/2011	HUD	Technical Corrections & Clarifying Amendments to RESPA Regulations	4
8/15/2011	FED	Fair Credit Reporting Risk-Based Pricing (Credit Score Disclosures)	24
8/15/2011	FED	Regulation B - Equal Credit Opportunity Act (Credit Score Disclosures)	13
8/19/2011	FTC	Mortgage Acts & Practices - Advertising Rule	22
8/29/2011	HUD	SAFE Mortgage Licensing Act: Minimum Licensing Standards and Oversight Responsibilities	38
10/1/2011	FED	CARD Act Clarifications	93
10/1/2011	FED	Debit Interchange Fee and Routing Regulations (Regulation II)	82

10/1/2011	FED	Federal Reserve Board's Interim Final Rule on the Interchange Fee Fraud-Prevention Adjustment	11
10/19/2011	Treasury	Indorsement and Payment of Checks Drawn on the United States Treasury	3
10/31/2011	NCUA	Net Worth & Equity Ratio	4
11/14/2011	Labor	Notification of Employee Rights under the National Labor Relations Act	44
11/30/2011	NCUA	NCUA Remittance Transfers Rule	2
12/2/2011	NCUA	Community Development Revolving Loan Fund (CDRLF) Access for Credit Unions	8
12/23/2011	NCUA	Low-Income Designation – Technical Amendment	1
1/1/2012	NCUA	Accuracy of Advertising and Notice of Insured Status	2
1/23/2012	NCUA	Corporate Credit Union Rule – Technical Amendment	3
4/19/2012	IRS	Guidance on Reporting Interest Paid to Nonresident Aliens	5
5/31/2012	NCUA	Corporate Credit Union Follow-up Rule	10
6/29/2012	CFPB	Rules of Practice for Adjudication Proceedings	44
6/29/2012	CFPB	Rules Relating to Investigations Final Rule	11

7/2/2012	NCUA	Regulatory Flexibility Program	12
7/2/2012	NCUA	Regulatory and Reporting Treatment of Troubled Debt Restructurings	12
7/12/2012	FED	Regulation J (Collection of Checks and Other Items by Federal Reserve Banks. Etc)	7
7/12/2012	FED	Regulation D (Reserve Requirements of Depository Institutions: Reserves Simplification)	8
8/16/2012	CFPB	Confidential Treatment of Privileged Information Final Rule	7
9/17/2012	CFTC	End-User Exemption to the Mandatory Clearing of Swaps	32
9/30/2012	NCUA	Interest Rate Risk Policy and Program Final Rule	12
10/1/2012	FED	Debit Interchange Fee and Routing Regulations (Regulation II) - Fraud	25
11/23/2012	CFPB	Delayed Implementation of Certain New Mortgage Disclosures	9
11/30/2012	FED	Reserve Requirements of Depository Institutions	2
12/13/2012	NCUA	Fidelity Bond	2
12/15/2012	FASB	Guidance on Troubled Debt Restructurings	27
1/18/2013	NCUA	Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government Final Rule	1

2/19/2013	NCUA	Acceptance Deadline - Low-Income Designation Final Rule	2
2/19/2013	NCUA	Definition of a "Small Credit Union" Final Rule	6
2/19/2013	NCUA	Definition of "Troubled Condition" Final Rule	3
3/18/2013	FHA	Implementation of the Fair Housing Act's Discriminatory Effects Standard Final Rule	23
3/26/2013	CFPB	Disclosures at Automated Teller Machines Final Rule - Reg E	4
3/28/2013	CFPB	Credit Card Limitations on Fees Final Rule - Reg Z	4
3/29/2013	NCUA	Investment and Deposit Activities (TIPS) Final Rule	2
4/1/2013	NCUA	Rural District Final Rule	3
5/31/2013	NCUA	Technical Amendments Final Rule	6
6/1/2013	CFPB	Escrow Accounts Final Rule - Reg Z	32
6/1/2013	CFPB	Escrow Accounts Amendments Final Rule - Reg Z	8
6/11/2013	NCUA	Alternatives to the Use of Credit Ratings Final Rule	9
6/28/2013	FMS	Garnishment of Accounts Containing Federal Benefits Final Rule	12

7/1/2013	FTC	COPPA Final Rule	43
7/25/2013	NCUA	Loan Participations Final Rule	12
10/28/2013	CFPB	Remittance Transfers 2012 Final Rule - Reg E	117
10/28/2013	CFPB	Remittance Transfers Safe Harbor, Preauthorized Transfers Final Rule - Reg E	46
10/28/2013	CFPB	Remittance Transfers 2013 Final Rule - Reg E	61
11/4/2013	CFPB	Consumer's Independent Ability to Pay Final Rule - Reg Z	22
11/18/2013	NCUA	Federal Credit Union Ownership of Fixed Assets Final Rule	4
12/19/2013	NCUA	Charitable Donation Accounts Final Rule	3
1/1/2014	NCUA	Electronic Filing of Financial and Other Reports Final Rule	2
1/3/2014	FinCEN	BSA Definitions - Definitions of Transmittal of Funds and Funds Transfer Final Rule	4
1/10/2014	CFPB	Mortgage Loan Origination Compensation Final Rule	148
1/10/2014	CFPB	Mortgage Servicing Final Rule - Reg X	203
1/10/2014	CFPB	Mortgage Servicing Final Rule - Reg Z	120

1/10/2014	CFPB	Ability to Repay / QM Final Rule	213
1/10/2014	CFPB	Ability to Repay / QM - Exemptions, Modifications, and Clarifications	15
1/10/2014	CFPB	QM and Mortgage Servicing Clarifications	42
1/10/2014	CFPB	HOEPA – "High-Cost Mortgage" Loans Final Rule	120
1/10/2014	CFPB	Homeownership Counseling Organizations Lists Interpretive Rule	2
1/18/2014	CFPB	Regulation B - Copies of Appraisals Final Rule	35
1/18/2014	NCUA	Interagency Higher-Priced Mortgage Appraisals Final Rule	80
1/18/2014	NCUA	Interagency Higher-Priced Mortgage Appraisals Supplemental Final Rule	69
3/3/2014	NCUA	Derivatives Final Rule	19
3/31/2014	NCUA	Liquidity and Contingency Funding Plans Final Rule	4
5/30/2014	NCUA	Capital Planning and Stress Testing	7
6/30/2014	NCUA	Credit Union Service Organizations (CUSOs) Final Rule	13
7/1/2014	IRS	FATCA- (Temporary Regulations under Chapter 4)	54

7/1/2014	IRS	FATCA - (Temporary Regulations under Chapters 3 and 61)	84
7/1/2014	IRS	FATCA Final Rule	123
7/17/2014	CFPB	Application of Regulation Z's Ability-to-Repay Rule to Certain Situations Involving Successors-in-Interest	3
7/17/2014	CFPB	Policy Guidance on Supervisory and Enforcement Considerations Relevant to Mortgage Brokers Transitioning to Mini-Correspondent Lenders	5
7/28/2014	NCUA	Voluntary Liquidation Final Rule	3
10/3/2014	NCUA	Unfair or Deceptive Acts or Practices; Technical Amendments	4
10/23/2014	CFPB	Compliance Bulletin and Policy Guidance—Mortgage Servicing Transfers	5
10/28/2014	CFPB	Annual Privacy Notice Requirement Under the Gramm-Leach-Bliley Act (Regulation P)	26
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1/10/2015	HUD	Federal Housing Administration (FHA): Adjustable Rate Mortgage Notification Requirements and Look-Back Period for FHA-Insured Single Family Mortgages	3
1/21/2015	HUD	Federal Housing Administration (FHA): Handling Prepayments: Eliminating Post-Payment Interest Charges	4
4/17/2015	CFPB	Submission of Credit Card Agreements under TILA	6
4/21/2015	CFPB	Homeownership Counseling Organizations Lists and High-Cost Mortgage Counseling Interpretive Rule	4

6/5/2015	NCUA	Corporate Credit Unions	8
6/10/2015	NCUA	Policy Statement re Standards for Assessing Diversity Policies and Practices	10
7/6/2015	NCUA	Chartering & FOM Manual	8
8/1/2015	CFPB	Integrated Mortgage Disclosures under TILA and RESPA Final Rule	1273
10/1/2015	NCUA	Loans in Areas Having Special Flood Hazards	49
10/1/2015	DOD	Limitations on Terms of Consumer Credit Extended to Service Members & Dependents	54
10/2/2015	NCUA	FCU Ownership of Fixed Assets	8
10/3/2015	CFPB	TILA-RESPA Integrated Disclosures	11
1/1/2016	NCUA	Capital Planning and Stress Testing - Schedule Shift	4
1/1/2016	CFPB	Amendments on Small Creditors & Rural or Underserved Areas Under TILA	31
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ATTACHMENT II

MEMORANDUM RELATED TO CFPB EXEMPTION AUTHORITY

This memorandum addresses the Bureau's statutory authority to exempt credit unions from obligations imposed by: (1) Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act[5] ("Dodd-Frank Act") and Bureau regulations issued under Title X; and (2) the "enumerated consumer laws" and Bureau regulations to implement those laws.

Executive Summary

As described in greater detail below, the Bureau has several sources of statutory authority that it could use to provide exemptions from the requirements of statutes or implementing regulations generally or the requirements of certain provisions specifically.[6] These statutory provisions individually and together grant broad authority to the Bureau and constitute a strong legal framework to support the agency's reasonable use of its exemption authority.

For example, Section 1022 of Title X of the Dodd-Frank Act permits the Bureau to exempt ***any* class of covered person from *any* provision of Title X or *any* rule issued by the Bureau under Title X** if such an exemption is consistent with relevant statutory considerations that the Bureau must take into account in issuing an exemption.

In addition to this general authority, of the eighteen enumerated consumer laws, eleven provide the Bureau with specific exemption authority. Specifically, of the eighteen enumerated consumer laws:

- Five permit the Bureau generally to provide exemptions for specific classes of transactions only;
- Five permit the Bureau to make exemptions from specific statutory provisions only; and
- One permits the Bureau to provide exemptions for specific classes of transactions and also permits the Bureau to make exemptions from specific statutory provisions.

As discussed below, however, the various statutes generally do not define the phrase "class of transaction" or otherwise clarify whether a "class of transaction" may apply to a

[5] Public Law 111-203, 124 Stat. 1376 (2010).
[6] We note that, in large part, the Bureau's exemption authority is permissive and not mandatory. That is, where permitted, the Bureau may (but is not required to) provide exemptions.

specific type of institution. Nonetheless, the Bureau's exemption authority under specific provisions of certain laws may be broader than its more general "class of transaction" authority.

Five of the eighteen enumerated consumer laws permit the Bureau to make exemptions for classes of transactions subject to substantially similar state laws.[7] This "substantially similar state law" exemption authority requires, among other things, that there be a state law that is substantially similar to the federal law and that there is adequate provision for enforcement of that state law.

Regardless of the source of exemption authority, our discussion below assumes that any Bureau use of its exemption authority would be consistent with the Administrative Procedure Act. Specifically, we assume that any Bureau use of its exemption authority by rule would not be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[8] For example, if the Bureau were to make an exemption for credit unions and not for other types of institutions as well, the Bureau would need a sufficient basis for treating credit unions differently than other types of institutions.

Background on the Bureau

As you know, Title X of the Dodd-Frank Act created the Bureau as an independent agency within the Federal Reserve System. In general, the Bureau is charged with writing rules to implement a number of federal consumer financial laws, as well as supervision and enforcement of those laws. Certain consumer financial protection functions previously performed by the federal banking agencies and the National Credit Union Administration ("NCUA") were transferred from such agencies to the Bureau. In addition to inheriting supervisory and enforcement authority for certain institutions, the Bureau is generally authorized to issue regulations to implement various consumer financial protection laws. Separately, the Bureau is authorized to engage in rulemakings and to take certain actions regarding unfair, deceptive or abusive acts or practices in connection with consumer financial products and services.[9]

Broad Bureau Exemption Authority Under Section 1022 of Title X

Section 1022 of Title X of the Dodd-Frank Act authorizes the Bureau "to exercise its authorities under Federal consumer financial law to administer, enforce, and otherwise

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[7] Note that only one law, the Fair Debt Collection Practices Act, includes only the "substantially similar state law" exemption authority. That is, four of the five laws that include this type of exemption authority also include another type of exemption authority, such as the "class of transaction" authority discussed above.

[8] 5 U.S.C. § 706(2)(A).

[9] *See* 15 U.S.C. § 5531.

implement the provisions of Federal consumer financial law."[10] Section 1022 permits the Bureau to "prescribe rules and issue orders and guidance, as may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof."[11] The "Federal consumer financial laws" include Title X, the "enumerated consumer laws" and any Bureau rule prescribed under Title X or the enumerated consumer laws. As a result, in addition to any other rule writing authority provided for under Title X or the enumerated consumer laws, Section 1022 separately authorizes the Bureau to write rules as it deems appropriate to carry out the purposes and objectives of the Federal consumer financial laws.

Section 1022 also provides the Bureau with exemption authority with respect to Title X and the rules that the Bureau may prescribe to carry out the purposes and objectives of the Federal consumer financial laws (*i.e.*, Bureau rules issued under Title X). Specifically, Section 1022 provides that the Bureau "**may conditionally or unconditionally exempt any class of covered persons . . . from any provision of [Title X], or from any rule issued under [Title X]**, as the Bureau determines necessary or appropriate to carry out the purposes and objectives of" the Title.[12]

This exemption authority is far-reaching. Section 1022 authorizes the Bureau to provide an exemption from a Bureau rule issued under Title X that addresses conduct governed by an enumerated consumer law, even if that specific law does not provide the Bureau with independent exemption authority. That is, the Bureau's authority to provide an exemption from a rule issued under Title X is not contingent on statutory exemption set forth under the underlying enumerated consumer laws.

In order to exempt credit unions from a rule issued under Title X, the Bureau must determine that such an exemption is appropriate to carry out the purposes and objectives of Title X. The broadly stated "purpose" of Title X, as described in Section 1029A, is for the Bureau to implement and enforce the Federal consumer financial laws "consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive."[13] For example, if credit unions could no longer offer certain consumer financial products or services because of an inability to do so on a competitive cost basis, including because compliance costs outweigh revenue, the Bureau may find an exemption appropriate in order to ensure or expand consumer access to those products.

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[10] 12 U.S.C. § 5512(a).
[11] 12 U.S.C. § 5512(b)(1).
[12] 12 U.S.C. § 5512(b)(3)(A) (emphasis added).
[13] 12 U.S.C. § 5511(a).

Moreover, the stated "objectives" of Title X, as described in Section 1029A, are that the Bureau's authority under the Federal consumer financial laws is "for the purposes of ensuring" that: (1) consumers are provided with timely and understandable information to make responsible decisions about financial transactions; (2) consumers are protected from unfair, deceptive, or abusive acts and practices and from discrimination; (3) outdated, unnecessary, or unduly burdensome regulations are regularly identified and addressed in order to reduce unwarranted regulatory burdens; (4) federal consumer financial law is enforced consistently, without regard to the status of a person as a depository institution, in order to promote fair competition; and (5) markets for consumer financial products and services operate transparently and efficiently to facilitate access and innovation.[14] For example, the Bureau may find it appropriate to rely on the "burden" objective (3) or the "markets" objective (5) to take the position that an exemption is appropriate where credit unions were not able to provide their members with access to certain financial products or services because of compliance burdens or cost challenges.

Finally, Section 1022 also includes three statutory considerations that the Bureau must take into account in issuing an exemption to a rule issued under Title X. Specifically, in issuing such an exemption, the Bureau must, as appropriate, consider three factors: (1) the total assets of the class of covered persons; (2) the volume of transactions involving consumer financial products or services in which the class of covered persons engages; and (3) existing provisions of law that are applicable to the consumer financial product or service and the extent to which such provisions provide consumers with adequate protections.[15] The statute is silent on how the Bureau should consider these factors. Nonetheless, based on the context, the Bureau might determine that an exemption is appropriate where, for example, a covered person has fewer total assets or engages in a volume of transactions that is less than the average covered person.

Bureau Exemption Authority Under the Enumerated Consumer Laws

As indicated above, the Dodd-Frank Act transferred certain existing rule writing authority under the "enumerated consumer laws" from other agencies to the Bureau. Of the enumerated consumer laws, the following twelve provide the Bureau with some type of express exemption authority:

(1) the Consumer Leasing Act of 1976 ("CLA");
(2) the Electronic Fund Transfer Act ("EFTA"), except for Section 920 (debit interchange);
(3) the Equal Credit Opportunity Act ("ECOA");
(4) the Fair Credit Billing Act ("FCBA");

[14] 12 U.S.C. § 5511(b).
[15] 12 U.S.C. § 5512(b)(3)(B).

(5) the Fair Credit Reporting Act ("FCRA"), except for Section 615(e) (red flags) and Section 628 (disposal of credit report information);
(6) the Fair Debt Collection Practices Act ("FDCPA");
(7) Subsections (b) through (f) of Section 43 of the Federal Deposit Insurance Act ("FDIA");
(8) Sections 502 through 509 of the Gramm-Leach-Bliley Act ("GLBA"), except for Section 505 (enforcement) as it applies to Section 501(b) (information security);
(9) the Home Mortgage Disclosure Act of 1975 ("HMDA");
(10) the Home Ownership and Equity Protection Act of 1994 ("HOEPA");
(11) the Real Estate Settlement Procedures Act of 1974 ("RESPA"); and
(12) the Truth in Lending Act ("TILA").[16]

Each of these twelve enumerated consumer laws provides the Bureau with specific exemption authority, but such authority is not uniform. For ease of use, we have separated the discussion of the Bureau's exemption authority into the following three sections based on the type of exemption authority:

- General authority to exempt specific classes of transactions;
- Authority to make exemptions from specific provisions of a statute; and
- Authority to exempt persons subject to substantially similar requirements under state law.

Class of Transaction Exemption Authority

A number of the enumerated consumer laws authorize the Bureau to make exceptions for classes of transactions that would otherwise be covered by these laws. Specifically, TILA, EFTA, ECOA, HMDA, RESPA and CLA each provide the Bureau with general authority to exempt classes of transactions. As discussed below, these statutes do not define the scope of this "class of transaction" exemption authority.

- Section 104 of TILA provides that the statute does not apply to any transaction for which the Bureau determines by rule that coverage under the statute is not necessary to carry out its purposes.[17]

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[16] *See* 12 U.S.C. § 5481(12). Six of the enumerated consumer laws either do not provide the Bureau with specific rule writing authority or do not provide the Bureau with express authority to make exceptions for credit unions. These six laws are: (1) the Truth in Savings Act; (2) the Alternative Mortgage Transaction Parity Act of 1982; (3) the Home Owners Protection Act of 1998; (4) the Interstate Land Sales Full Disclosure Act; (5) the S.A.F.E. Mortgage Licensing Act of 2008; and (6) Section 626 of the Omnibus Appropriations Act, 2009. If, however, the Bureau were to issue a rule under Title X relating to conduct also covered by these six laws, Section 1022 would appear to provide the Bureau with exemption authority for that rule, assuming that the rule was issued pursuant to Title X and not one of the six laws.
[17] 15 U.S.C. § 1603(5).

- Section 105 of TILA provides that any Bureau regulation to carry out the purposes of TILA (except for the mortgage limitations of Section 129 (HOEPA)) "may provide for such . . . exceptions for all or any class of transactions, as in the judgment of the Bureau are necessary or proper to effectuate the purposes of [TILA], to prevent circumvention or evasion thereof, or to facilitate compliance therewith."[18]

- Section 105 of TILA also authorizes the Bureau to exempt by regulation from all or part of TILA "all or any class of transactions, other than transactions involving any mortgage described in section 103(aa), for which, in the determination of the Bureau, coverage under all or part of [TILA] does not provide a meaningful benefit to consumers in the form of useful information or protection."[19]

- Section 129H of TILA provides that the Bureau, the federal banking agencies, the NCUA and the Federal Housing Finance Agency may jointly exempt by rule "a class of loans" from the requirements of Sections 129H(a) and 129H(b) (relating to limitations on higher-risk mortgages without a written appraisal and the related appraisal requirements) if the agencies determine that the exemption is in the public interest and promotes the safety and soundness of creditors.[20]

- Section 904 of the EFTA provides that any Bureau regulation to carry out the purposes of the EFTA "may provide for such . . . exceptions" for any class of electronic fund transfers or remittance transfers, as the Bureau believes are necessary or proper to effectuate the purposes of the EFTA, to prevent circumvention or evasion thereof or to facilitate compliance with the EFTA.[21]

- Section 703 of the ECOA provides that any Bureau regulation to carry out the purposes of the ECOA "may provide for such . . . exceptions" for any class of transaction, as the Bureau believes are necessary or proper to effectuate the purposes of the ECOA, to prevent circumvention or evasion thereof or to facilitate compliance with the ECOA.[22]

- Section 703 of the ECOA also provides that the Bureau's regulations may exempt from the ECOA "any class of transactions that are not primarily for personal, family, or household purposes, or business or commercial loans made available

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[18] 15 U.S.C. § 1604(a).
[19] 15 U.S.C. § 1604(f)(1). In determining whether to exempt a class of transactions, the Bureau must consider five factors, including, for example, whether the goal of consumer protection would be undermined by the exemption. 15 U.S.C. § 1604(f)(2).
[20] 15 U.S.C. § 1639h(b)(4)(B).
[21] 15 U.S.C. § 1693b(c).
[22] 15 U.S.C. § 1693b(a)(1).

by a financial institution, except that a particular type within a class of such transactions may be exempted if the Bureau determines, after making an express finding that the application of [the ECOA or any ECOA provision] of such transaction would not contribute substantially to effecting the purposes of" the ECOA.[23]

- HMDA provides that the Bureau's regulations to carry out the purposes of HMDA "may provide for such . . . exceptions" for any class of transaction that the Bureau believes are necessary or proper to effectuate the purposes of HMDA, to prevent circumvention or evasion thereof or to facilitate compliance with HMDA.[24]

- RESPA provides the Bureau with authority "to grant such reasonable exemptions for classes of transactions, as may be necessary to achieve the purposes of" the statute.[25]

- The CLA provides the Bureau with authority to "provide for . . . exceptions for any class of transactions, as the Bureau considers appropriate."[26]

To use these specific exemption authorities, the Bureau must classify or distinguish transactions that otherwise would be subject to the underlying statute. That is, the Bureau must determine what a "class of transactions" entails. Although the phrase "class of transaction" is not defined in the relevant statutory provisions, the plain language references transactions and not persons or specific types of persons, such as creditors. Nonetheless, the Bureau could take the position that one way to classify or distinguish transactions is to look to the type of institution that is engaging in the transaction, such as a credit union that is not for profit (as opposed to for-profit entities). For example, the Bureau could take the position that a credit card issued by a not-for-profit credit union (or similar entity) is a "class of transaction" for purposes of TILA.

Each of the provisions cited above (other than the CLA) provide that the exemption authority must be used as necessary or appropriate to fulfill the purposes of the underlying statute. Similar to the discussion above with respect to Section 1022, the need to determine that an exemption is appropriate to fulfill the purposes of the underlying statute would apply in the context of providing an exemption for credit unions; that is, where applicable, the Bureau would have to determine that an exemption for credit unions meets the underlying purpose of the statute. Depending on the specific exemption being considered, the Bureau may determine that an exemption for credit

[23] 15 U.S.C. § 1693b(b). Note that such an exemption may only be for a period of five (5) years and only may be extended if the Bureau determines that such exemption remains appropriate. 15 U.S.C. § 1693b(c).
[24] 12 U.S.C. § 2804(a).
[25] 12 U.S.C. § 2617(a).
[26] 15 U.S.C. § 1667f(a)(2).

unions is consistent with a statute's purpose, such as if the Bureau were to find that such an exemption would ensure or expand consumer access to a particular financial product or service. For example, the Bureau is currently considering a remittance regulation under Regulation E. In this context, the Bureau may determine that an exemption for credit unions is consistent with the EFTA's purpose.

Although not exemption authority *per se*, we note that Section 904 of the EFTA directs the Bureau by regulation to modify the requirements of the EFTA "on small financial institutions if the Bureau determines that such modifications are necessary to alleviate any undue compliance burden on small financial institutions and such modifications are consistent with the purpose and objective of" the EFTA.[27] In addition to the Bureau's authority under the EFTA to provide for exceptions, including potentially for small financial institutions, the Bureau also would have the authority to modify (and presumably reduce the compliance burden associated with) specific requirements of the EFTA for small financial institutions.

Exemption Authority for Specific Statutory Provisions

A number of the enumerated consumer laws, specifically, TILA, FCBA, FCRA, GLBA, Section 43(d) of FDIA and HOEPA, include provisions that permit the Bureau to make exceptions from specific requirements of those laws (as opposed to exemptions from the laws generally). In some cases, such as, for example, TILA, this specific exemption authority is in addition to other exemption authority.

- Section 129D of TILA provides that the Bureau may exempt from the requirements of Section 129D(a) (relating to escrow or impound accounts) a creditor that: (1) operates predominantly in rural or underserved areas; (2) together with all affiliates, has total annual mortgage loan originations that do not exceed a limit set by the Bureau; (3) retains its mortgage loan originations in portfolio; and (4) meets any asset size threshold and any other criteria the Bureau may establish, consistent with the statutory purpose.[28]

- The FCBA provides that the Bureau may by rule provide "reasonable exceptions" to the statute's limitation on increases in the annual percentage rate for promotional rates for credit card accounts within the first six month such rate is effective.[29]

- Section 615(h) of the FCRA specifies that the Bureau's rules to implement the risk-based pricing requirements must address "exceptions to the [risk-based

[27] 15 U.S.C. § 1693b(c).
[28] 15 U.S.C. § 1639d(c). Note that the Federal Reserve Board issued a proposal in March 2011 to make such an exemption. *See* 76 Fed. Reg. 11,598 (Mar. 2, 2011).
[29] 15 U.S.C. § 1666i-2(b).

pricing] notice requirement . . . for classes of persons or transactions regarding which the agencies determine that notice would not significantly benefit consumers."[30]

- Section 504 of the GLBA provides that the Bureau's regulations to implement the GLBA privacy provisions may include exceptions to Section 502's opt-out requirements and limitations on reuse of information and sharing of account numbers for marketing purposes.[31]

- Section 43(d) of the FDIA provides that the Bureau may make exceptions to the Section 43(b) disclosure requirements applicable to depository institutions that do not have federal deposit insurance (*i.e.*, consumer oriented disclosures regarding the fact that an institution lacks federal deposit insurance) for any such institution that "does not receive initial deposits of less than an amount equal to the standard maximum deposit insurance amount from individuals who are citizens or residents of the United States, other than money received in connection with any draft or similar instrument issued to transmit money."[32]

- Section 129 of HOEPA provides that the Bureau may by rule exempt specific mortgage products or categories of mortgages from certain of Section 129's prohibitions, such as for prepayment penalties, balloon payments and negatively amortizing loans.[33]

To the extent that this exemption authority is not based on a specific type of transaction or product (like the HOEPA exemption authority), the Bureau would not have to address the scope of a "class of transaction" in order to use such authority, as discussed above. That is, the Bureau would not need to define a type of institution, such as a credit union, as a "class of transaction" in order to use this exemption authority. For example, to the extent a provision simply indicates that the Bureau has the authority to make exemptions without imposing conditions on such authority (*e.g.*, section 504 of the GLBA), the Bureau should have greater authority than under a provision that limits its exemption authority to certain types of transactions or products or under a provision that requires that the Bureau find that an exemption is appropriate to carry out the purposes or objectives a statute. As a result, the Bureau may have even greater flexibility to make exemptions for credit unions under these provisions than the "class of transactions" authority discussed above.

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[30] 15 U.S.C. § 1681m(h)(6)(B)(iii).
[31] 15 U.S.C. § 6804(b).
[32] 12 U.S.C. § 1831t(d).
[33] 15 U.S.C. § 1639(p)(1). Note that the Bureau must find that an exemption is in the interest of the borrowing public and will apply only to products that maintain and strengthen home ownership and equity protection. 15 U.S.C. §§ 1639(p)(1)(A) - (B).

Substantially Similar State Law Exemption Authority

A number of the enumerated consumer laws authorize the Bureau to exempt from coverage under those laws classes of transactions that are subject to state laws that impose substantially similar state requirements or provide for greater consumer protection and that make adequate provision for enforcement. Specifically, TILA, FCBA, HMDA, CLA and FDCPA include this type of exemption authority.

- Section 123 of TILA directs the Bureau by regulation to exempt from the requirements of Chapter 2 of TILA (relating to consumer credit cost disclosures) "any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under [Chapter 2], and that there is adequate provision for enforcement."[34]

- The FCBA directs the Bureau to exempt from the requirement of the statute "any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under [the Act] or that such law gives greater protection to the consumer, and that there is adequate provision for enforcement."[35]

- HMDA provides that the Bureau may by rule exempt from HMDA's requirements "any State-chartered depository institution within any State or subdivision thereof, if the [Bureau] determines that, under the law of such State or subdivision, that institution is subject to requirements that are substantially similar to those imposed under [HMDA], and that such law contains adequate provisions for enforcement."[36]

- The CLA directs the Bureau to write rules exempting from the requirements of the statute "any class of lease transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under [the Act] or that such law gives greater protection and benefit to the consumer, and that there is adequate provision for enforcement."[37]

- The Fair Debt Collection Practices Act ("FDCPA") directs the Bureau to exempt from the FDCPA's requirements "any class of debt collection practices within any State if the Bureau determines that under the law of that State that class of debt

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[34] 15 U.S.C. § 1633. Note that the Bureau has proscribed procedures for a state to apply for such an exemption. 12 C.F.R. pt. 1026, App. B.
[35] 15 U.S.C. § 1666j(b).
[36] 12 U.S.C. § 2805(b).
[37] 15 U.S.C. § 1667e(b).

collection practices is subject to requirements substantially similar to those imposed by [the FCPA], and that there is adequate provision for enforcement."[38]

This type of exemption authority is more limited than the others discussed above. First, the Bureau must find that a class of transactions subject to the specific federal statute is also subject to a similar state law. This factor itself could limit the availability of the exemption to state-chartered credit unions in some instances. The Bureau also must find that the state law's requirements are "substantially similar" to those imposed by the federal statute. In addition, the Bureau must find that there is adequate provision for enforcement of the state laws. Also, this type of exemption authority is frequently limited to exempting classes of transactions. Since credit unions only would be exempt if they were also subject to substantially similar state laws, it is not clear whether this exemption authority would be as meaningful as the other exemption authorities discussed herein.

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[38] 15 U.S.C. § 1692o.