



Testimony of

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On behalf of the

**Independent Community Bankers of America**

Before the

U.S. House of Representatives  
Committee on Financial Services  
Subcommittee on Financial Institutions and Consumer Credit

Hearing on

**“Regulatory Relief for Small Community Financial  
Institutions”**

April 16, 2013  
Washington, D.C.

Chairman Capito, Ranking Member Meeks, and members of the subcommittee, my name is William A. Loving, Jr., and I am President and CEO of Pendleton Community Bank, a \$260 million asset bank in Franklin, West Virginia that serves four rural markets in West Virginia and one Virginia community. I am also Chairman of the Independent Community Bankers of America and I testify today on behalf of its nearly 5,000 members. Thank you for convening this hearing on regulatory relief for small community financial institutions. Community banks nationwide have identified regulatory burden as a top concern and impediment to their viability and ability to provide credit in their communities.

America's 7,000 community banks are critical to the prosperity of the U.S. economy, particularly in micropolitan and rural communities. Providing 60 percent of all small business loans under \$1 million, as well as customized mortgage and consumer loans suited to the unique characteristics of their local communities, community banks are playing a vital role in ensuring the economic recovery is robust and broad based, reaching communities of all sizes and in every region of the country.

In order to reach their full potential as catalysts for entrepreneurship, economic growth, and job creation, community banks must have regulation that is calibrated to their size, lower-risk profile, and traditional business model. Working with community bankers from across the nation, ICBA has developed its Plan for Prosperity, a platform of legislative recommendations that will provide meaningful relief for community banks and allow them to thrive by doing what they do best – serving and growing their communities. By rebalancing unsustainable regulatory burden, the Plan will ensure that scarce capital and labor resources are used productively, not sunk into unnecessary compliance costs, allowing community banks to better focus on lending and investing that will directly improve the quality of life in our communities. Each provision of the Plan was crafted to preserve and strengthen consumer protections and safety and soundness. The Plan for Prosperity is attached to this testimony.

I would like to thank this Committee and the House for quickly passing a key provision of the Plan for Prosperity, relief from annual privacy notice mailings when a bank has not changed its privacy policies. My bank simply does not have the scale to automate the annual privacy notice mailings. For us, the mailings are a manual, fairly labor intensive process. The Privacy Notice Confusion Elimination Act (H.R., 749), introduced by Rep. Blaine Luetkemeyer, will save my bank approximately \$10,000 a year, real money for a community bank. And importantly, it will do so without putting consumers at risk or reducing their control over the use of their personal data. I encourage this committee to build on the success of H.R. 749 by taking up additional provisions of the Plan for Prosperity that will match or significantly exceed the relief provided by H.R. 749 without increasing risk to customers, community banks, or the financial system.

Perhaps the most serious threat to the community bank business model is the Basel III proposed capital rules. I'm grateful for the opportunity to testify before this subcommittee last November on that topic, and I thank the many members of the Financial Services Committee who have sent letters to the banking regulators expressing their serious concerns about the impact of Basel III and the standardized approach on community banks. Pending the final rule, which is expected this spring, I will focus my remarks today on regulatory relief proposals in the Plan for Prosperity.

While we have recommended specific regulatory relief measures in our Plan for Prosperity, the problem is a cumulative one. Regulations have accreted steadily over past decades, but are rarely removed or modernized, resulting in a redundant and sometimes conflicting burden. To set the stage for this discussion, I'd like to share with you a few broad, headline numbers to illustrate how increasing regulatory burden is fundamentally changing the nature of the business of community banking.

- The cost of Pendleton Community Bank's annual compliance audit increased by 19.5 percent between 2010 and 2012. This is just the cost of the audit, which is of course in addition to the substantial cost of compliance.
- As of 2013, Pendleton Community Bank has established a Compliance Committee consisting of 8 members of senior management that meets monthly to review compliance issues, current regulations, and the impact of proposed regulations or other rule changes on our operation and our customers. This change is a result of the increasing complexity of regulatory compliance and carries with it a costly expenditure of man-hours.
- As recently as 2007, a review of mortgage loan compliance required 3 to 4 days of work quarterly. Today, even with a 15 percent decrease in loan applications, we have to dedicate 8 to 10 days a quarter to mortgage loan compliance review. We expect this burden to increase in the coming quarters.
- Our scarce staff resources are increasingly dedicated to compliance rather than serving customers. We are now considering hiring an additional full-time employee to work exclusively on compliance because our current compliance officer is struggling to maintain the high quality of his review with increasing demands on his time. This new FTE, in addition to the 8 member Compliance Committee noted above, will result in more than 10 percent of Pendleton's 79 FTE staff with a significant role in compliance.

Again, these are just a few broad indicators, though they illustrate a clear trend of growing regulatory burden. I will provide more impact data in the context of the specific provisions covered below, beginning with our recommendations to preserve community bank mortgage lending.

### **Mortgage Reform for Community Banks**

Every aspect of mortgage lending will be subject to new, complex, and expensive regulations that will upend the economics of this line of business. These regulations are being enacted in response to the worst abuses of the pre-crisis mortgage market – abuses in which community banks did not engage.

Key provisions of the Plan for Prosperity are designed to keep community banks in the business of mortgage lending. The Plan for Prosperity focuses on those reforms that will have the greatest impact and are ripe for enactment, including:

- “Qualified mortgage” safe harbor status for loans originated and held in portfolio for the life of the loan by banks with less than \$10 billion in assets, including balloon mortgages;
- Exempting banks with assets below \$10 billion from escrow requirements for loans held in portfolio;
- Increasing the “small servicer” exemption threshold to 20,000 loans (up from 5,000); and
- Reinstating the FIRREA exemption for independent appraisals for portfolio loans of \$250,000 or less made by banks with assets below \$10 billion.

ICBA appreciates the CFPB's efforts to accommodate community banks in their recent rulemakings. However, we believe that they did not go far enough in providing for tiered regulation, as does the Plan for Prosperity, that will preserve the role of community banks in the mortgage marketplace.

Community banks represent approximately 20 percent of the mortgage market, but more importantly, much of this mortgage lending is concentrated in the small towns and rural areas of our country, which are not effectively served by megabanks. As the FDIC Community Banking Study showed, in one out of every five counties in the United States, the only physical banking offices are those operated by community banks. Community banks have a starkly different business model than that of larger mortgage lenders, which are driven by volume and margins. Community banks, by contrast, are relationship lenders with deep roots in their communities. Our mortgages are well underwritten because we know our customers, their businesses or employers, and the local economic conditions. The strength of our underwriting is confirmed by Federal Reserve data. In recent years, the delinquency rate of mortgages held by community banks never exceeded 4 percent, compared to 22 percent for fixed rate subprime mortgages and 46 percent for subprime variable rate mortgages. In fact, community bank mortgages have outperformed fixed rate, prime loans, thought to be the best performing category of all loans.<sup>1</sup>

A chief characteristic of community bank mortgages in small and rural communities is that they are often collateralized by unique properties without adequate comparables that don't fit the inflexible requirements of the secondary market. In addition, the borrowers may be farmers or small business owners whose debt-to-income ratios fall outside of secondary market parameters, despite their personal net worth and means to repay the loan. Large lenders shun such loans because they don't fit their underwriting models and require first-hand assessment of the property and the borrower. Only community banks are willing to extend credit to such borrowers, often through the use of balloon loans held in portfolio. Because holding a fixed rate 15 year or 30 year mortgage on the books would expose a community bank to unmanageable interest rate risk, these loans are made typically for 3 or 5 years, and repriced and renewed when they come due. Community banks have safely made balloon mortgages for many decades.

Pendleton Community Bank holds all but a few of our mortgage loans in portfolio, including balloon loans. This is broadly typical of community banks. In a recent survey of community banks, 50 percent of respondents hold all of their mortgage loans in portfolio, and 72 percent of respondents hold at least half of their mortgage loans in portfolio.<sup>2</sup> While secondary market sales are a significant line of business for an important segment of the community banking industry, ICBA estimates that community banks under \$10 billion in assets may hold as much as \$412 billion in balloon payment mortgages for as many as 5.5 million borrowers.<sup>3</sup> For many community banks, portfolio lending is a necessary corollary of the types of mortgages they underwrite – mortgages that cannot be securitized.

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<sup>1</sup> "Community Banks and Mortgage Lending," Remarks by Federal Reserve Governor Elizabeth Duke. November 9, 2012.

<sup>2</sup> ICBA Mortgage Lending Survey, September 2012.

<sup>3</sup> This estimate is based on recent call report data which shows that community banks under \$10 billion in assets hold a total of \$550 billion in residential 1-4 family mortgages. Assuming that balloon payment mortgages account for 75% of community bank mortgages assets, which is consistent with survey results, the result is \$412 billion in balloon payment mortgages. Assuming an average loan balance of \$75,000, the result is 5.5 million borrowers.

Another corollary of community bank customized underwriting is that the loans often meet the regulatory definition of “higher priced mortgage loans.” Because the loans cannot be securitized they must be funded through retail deposits which include higher cost certificates of deposits, and this results in a higher interest rate. The regulatory definition is heavily weighted toward the pricing that Fannie Mae and Freddie Mac set based on their ability to access capital and funding markets that are not available to community banks. In addition, in today’s historically-low interest rate environment, it is more likely that a reasonably-priced loan will meet the Federal Reserve’s definition of “higher priced.” Almost half of survey respondents (44 percent) said that more than 70 percent of their loans were “higher priced.” In Pendleton Bank’s portfolio, 89 percent of the HMDA reportable loans originated in 2012 meet the regulatory definition of “higher priced.”

This lending model – customized balloon loans held in portfolio and, due to a higher cost of funds, priced higher than securitized loans – has worked well for decades and is a proven private market solution that serves certain borrowers and communities that cannot access the secondary market. If this lending model is made infeasible by new regulation, rural borrowers will have no place to turn and be deprived of credit. The communities they live in will stagnate.

This community bank model of providing mortgages and making home ownership possible to those who, in many cases, would have no other option is under direct threat because the loans share superficial characteristics with subprime loans such as balloon terms and relatively high rates – loan terms that have been targeted by new mortgage regulation. The new ability-to-repay regulations will expose lenders to litigation risk unless their loans meet the definition of “qualified mortgage.” However, a staple of community bank mortgage lending, balloon loans, are explicitly excluded from “qualified mortgage” status unless they are made in rural areas under an unreasonably narrow definition of “rural.” ICBA has applied the CFPB’s definition of rural to every county in the U.S. The results are shown in an attachment to this testimony. I think the members of this committee will be surprised at what counties in their own states and districts fail to qualify as “rural.” For example, in the state of West Virginia, 26 out of 55 counties fail to meet the definition of rural. Under any reasonable definition, the entire state of West Virginia should be considered rural. ICBA is urging the CFPB to expand its definition.

Similarly, “higher priced” loans – even when that pricing is aligned with the lender’s cost of funds, risk, and other factors – are excluded from the conclusive presumption of compliance (or “safe harbor”) protections under “qualified mortgage” and instead carry only a “rebuttable presumption of compliance,” a much weaker protection which exposes the lender to unacceptable litigation risk for the life of the loan. We appreciate that the CFPB is proposing a higher price trigger for the safe harbor for community bank loans – 3.5 percent above average prime rate offer (APOR) – though we have recommended that the CFPB adopt an alternative rate threshold that takes into account a community bank’s cost of funds.

#### *“Qualified Mortgage” Status for Community Bank Portfolio Mortgages*

The Plan for Prosperity solution to this new regulatory threat is simple, straightforward, and will preserve the community bank lending model described above – safe harbor “qualified mortgage” status for community bank loans held in portfolio, including balloon loans in rural and non-rural areas and without regard to their pricing. When a community bank holds a loan in portfolio it holds 100 percent of the credit

risk and has every incentive to ensure it understands the borrower's financial condition and to work with the borrower to structure the loan properly and make sure it is affordable. Withholding safe harbor status for loans held in portfolio, and exposing the lender to litigation risk, will not make the loans safer, nor will it make underwriting more conservative, it will merely deter community banks from making such loans in the many counties that do not meet the definition of rural and where a bank's cost of funds results in "higher priced mortgages." In our case, Pendleton's mortgages are qualified mortgages because we satisfy the "rural test"; however, because our mortgages are "higher priced," they are denied "safe harbor" protections and instead carry a "rebuttable presumption of compliance," under the CFPB's final rule. Accordingly, we, like many community banks across our nation, will be forced to make a risk-reward calculation to determine whether we will continue providing mortgage financing to our communities.

#### *Escrow Requirement Exemption for Community Bank Portfolio Mortgages*

Escrow requirements for property taxes and insurance are an additional deterrent to community bank mortgage lending. Loans held in portfolio by community banks should be exempt from such requirements. When loans are held in portfolio, lenders have every incentive to protect their collateral by ensuring that tax and insurance payments are current. The escrow requirement for higher priced loans is unnecessary, impractical, and a significant expense for a community bank. A large majority of community banks do not currently escrow because of the cost and requiring them to do so will only deter them from making higher cost loans. In a September 2012 ICBA survey of over 430 community banks, 55 percent of the bankers stated they decreased their mortgage business or completely stopped providing higher-priced mortgage loans due to the expense of complying with escrow requirements for higher priced mortgages that took effect in 2010. Pendleton Community Bank began escrowing in compliance with the Federal Reserve rule at a significant investment in systems and software, employee training and legal fees. We currently escrow for 300 loans in portfolio at an expense of 300 man-hours annually. As we originate additional loans requiring escrows, we will be shackled with additional operating costs. Another West Virginia community banker I know employs four people in escrow at a cost of \$240,000 a year including benefits. Many community banks do not have the resources to do it in house. Outsourcing escrow services may not be an affordable option either. For third party servicers it is simply not economical to offer escrow-only services, not packaged with other services, to low volume lenders. The Plan for Prosperity calls for an exemption from escrow requirements for community bank loans held in portfolio.

#### *Small Servicer Exemption*

The relationship lending model, so important to community banks, extends beyond underwriting to servicing. Community banks frequently service the loans they originate, whether they are held in portfolio or sold into the secondary market. For community banks that sell their loans, retention of servicing is important to maintaining long-term relationships with customers and the opportunity to meet their future banking needs.

The community bank practices that strengthen underwriting and result in better loan performance also produce stronger servicing. Bankers that know their customers and the economic trends in their communities can better anticipate borrowers' potential difficulties and intervene early and effectively. As is true with underwriting, the data clearly show that community bank serviced mortgages perform better.

Public policy should keep community banks in the business of servicing mortgages and deter further consolidation among servicers.

In this regard, community banks are deeply concerned about the impact of servicing standards that are overly prescriptive with regard to the method and frequency of delinquent borrower contacts, reducing community banks' flexibility to use methods that have proved successful in holding down delinquency rates. Examples of difficult and unnecessary requirements include new monthly statements; additional notices regarding interest rate adjustments on ARM loans; rigid timelines for making contacts that leave no discretion to the servicer; and restrictions on forced placed insurance. Community banks' small size and local presence in the communities we serve make many of these requirements unnecessary.

The CFPB's recent servicing rule provides a small servicer exemption for banks that service fewer than 5,000 loans. We appreciate recognition that the rule is not appropriate for smaller servicers but believe that the CFPB set the threshold too low. Many community banks service larger portfolios that should qualify for an exemption because they use the community bank servicing practices and obtain the strong performance results. A West Virginia community banker I know is not exempt because he services 6600 accounts, yet has a very low delinquency rate, less than 4 percent. This banker estimates the monthly statement requirement alone will cost him about \$181,500 annually. He will also have to hire an additional collector, even with his low delinquency rate, to comply with the new early intervention requirements. ICBA's Plan for Prosperity calls for raising the small servicer exemption threshold to 20,000 loans. To put this proposed threshold in perspective, the average number of loans serviced by the five largest servicers subject to the national mortgage settlement is 6.8 million.<sup>4</sup> An exemption threshold of 20,000 would demarcate small servicers from both large and mid-sized servicers. It would help preserve the important role of community banks in servicing mortgages and deter further industry consolidation which is harmful to borrowers.

#### *Appraisal Exemption for Community Bank Portfolio Mortgages*

Appraisal standards have changed significantly over the past few years. First as a result of the Home Valuation Code of Conduct from Fannie Mae and Freddie Mac, and more recently as a result of the Dodd-Frank Act. These standards are well intentioned, having been designed to prevent abuses by unregulated mortgage brokers that contributed to the collapse of the housing market. However, they have made it nearly impossible for my bank to use local appraisers. As a result, Pendleton began using an appraisal management company in early 2013. This is quickly becoming the only practical option for a community bank mortgage lender. This expense, coupled with new appraisal requirements, has increased the cost of an appraisal for Pendleton's customers by 40 percent, an experience that is typical of other community banks. Passed on to the borrower, these costs increase the cost of credit. What's more, because the appraisal management company uses appraisers from outside the area, they produce poorer quality appraisals. ICBA's Plan for Prosperity calls for reinstating the FIRREA exemption for independent appraisals for portfolio loans of \$250,000 or less made by banks with assets below \$10 billion.

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<sup>4</sup> Source: Office of Mortgage Settlement Oversight ([www.mortgageoversight.com](http://www.mortgageoversight.com)).

## **Strengthen Accountability in Examinations**

The trend toward oppressive, micromanaged regulatory exams is a concern to community bankers nationwide. ICBA believes that the best means of creating a more balanced exam environment is to create a workable appeals process. ICBA's Plan for Prosperity calls for the creation of an independent body to receive, investigate, and resolve material complaints from banks in a timely and confidential manner. The goal is to hold examiners accountable and to prevent retribution against banks that file complaints.

The current appeals process is arbitrary and frustrating. Appeals panels, or other processes, routinely lack the independence and market expertise necessary to reach a fair, unbiased decision. The Financial Institutions Examination Fairness and Reform Act, introduced in the last Congress, would go a long way toward improving the oppressive examination environment by creating a workable appeals process and consistent, commonsense standards for classifying loans. We are grateful to Chairman Capito and Representative Maloney for introducing this legislation which would improve the appeals process by taking it out of the examining agencies and empowering a newly created Ombudsman, situated in the Federal Financial Institutions Examination Council, to make final appeals decisions. Though we favor additional measures to bring a higher level of accountability to the regulators and their field examiners, we are pleased to support the provisions this legislation.

## **Municipal Advisor Registration Exemption**

ICBA's Plan for Prosperity calls for exempting community banks and their employees from registration as municipal advisors with the Securities and Exchange Commission and the Municipal Securities Rulemaking Board. Community banks have always provided traditional banking services such as demand deposits, certificates of deposit, cash management services, loans and letters of credit to the municipal governments of the communities they serve. Pendleton Community Bank currently has numerous municipal relationships and \$17 million in municipal deposits. Our servicing of these accounts is closely supervised by our prudential bank regulator. The registration requirement, if interpreted broadly by the SEC, could force Pendleton and thousands of community banks to register as municipal advisors with the SEC and the Municipal Securities Rulemaking Board and be examined by the SEC in order to continue providing traditional banking services to municipalities. An act as simple as a town treasurer phoning a community bank to inquire about CD rates could be enough to trigger registration. As a one-time SEC registrant, we are fully aware of the additional costs associated with registration, not to mention the time devoted to ensuring that we fully understand and comply with yet another regulation.

On behalf of the many community banks that enjoyed substantial savings through the modernization of the shareholder registration threshold, I would like to thank this Committee and Congress for enacting the JOBS Act last year. This was and remains an important issue for Pendleton and other SEC registrants. So important that we decided to go through the painstaking process of deregistration approximately one year prior to modernization of the threshold because we believed that the cost of compliance produced no substantial, if any, improvement in reporting to our shareholders. Deregistration has only confirmed that belief. Conservatively estimated, deregistration saves us \$110,000 annually, a substantial amount that can be reinvested back into our community.



I hope that the good work that Congress has done won't be compromised by now allowing the SEC to force Pendleton and other community banks to register as municipal advisors and incur a burden that is anything like the one from which we just escaped.

ICBA is grateful to Reps. Steve Stivers and Gwen Moore for introducing the Municipal Advisor Oversight Improvement Act (H.R. 797), which will exempt enumerated traditional banking activities from triggering registration.

### **Relief from Accounting and Auditing Expenses for Publicly Traded Community Banks and Thrifts**

Another provision of the Plan for Prosperity would increase the current exemption from the internal control attestation requirements of Section 404(b) of the Sarbanes-Oxley Act from \$75 million in market capitalization to \$350 million. Because community bank internal control systems are monitored continually by bank examiners, they should not have to sustain the unnecessary annual expense of paying an outside audit firm for attestation work. This provision will substantially lower the regulatory burden and expense for small, publicly traded community banks without creating more risk for investors.

Separately, due to an inadvertent oversight in the recently-passed JOBS Act, thrift holding companies cannot take advantage of the increased shareholder threshold by which a bank or bank holding company may deregister as an SEC reporting company under Section 12 of the Securities Exchange Act of 1934. As mentioned above, Pendleton Community Bank recently deregistered our stock at a significant annual savings. Thrifts should be able to reap the benefit as well.

ICBA is grateful to Reps. Womack and Himes for introducing the Holding Company Registration Threshold Equalization Act (H.R. 801) which will correct the oversight in the JOBS Act and allow thrift holding companies to use the new 1200 shareholder deregistration threshold.

### **New Charter Option for Mutual Banks**

Mutual community banks are among the safest and soundest financial institutions. They remained strong during the financial crisis and continued to provide financial services to their customers. The Plan for Prosperity calls for the creation of a new OCC charter for mutual national banks. This option would provide flexibility for institutions to choose the charter that best suits their needs and the communities they serve.

### **Cost-Benefit Analysis for New Rules**

The Plan for Prosperity calls for legislation to prevent the financial regulatory agencies from issuing notices of proposed rulemaking unless they first determine that quantified costs are less than quantified benefits. The analysis must take into account the impact on the smallest banks which are disproportionately burdened by regulation because they lack the scale and the resources to absorb the associated compliance costs. In addition, the agencies would be required to identify and assess available alternatives including modifications to existing regulations. They would also be required to ensure that proposed regulations are consistent with existing regulations, written in plain English, and easy to interpret.

ICBA strongly supports the SEC Regulatory Accountability Act (H.R. 1062), introduced by Rep. Scott Garrett (R-NJ), which would require the Chief Economist of the SEC to determine that the benefits of any proposed regulation justify the costs before adopting such regulation.

### **Consumer Financial Protection Bureau Reform**

The Plan for Prosperity calls for legislation to strengthen the accountability of the CFPB. We thank this committee and the House for passing the Consumer Financial Protection Safety and Soundness Improvement Act, sponsored by Rep. Sean Duffy (R-WI), in the 112<sup>th</sup> Congress. That legislation would reform the structure of the CFPB so that it is governed by a five member commission rather than a single director; strengthen prudential regulatory review of CFPB rules by reforming the voting requirement for an FSOC veto from a two-thirds vote to a simple majority, excluding the CFPB Director, and change the standard to allow for a veto of a rule that “is inconsistent with the safe and sound operations of United States financial institutions” – a much more realistic standard than under current law. Combined, these changes would better protect the safety and soundness of the financial system, and provide reasonable measures to insulate community banks from additional regulatory burden.

### **Modernize the Federal Reserve’s Small Bank Holding Company Policy Statement**

The Plan for Prosperity calls for the Federal Reserve to revise the Small Bank Holding Company Policy Statement – a set of capital guidelines that have the force of law. The Policy Statement, makes it easier for small bank holding companies to raise additional capital by issuing debt, would be revised to apply to both bank and thrift holding companies and to increase the qualifying asset threshold from \$500 million to \$5 billion. Qualifying bank and thrift holding companies must not have significant outstanding debt or be engaged in nonbanking activities that involve significant leverage. This will help ease capital requirements for small bank and thrift holding companies.

### **Closing**

Thank you again for the opportunity to testify today. I hope that my testimony, while not exhaustive, gives you a sense of the sharply increasing resource demands placed on community banks by regulation and examination and what’s at stake for the future of community banking.

Left unaddressed, the increasing burden of regulation will discourage the chartering of new community banks and lead to further industry consolidation. Consolidation will lead to higher loan interest rates for borrowers, lower rates paid on deposits, and fewer product choices – especially in the rural areas and small towns currently served by community banks. A more concentrated industry, dominated by a small number of too-big-to-fail banks, will jeopardize the safety and soundness of the financial system and expose taxpayers to the risk of additional costly bailouts. That’s why it’s so important to enact sensible regulatory reforms. We hope that ICBA’s Plan for Prosperity will serve as a guide to this committee. The Plan is not meant to be comprehensive or the final word on regulatory reform; we anticipate that we will add to it in response to input from the members of this committee and as the regulatory environment evolves and new challenges and proposed solutions emerge.

We encourage you to reach out to the community bankers in your district. Ask them about the current regulatory environment and whether the reforms of the Plan for Prosperity would help them to better serve their customers and the communities of your district. We’re confident that they will agree with us.

Thank you again for the opportunity to testify today. We look forward to working with this committee to craft urgently needed legislative solutions.

**Attachments**

- **ICBA Plan for Prosperity**
- **State-By-State Rural County Designation Maps** (blue counties are rural; yellow are non-rural)



# Plan for Prosperity



## A Regulatory Relief Agenda to Empower Local Communities

2013

## **Plan for Prosperity: A Regulatory Relief Agenda to Empower Local Communities**

America's 7,000 community banks are vital to the prosperity of the U.S. economy, particularly in micropolitan and rural communities. Providing 60 percent of all small business loans under \$1 million, as well as customized mortgage and consumer loans suited to the unique characteristics of their local communities, community banks are playing a vital role in ensuring the economic recovery is robust and broad based, reaching communities of all sizes and in every region of the country.

In order to reach their full potential as catalysts for entrepreneurship, economic growth, and job creation, community banks must be able to attract capital in a highly competitive environment. Regulation calibrated to the size, lower-risk profile, and traditional business model of community banks is critical to this objective. ICBA's Plan for Prosperity provides targeted regulatory relief that will allow community banks to thrive by doing what they do best – serving and growing their communities. By rebalancing unsustainable regulatory burden, the Plan will ensure that scarce capital and labor resources are used productively, not sunk into unnecessary compliance costs, allowing community banks to better focus on lending and investing that will directly improve the quality of life in our communities. Each provision of the Plan was selected with input from community bankers nationwide and crafted to preserve and strengthen consumer protections and safety and soundness.

The Plan is not a bill; it is a platform and set of legislative priorities positioned for advancement in Congress. The provisions could be introduced in Congress individually, collectively or configured in whatever fashion suits interested members of Congress. The Plan is a flexible, living document that can be adapted to a rapidly changing regulatory and legislative environment to maximize its influence and likelihood of enactment. Provisions of the Plan include:

**Support for the Housing Recovery: Mortgage Reform For Community Banks.** Provide community banks relief from certain mortgage regulations, especially for loans held in portfolio. When a community bank holds a loan in portfolio, it has a direct stake in the loan's performance and every incentive to ensure it is affordable and responsibly serviced. Relief would include: Providing "qualified mortgage" safe harbor status for loans originated and held in portfolio for the life of the loan by banks with less than \$10 billion in assets, including balloon mortgages; exempting banks with assets below \$10 billion from escrow requirements for loans held in portfolio; increasing the "small servicer" exemption threshold to 20,000 loans (up from 5,000); and reinstating the FIRREA exemption for independent appraisals for portfolio loans of \$250,000 or less made by banks with assets below \$10 billion.

One Mission. Community Banks.

**Strengthening Accountability in Bank Exams: A Workable Appeals Process.** The trend toward oppressive, micromanaged regulatory exams is a concern to community bankers nationwide. An independent body would be created to receive, investigate, and resolve material complaints from banks in a timely and confidential manner. The goal is to hold examiners accountable and to prevent retribution against banks that file complaints.

**Redundant Privacy Notices: Eliminate Annual Requirement.** Eliminate the requirement that financial institutions mail annual privacy notices even when no change in policy has occurred. Financial institutions would still be required to notify their customers when they change their privacy policies, but when no change in policy has occurred, the annual notice provides no useful information to customers and is a needless expense.

**Serving Local Governments: Community Bank Exemption from Municipal Advisor Registration.** Exempt community bank employees from having to register as municipal advisors with the SEC and the Municipal Securities Rulemaking Board. Community banks provide traditional banking services to small municipal governments such as demand deposits, certificates of deposit, cash management services, loans and letters of credit. These activities are closely supervised by state and federal bank regulators. Municipal advisor registration and examination would pose a significant expense and regulatory burden for community banks without enhancing financial protections for municipal governments.

**Creating a Voice for Community Banks: Treasury Assistant Secretary for Community Banks.** Economic and banking policies have too often been made without the benefit of community bank input. An approach that takes into account the diversity and breadth of the financial services sector would significantly improve policy making. Creating an Assistant Secretary for Community Banks within the U.S. Treasury Department would ensure that the 7,000 + community banks across the country, including minority banks that lend in underserved markets, are given appropriate and balanced consideration in the policy making process.

**Balanced Consumer Regulation: More Inclusive and Accountable CFPB Governance.** Change the governance structure of the CFPB to a five-member commission rather than a single Director. Commissioners would be confirmed by the Senate to staggered five-year terms with no more than three commissioners affiliated with any one political party. This change will strengthen accountability and bring a diversity of views and professional backgrounds to decision-making at the CFPB. In addition, FSOC's review of CFPB rules should be strengthened by changing the vote required to veto a rule from an unreasonably high two-thirds vote to a simple majority, excluding the CFPB Director.

**Relief from Accounting and Auditing Expenses: Publicly Traded Community Banks and Thrifts.** Increase from \$75 million in market capitalization to \$350 million the exemption from internal control attestation requirements. Because community bank internal control systems are monitored continually by bank examiners, they should not have to sustain the unnecessary annual expense of paying an outside audit firm for attestation work. This provision will substantially lower the regulatory burden and expense for small, publicly traded community banks without creating more risk for investors. Separately, due to an inadvertent oversight in the recently-passed JOBS Act, thrift holding companies cannot take advantage of the increased shareholder threshold below which a bank or bank holding company may deregister with the SEC. Congress should correct this oversight by allowing thrift holding companies to use the new 1200 shareholder deregistration threshold.

**Ensuring the Viability of Mutual Banks: New Charter Option and Relief from Dividend Restrictions.** The OCC should be allowed to charter mutual national banks to provide flexibility for institutions to choose the charter that best suits their needs and the communities they serve. In addition, certain mutual holding companies – those that have public shareholders—should be allowed to pay dividends to their public shareholders without having to comply with numerous “dividend waiver” restrictions as required under a recent Federal Reserve rule. The Federal Reserve rule makes it difficult for mutual holding companies to attract investors to support their capital levels. Easier payment of dividends will ensure the viability of the mutual holding company form of organization.

**Rigorous and Quantitative Justification of New Rules: Cost-Benefit Analysis.** Provide that financial regulatory agencies cannot issue notices of proposed rulemakings unless they first determine that quantified costs are less than quantified benefits. The analysis must take into account the impact on the smallest banks which are disproportionately burdened by regulation because they lack the scale and the resources to absorb the associated compliance costs. In addition, the agencies would be required to identify and assess available alternatives including modifications to existing regulations. They would also be required to ensure that proposed regulations are consistent with existing regulations, written in plain English, and easy to interpret.

**Additional Capital for Small Bank Holding Companies: Modernizing the Federal Reserve’s Policy Statement.** Require the Federal Reserve to revise the Small Bank Holding Company Policy Statement – a set of capital guidelines that have the force of law. The Policy Statement, makes it easier for small bank holding companies to raise additional capital by issuing debt, would be revised to apply to both bank and thrift holding companies and to increase the qualifying asset threshold from \$500 million to \$5 billion. Qualifying bank and thrift holding companies must not have significant outstanding debt or be engaged in nonbanking activities that involve significant leverage. This will help ease capital requirements for small bank and thrift holding companies.



**Cutting the Red Tape in Small Business Lending: Eliminate Data Collection.** Exclude banks with assets below \$10 billion from new small business data collection requirements. This provision, which requires the reporting of information regarding every small business loan application, falls disproportionately upon community banks that lack scale and compliance resources.

**Facilitating Capital Formation: Modernize Subchapter S Constraints and Extend Loss Carryback.** Subchapter S of the tax code should be updated to facilitate capital formation for community banks, particularly in light of higher capital requirements under the proposed Basel III capital standards. The limit on Subchapter S shareholders should be increased from 100 to 200; Subchapter S corporations should be allowed to issue preferred shares; and Subchapter S shares, both common and preferred, should be permitted to be held in individual retirement accounts (IRAs). These changes would better allow the nation's 2300 Subchapter S banks to raise capital and increase the flow of credit. In addition, banks with \$15 billion or less in assets should be allowed to use a five-year net operating loss (NOL) carryback through 2014. This extension of the five-year NOL carryback is countercyclical and will support community bank capital and lending during economic downturns.

*The Independent Community Bankers of America®, the nation's voice for nearly 7,000 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services. For more information, visit [www.icba.org](http://www.icba.org).*

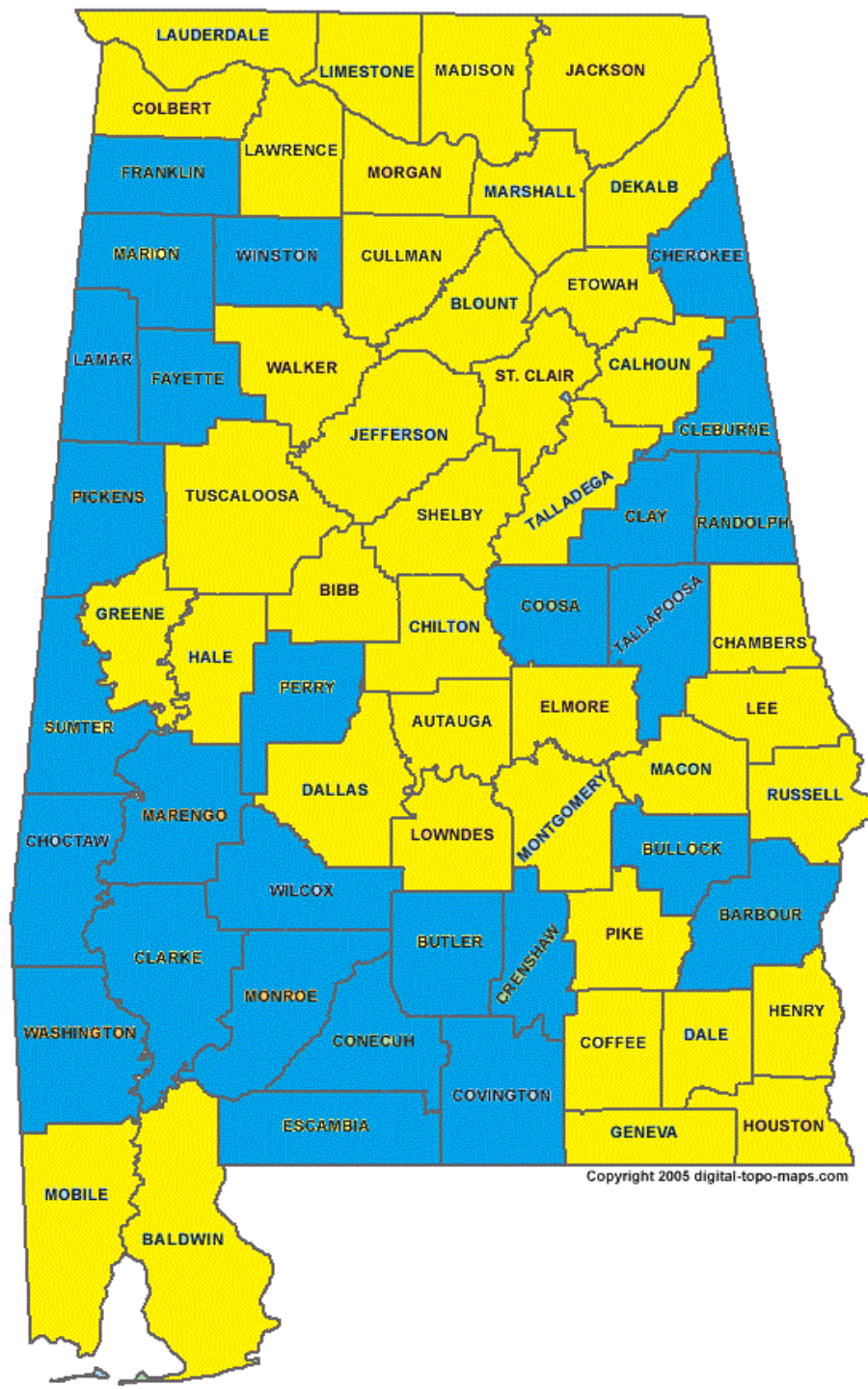
One Mission. Community Banks.



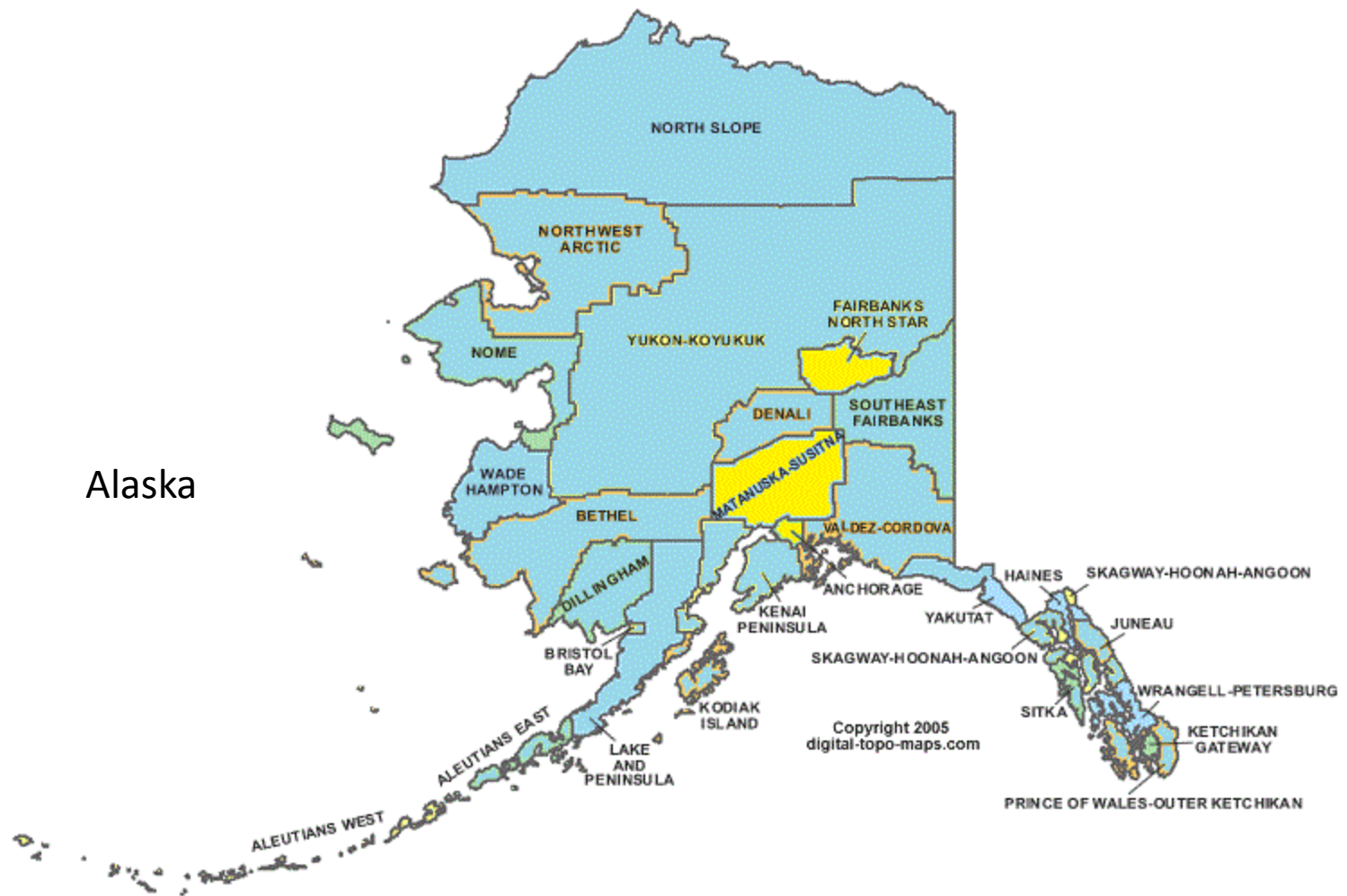
# State-by-State Impact of CFPB “Rural” Definition

Rural (blue) and Non-Rural (yellow)  
Counties Under the Consumer Financial  
Protection Bureau’s Final “Ability to  
Repay” Rule

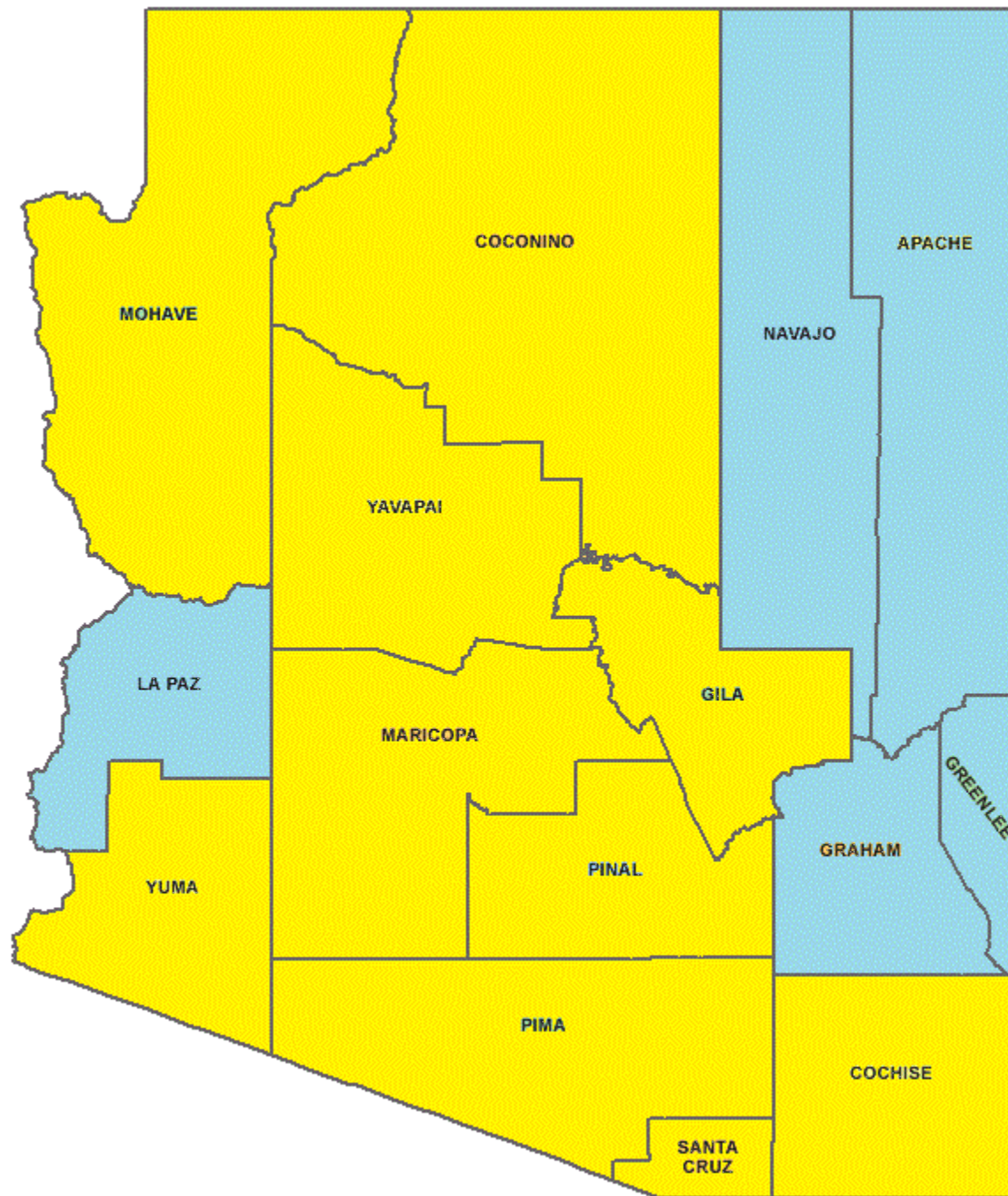
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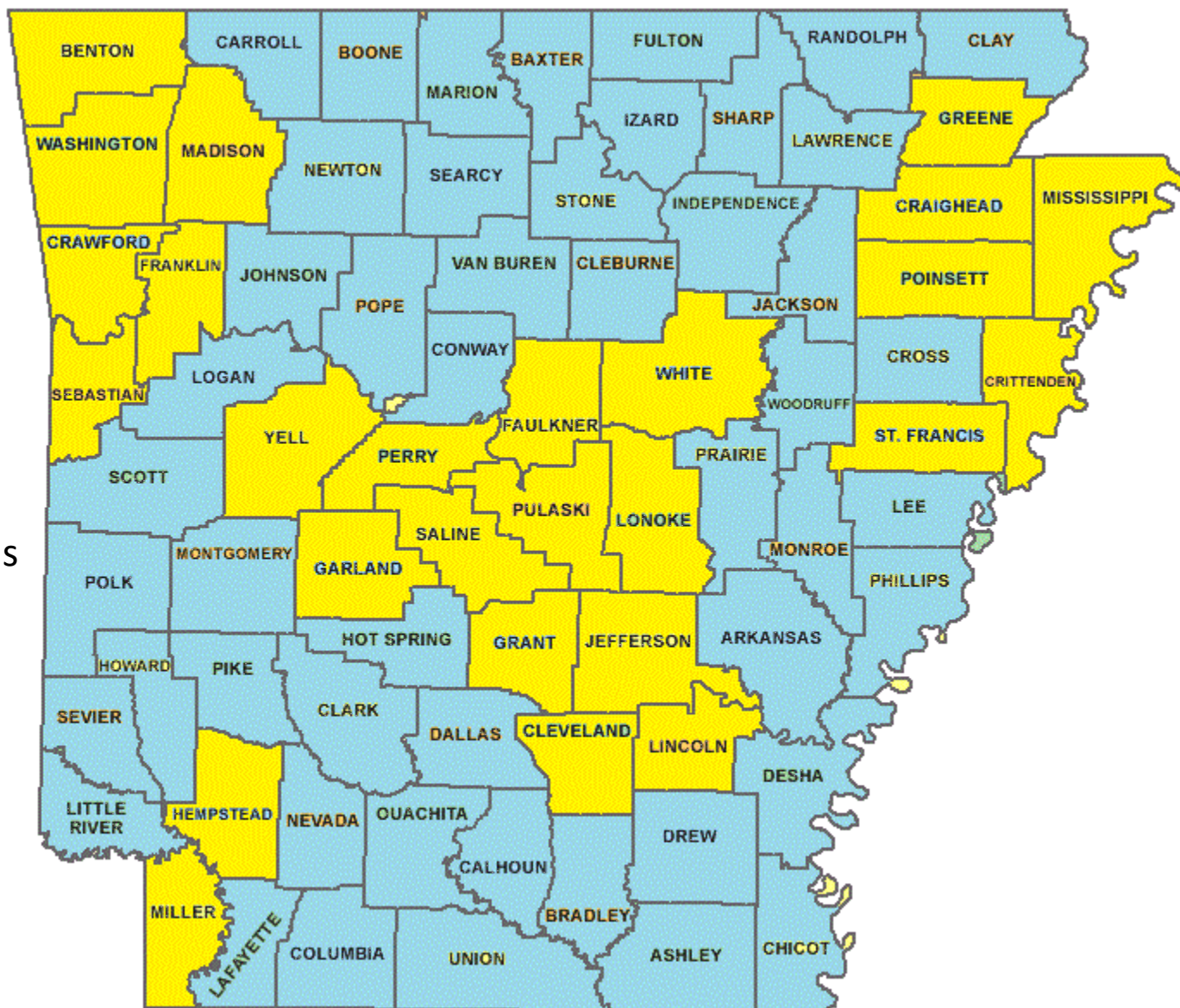
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Arizona



# Arkansas

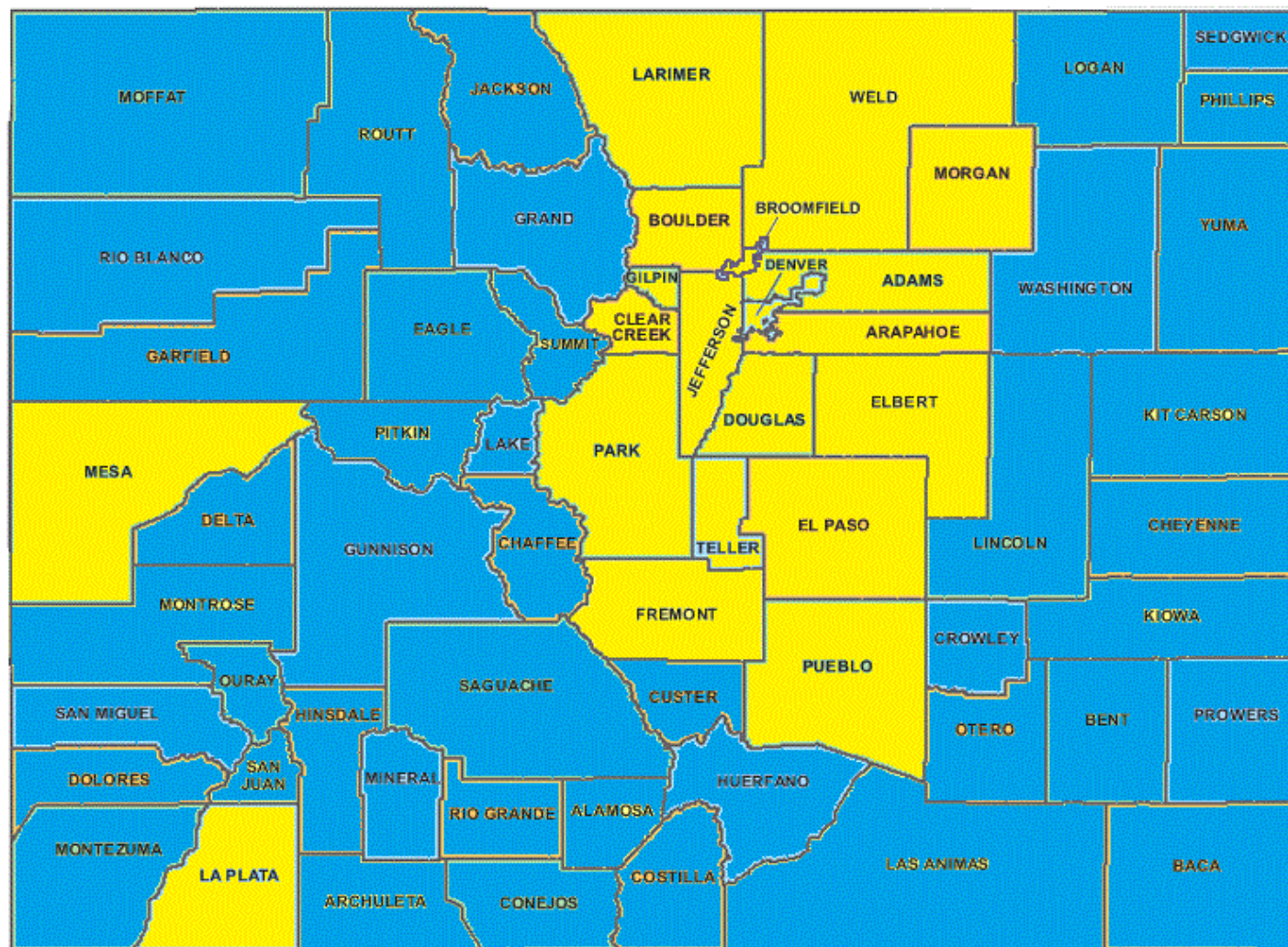




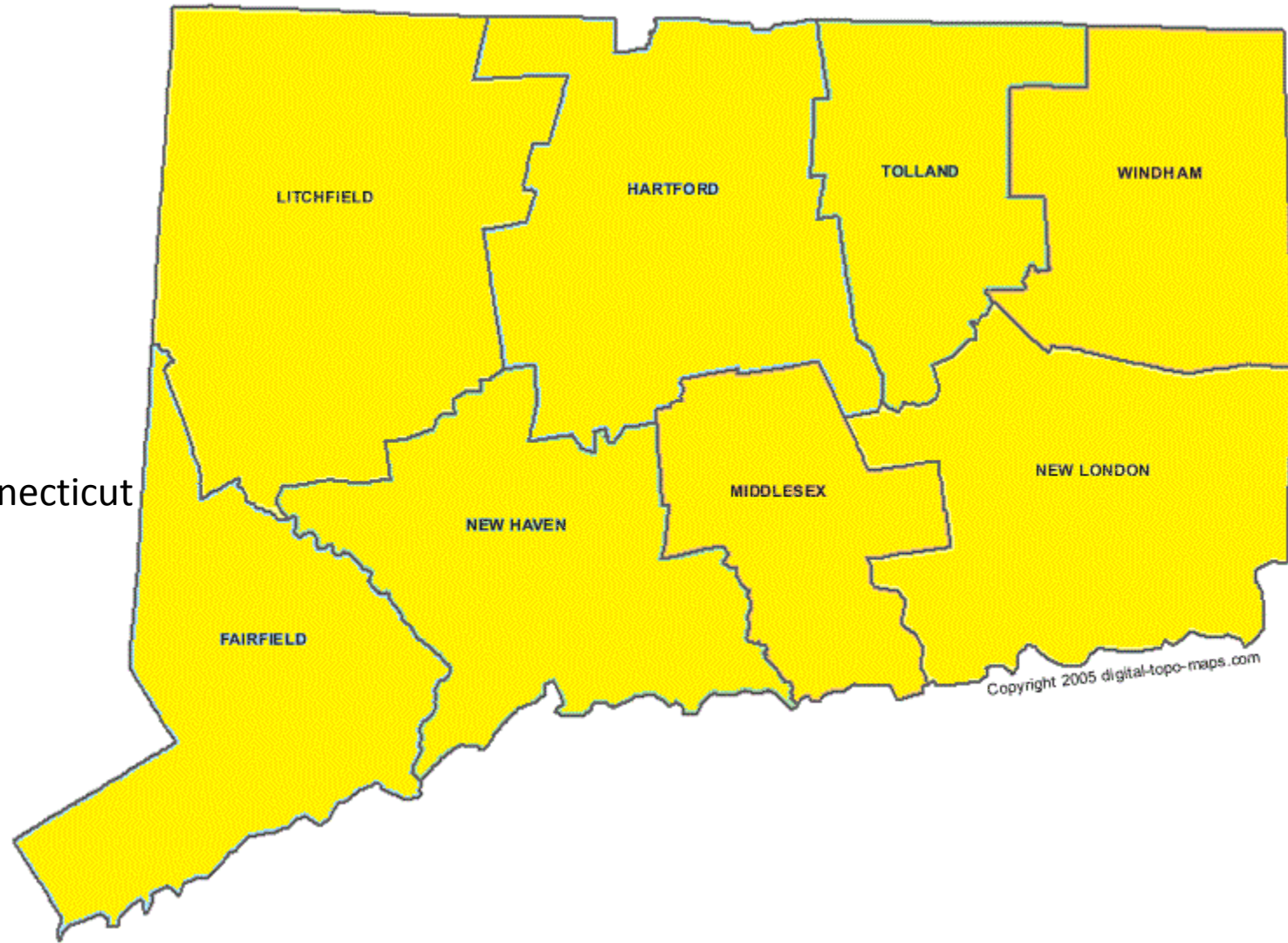
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# Colorado

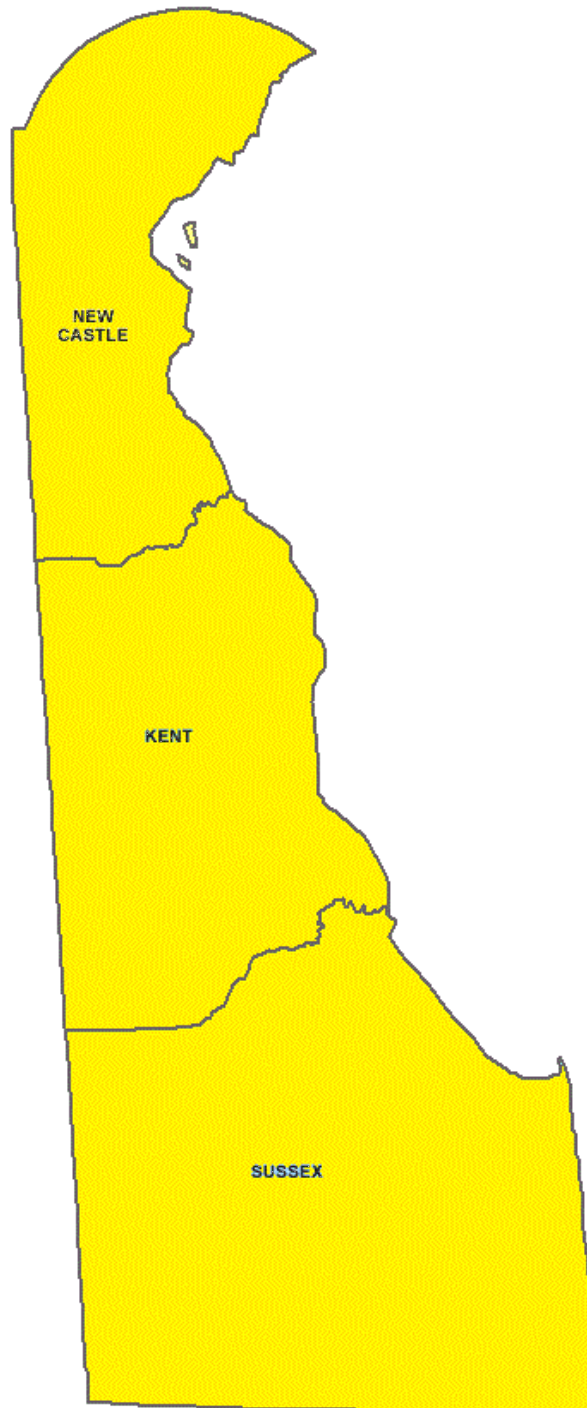


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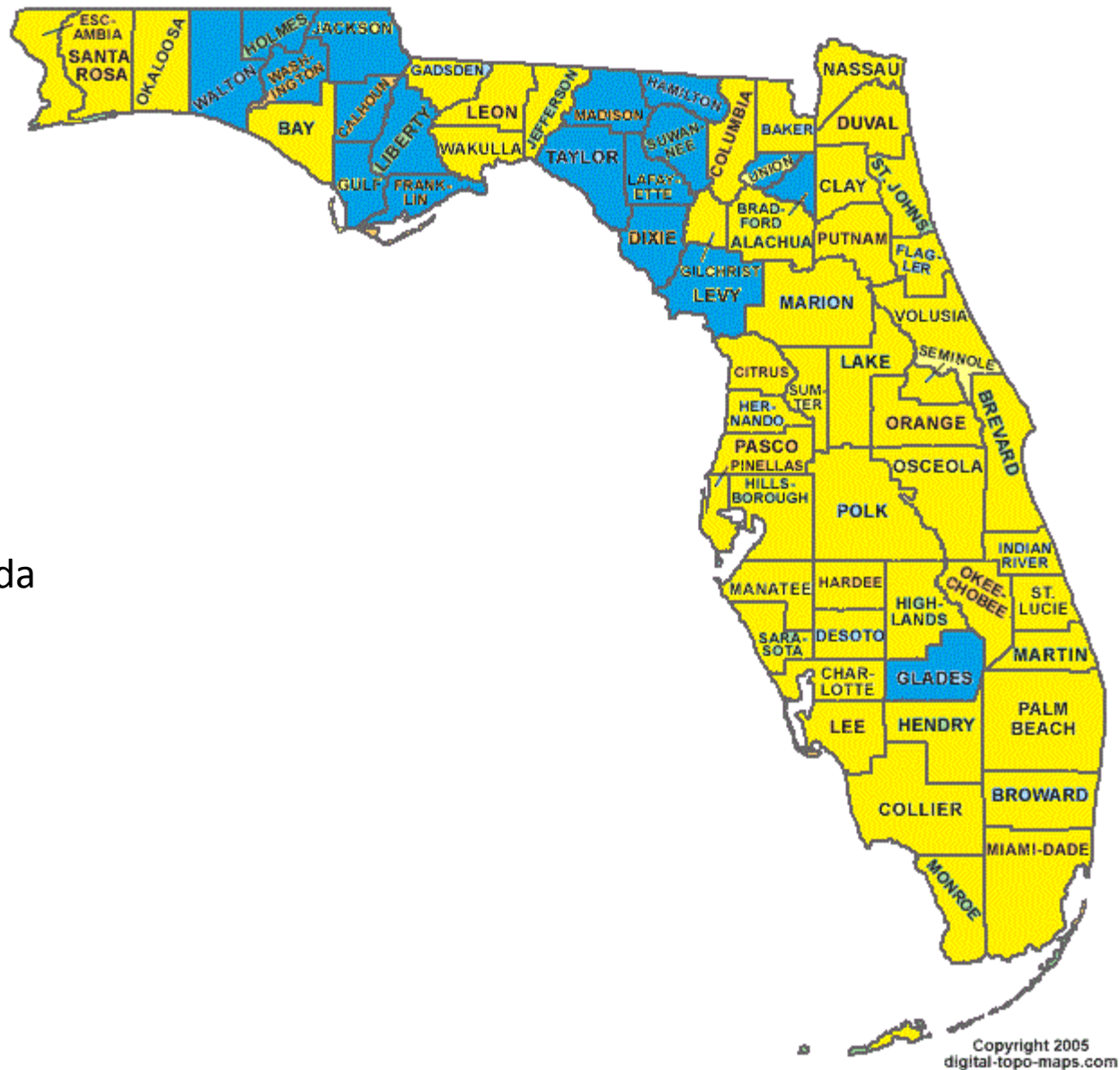




Delaware



Florida

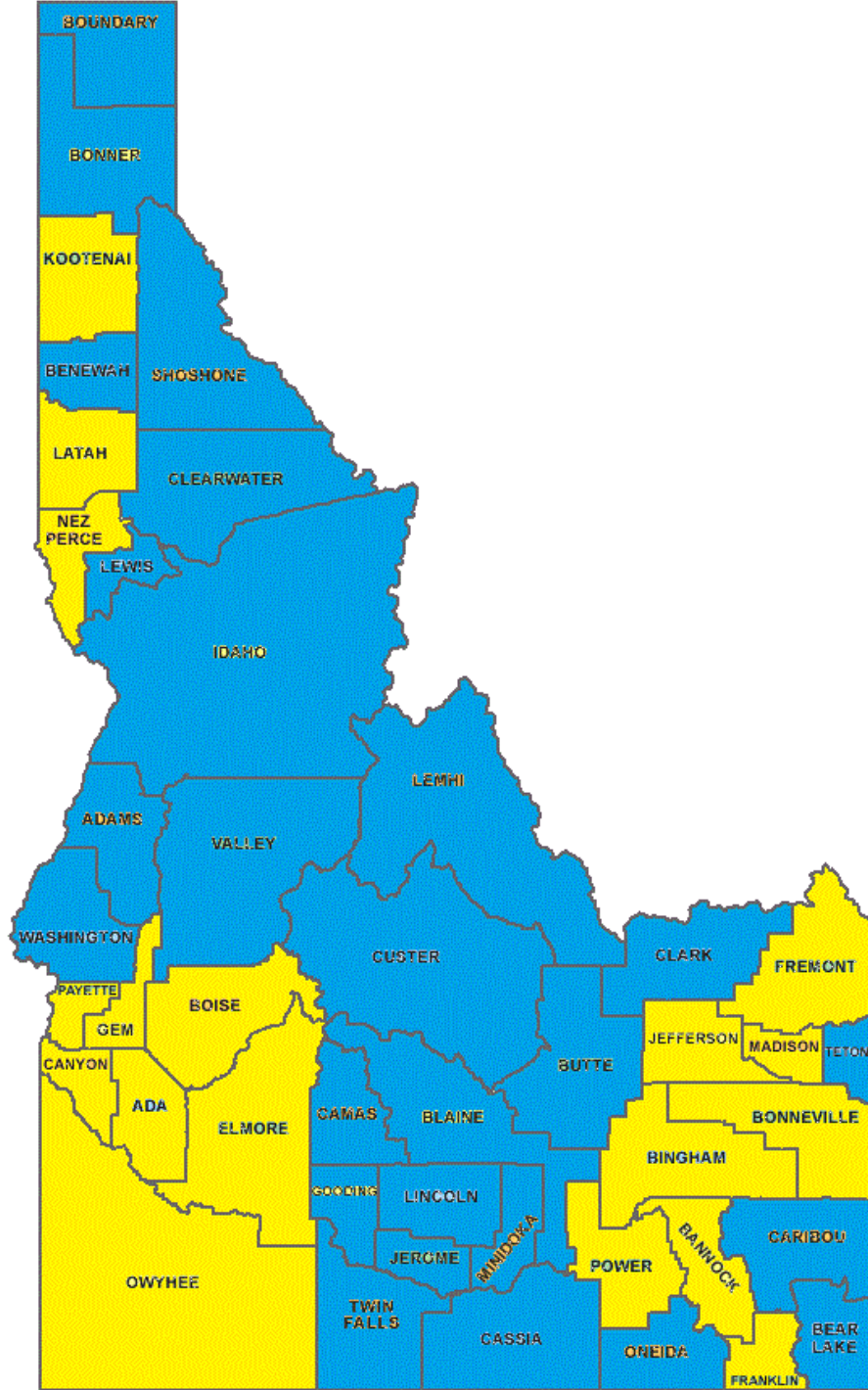


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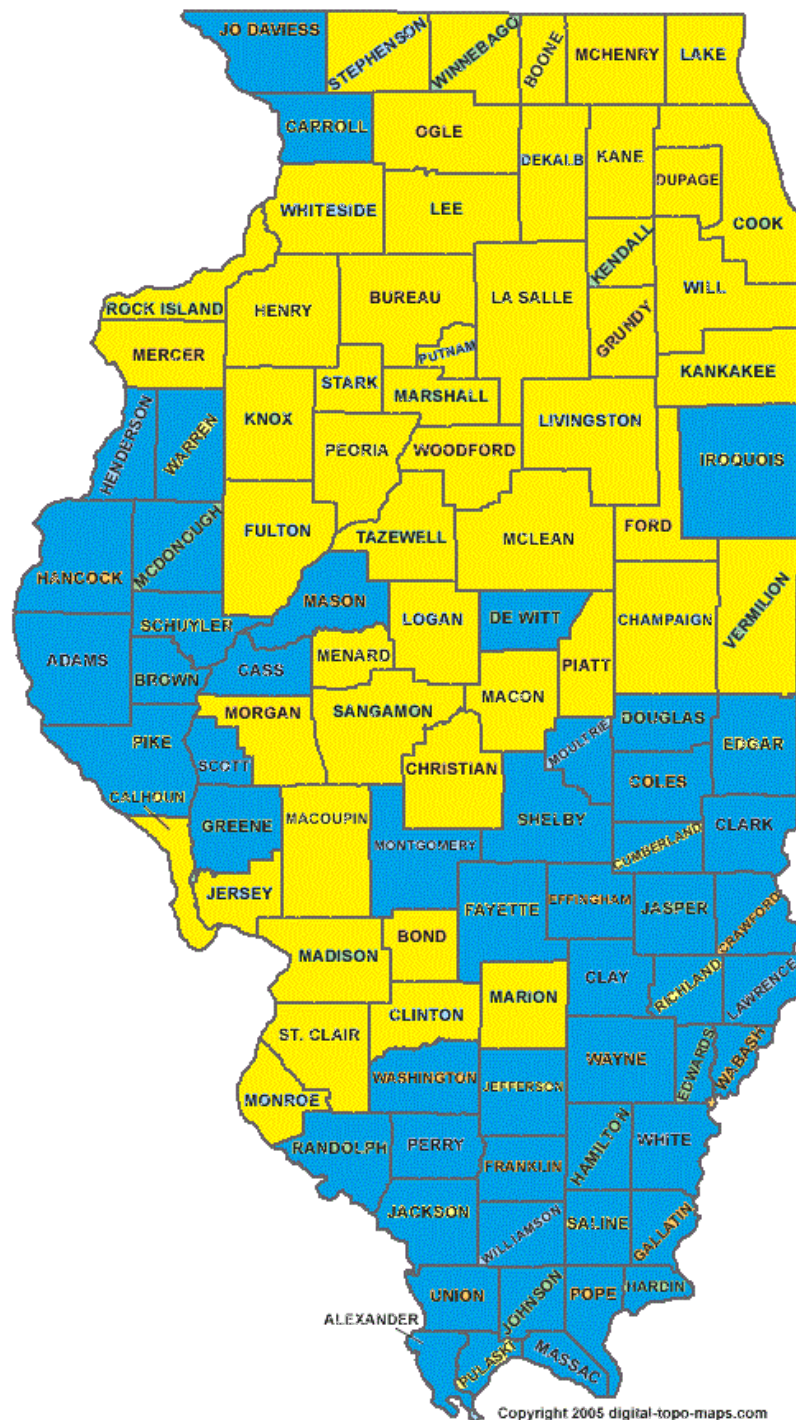
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Idaho

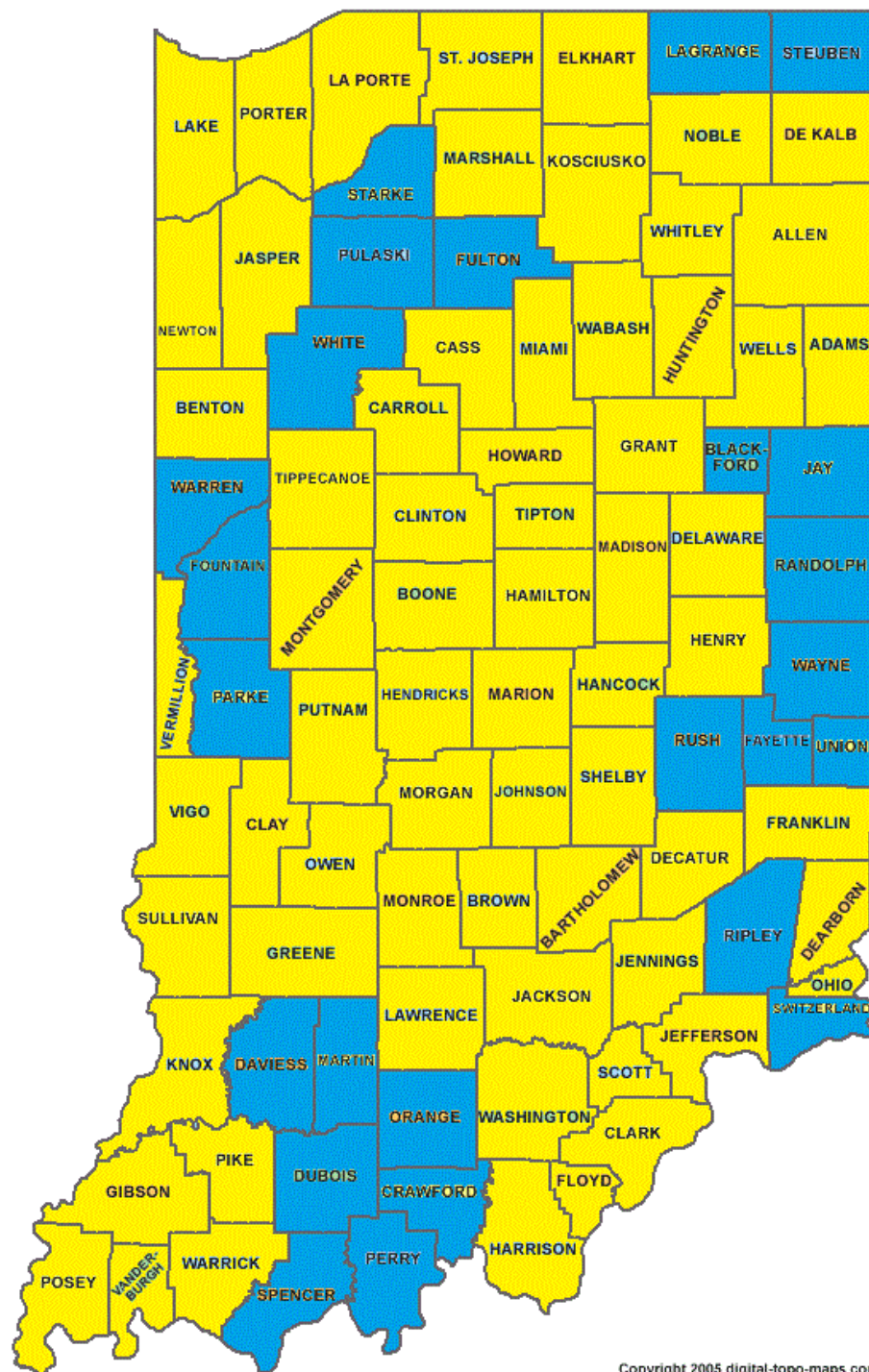




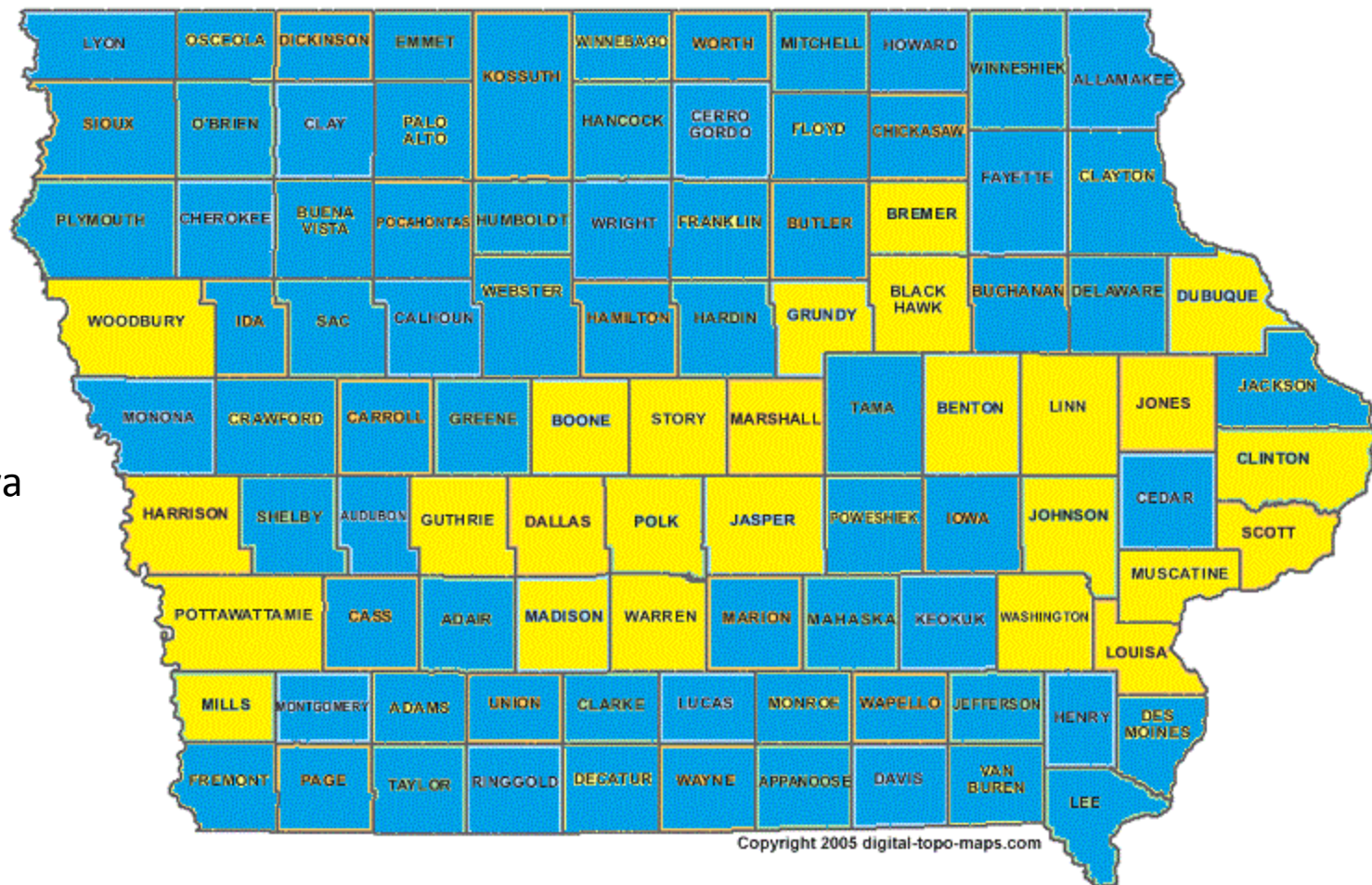
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# Indiana

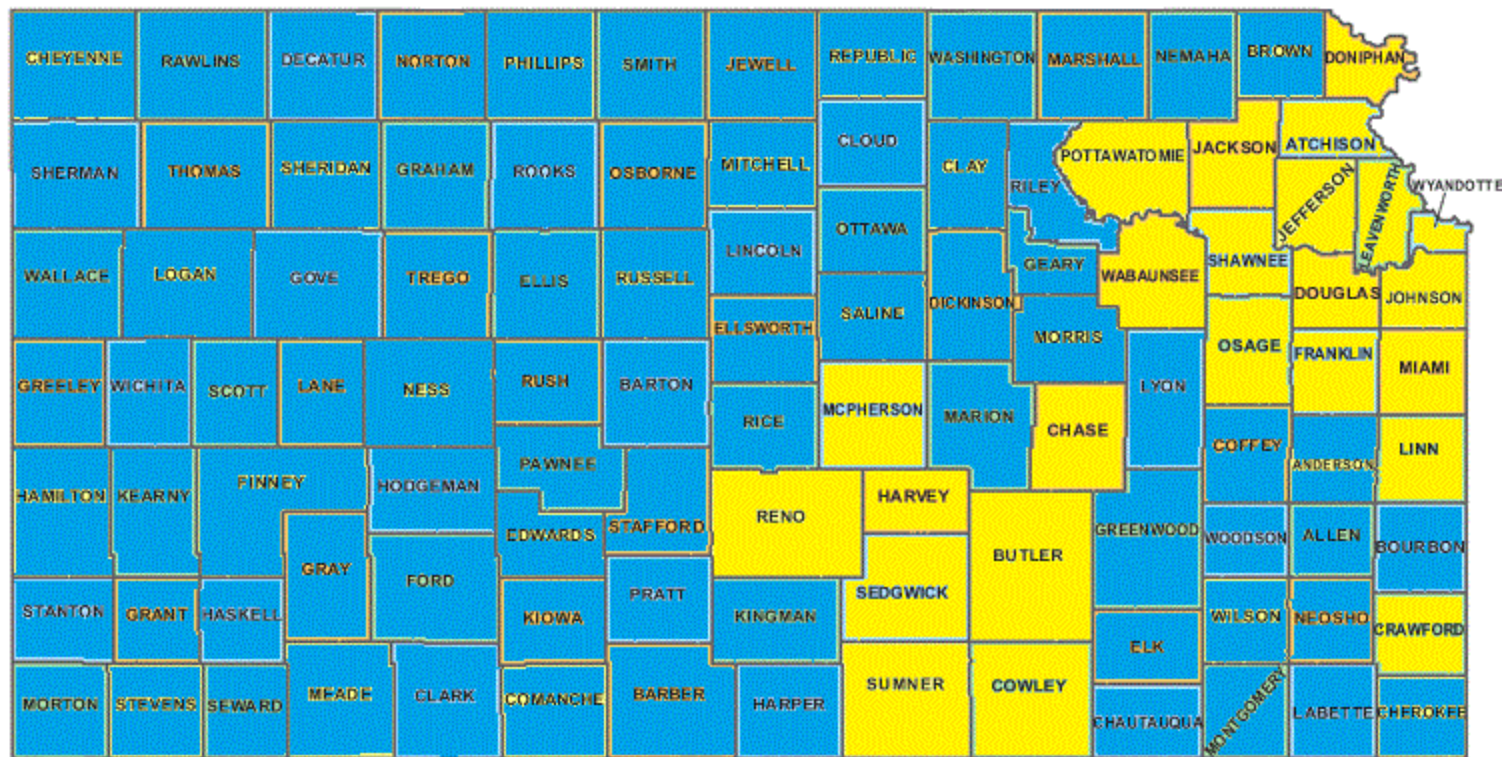


Iowa





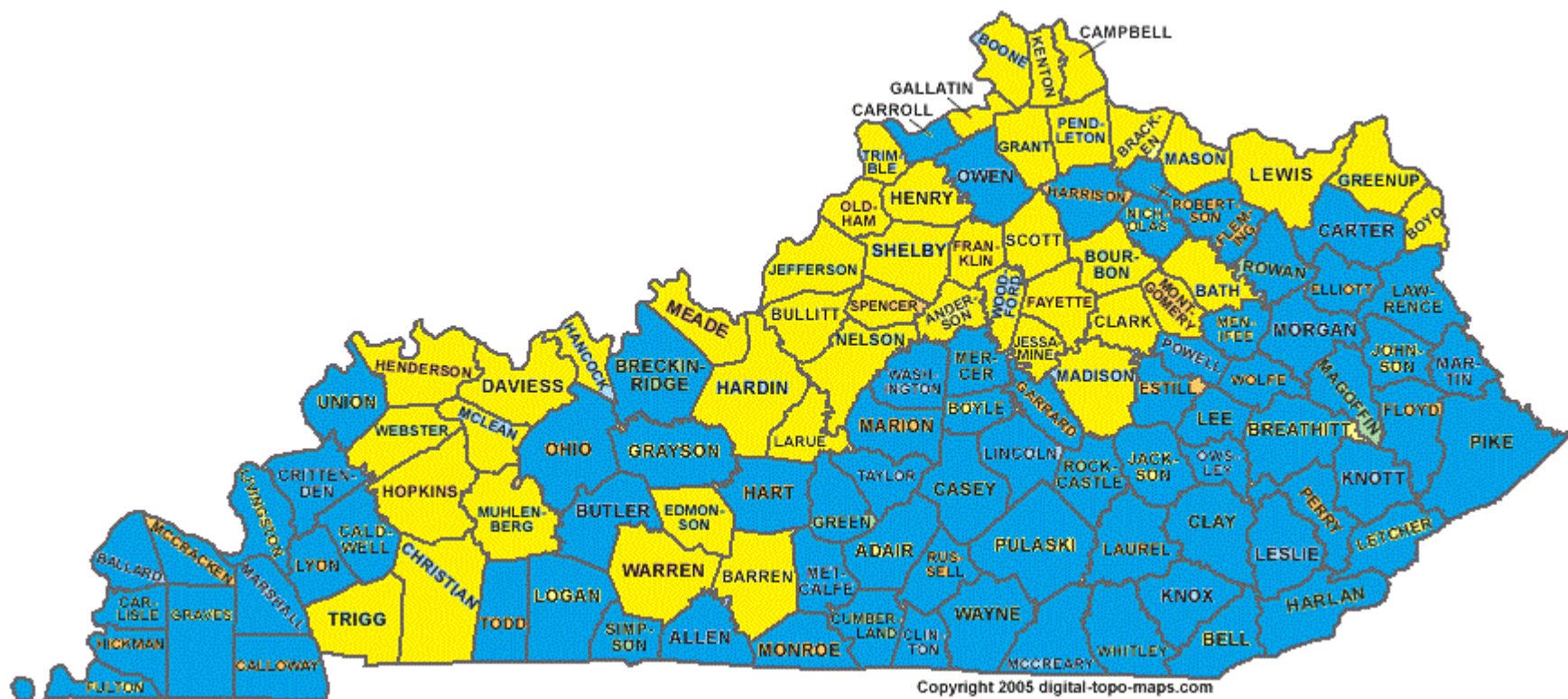
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Kentucky

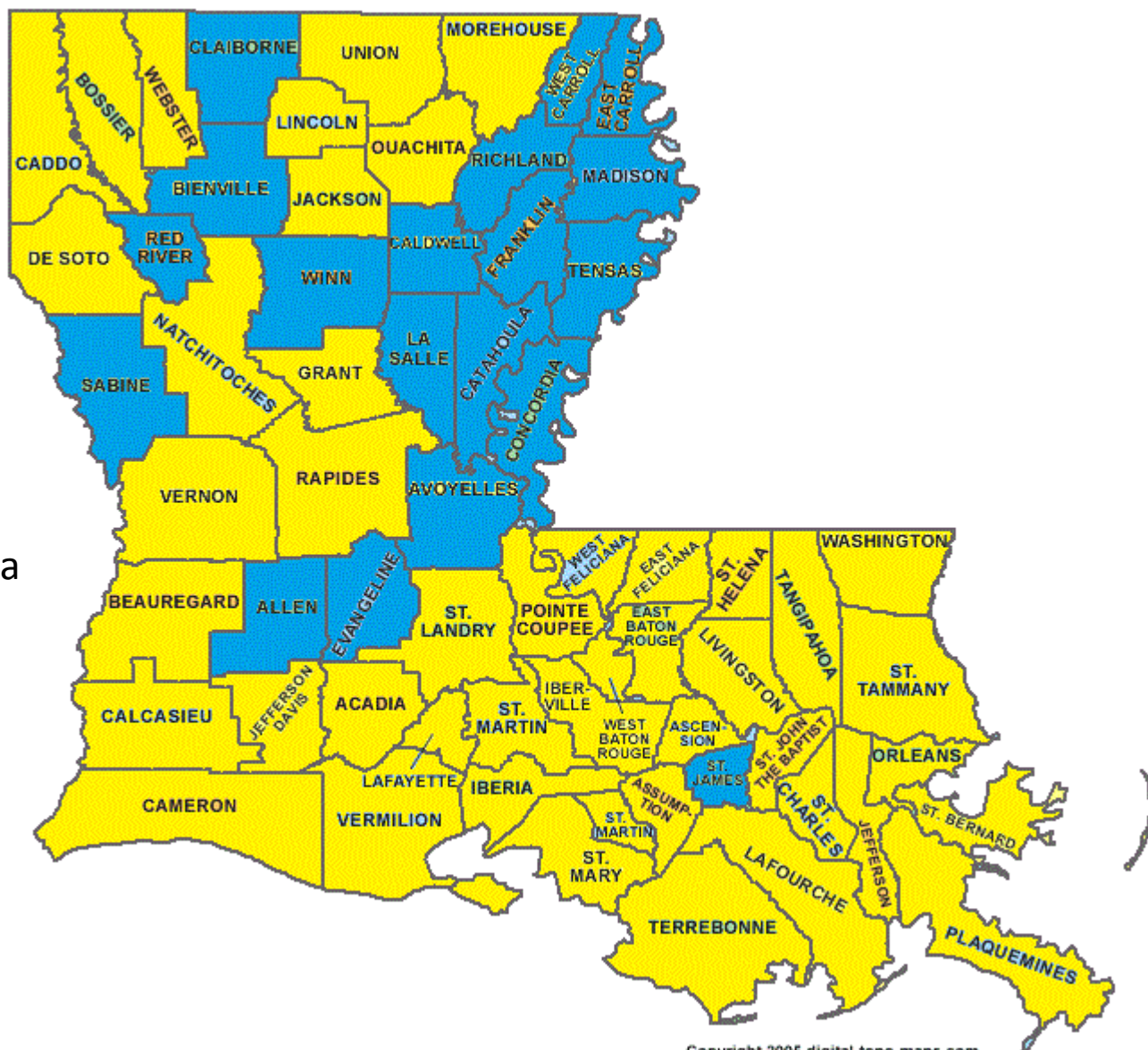
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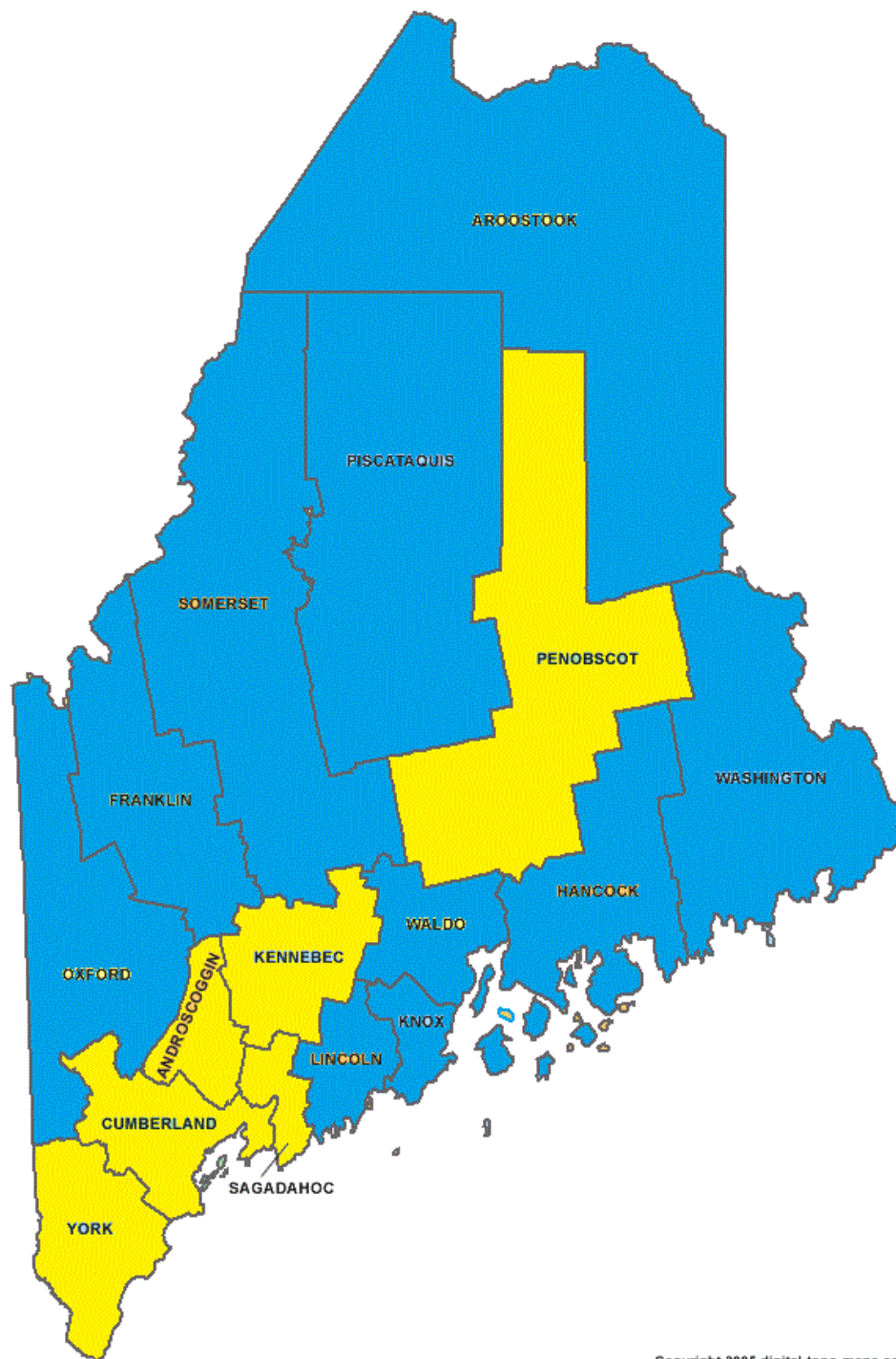
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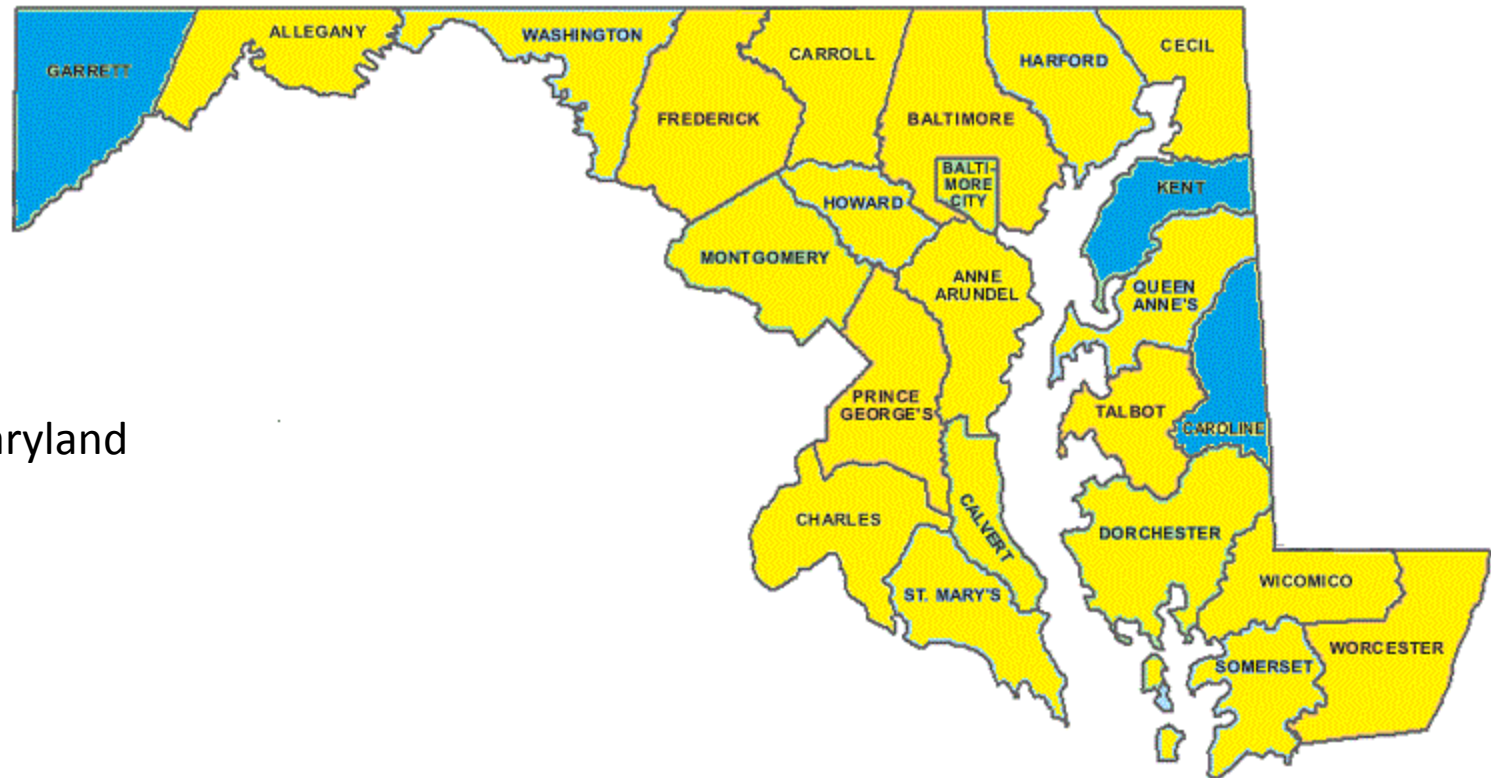




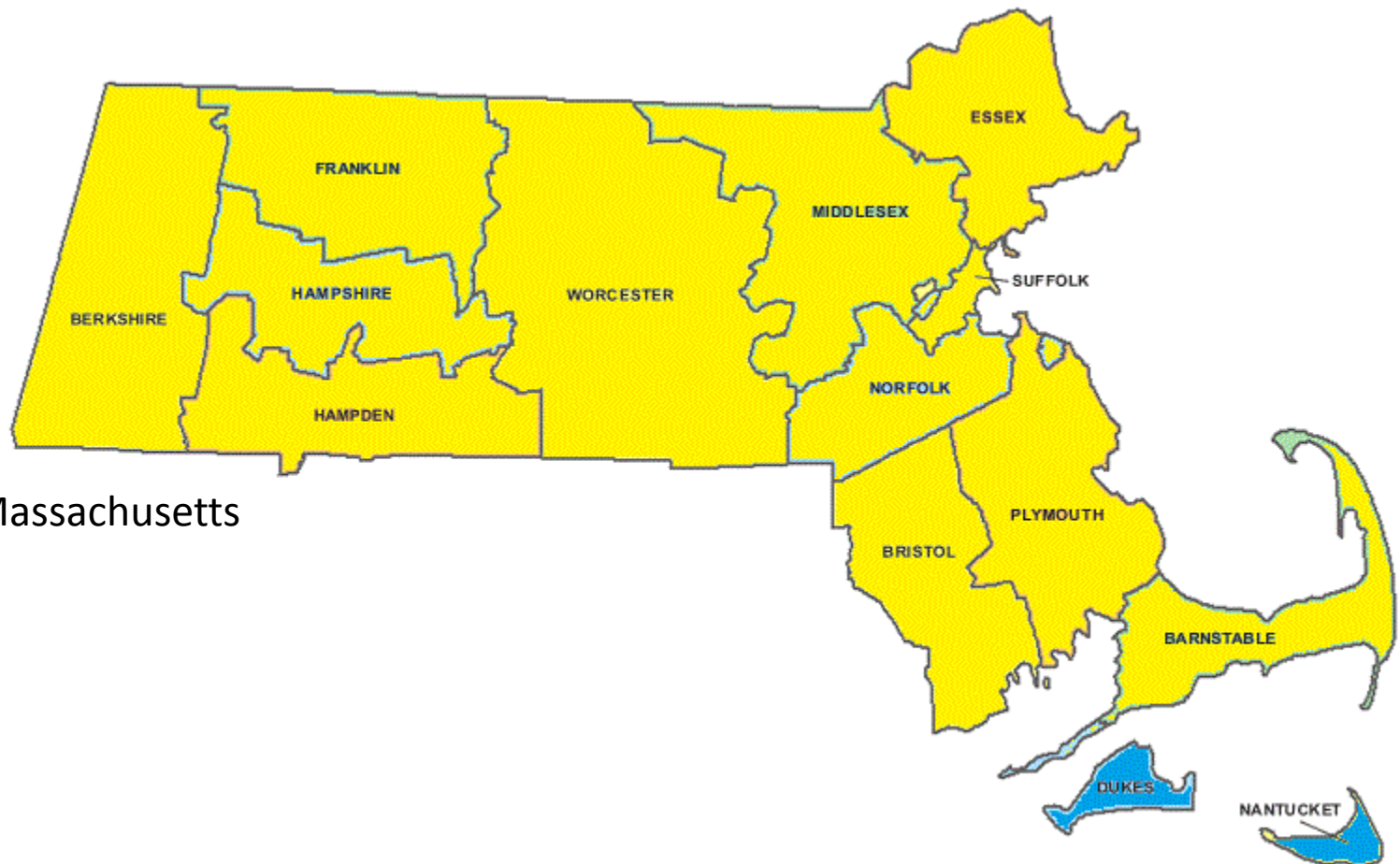
# Maine



# Maryland

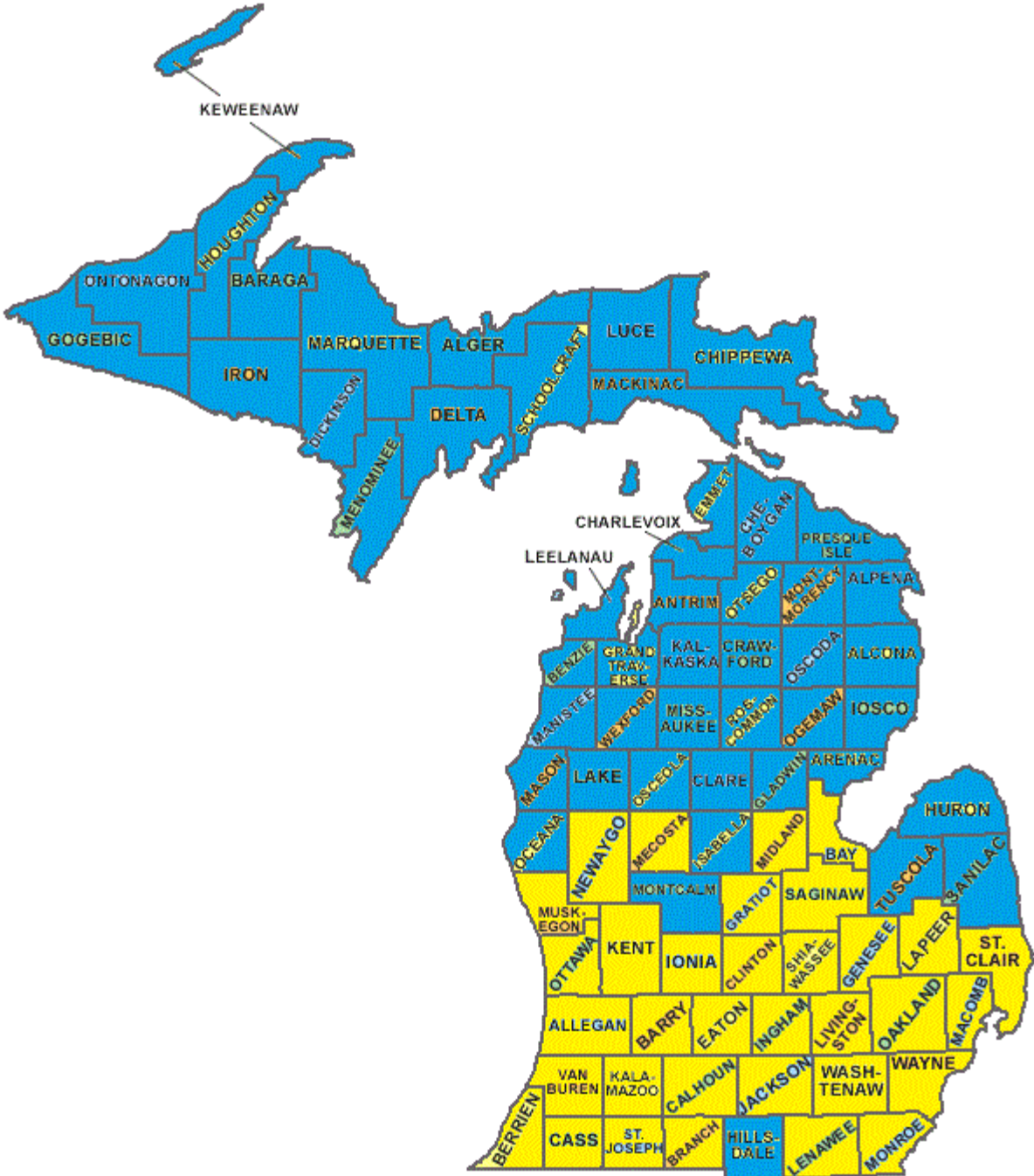


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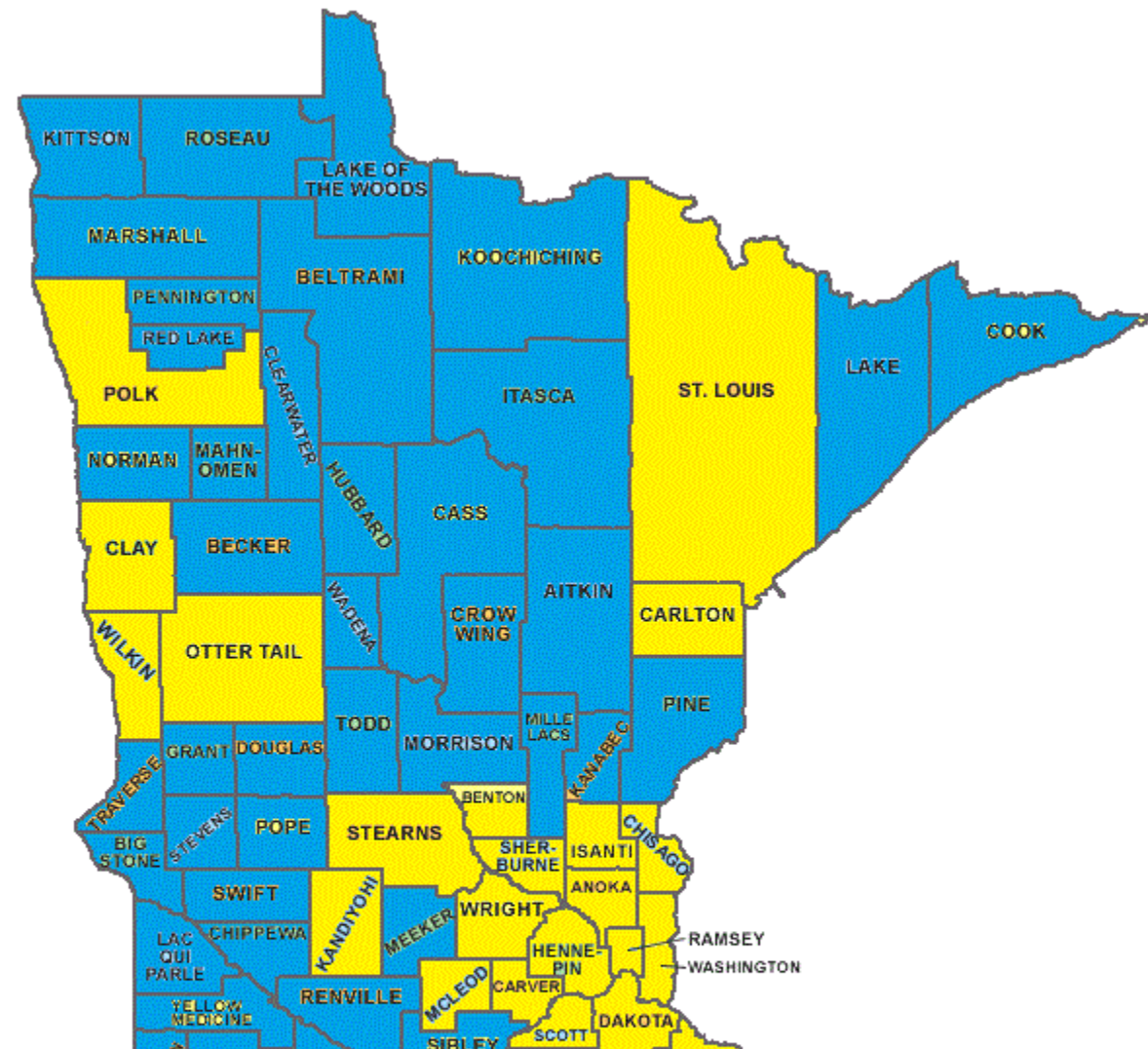
Massachusetts

# Michigan

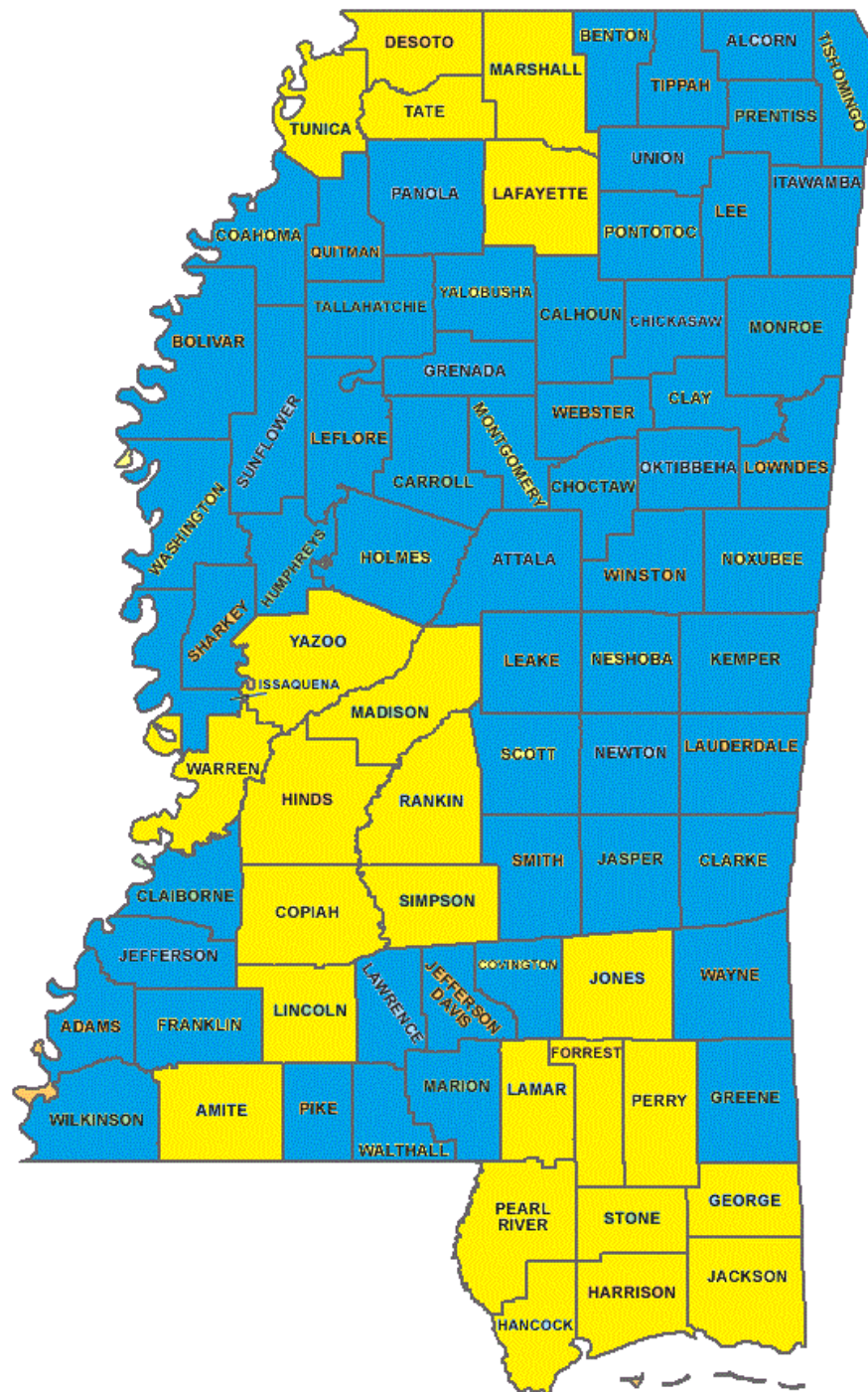




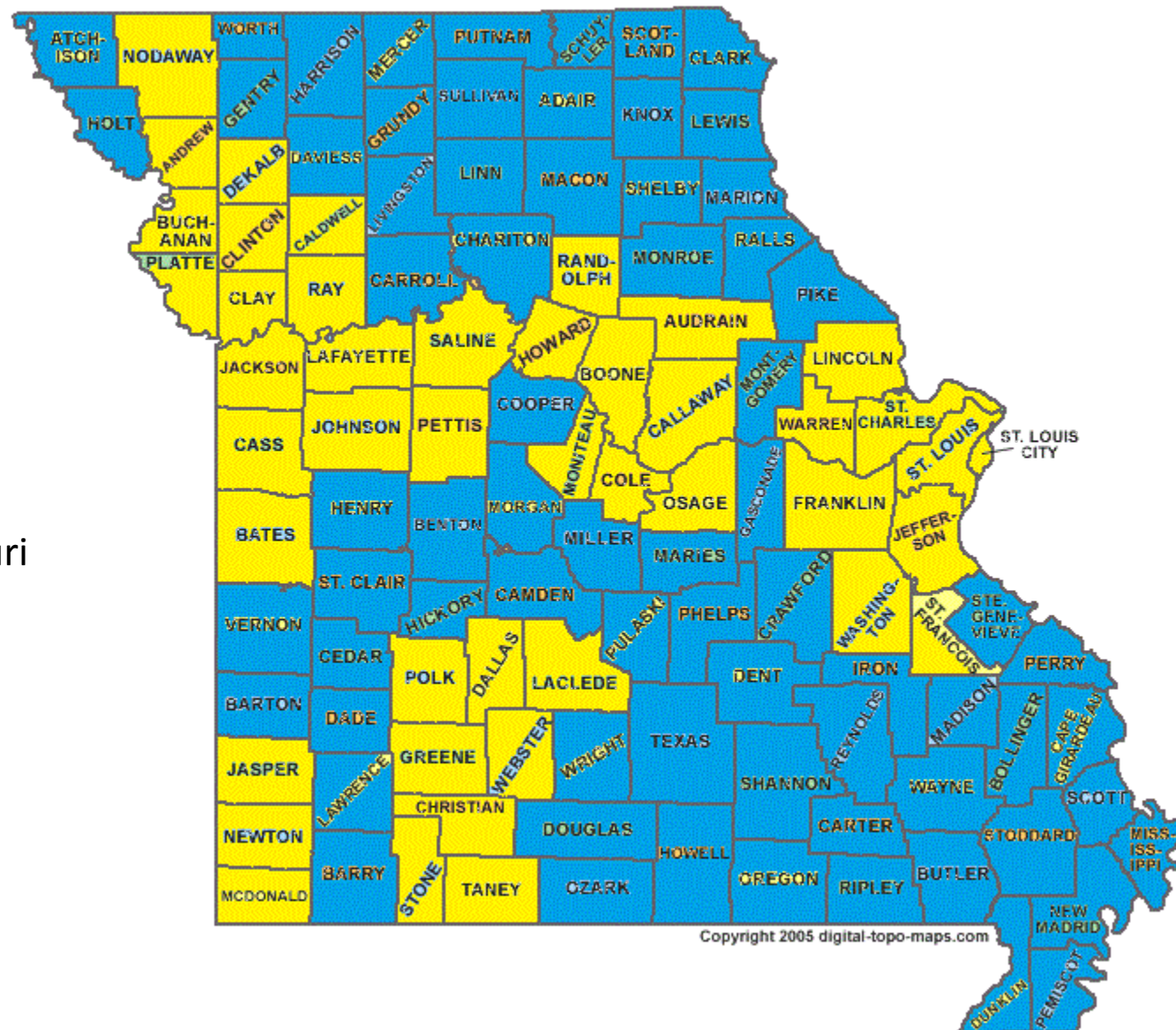
Minnesota



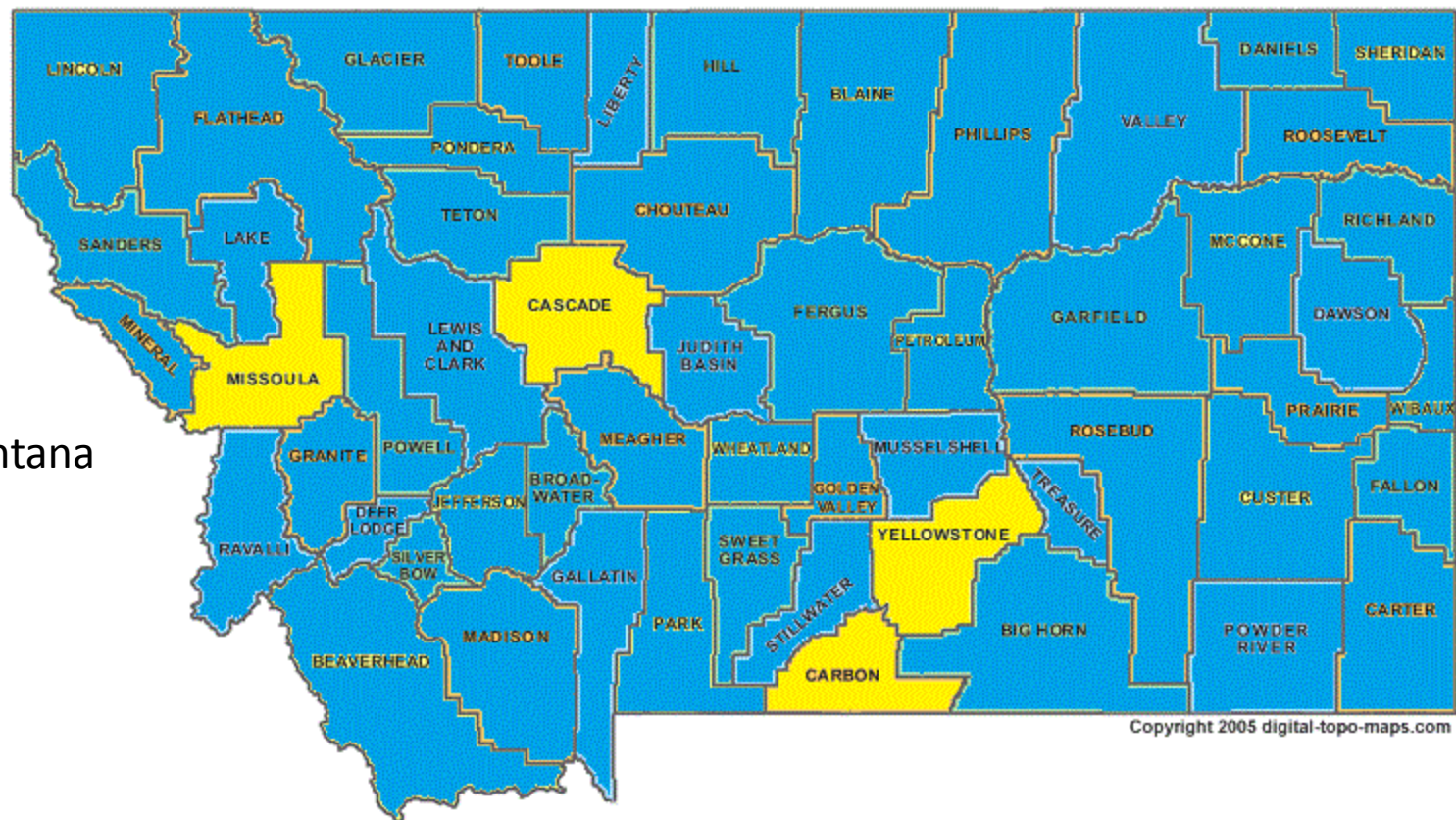
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# Missouri

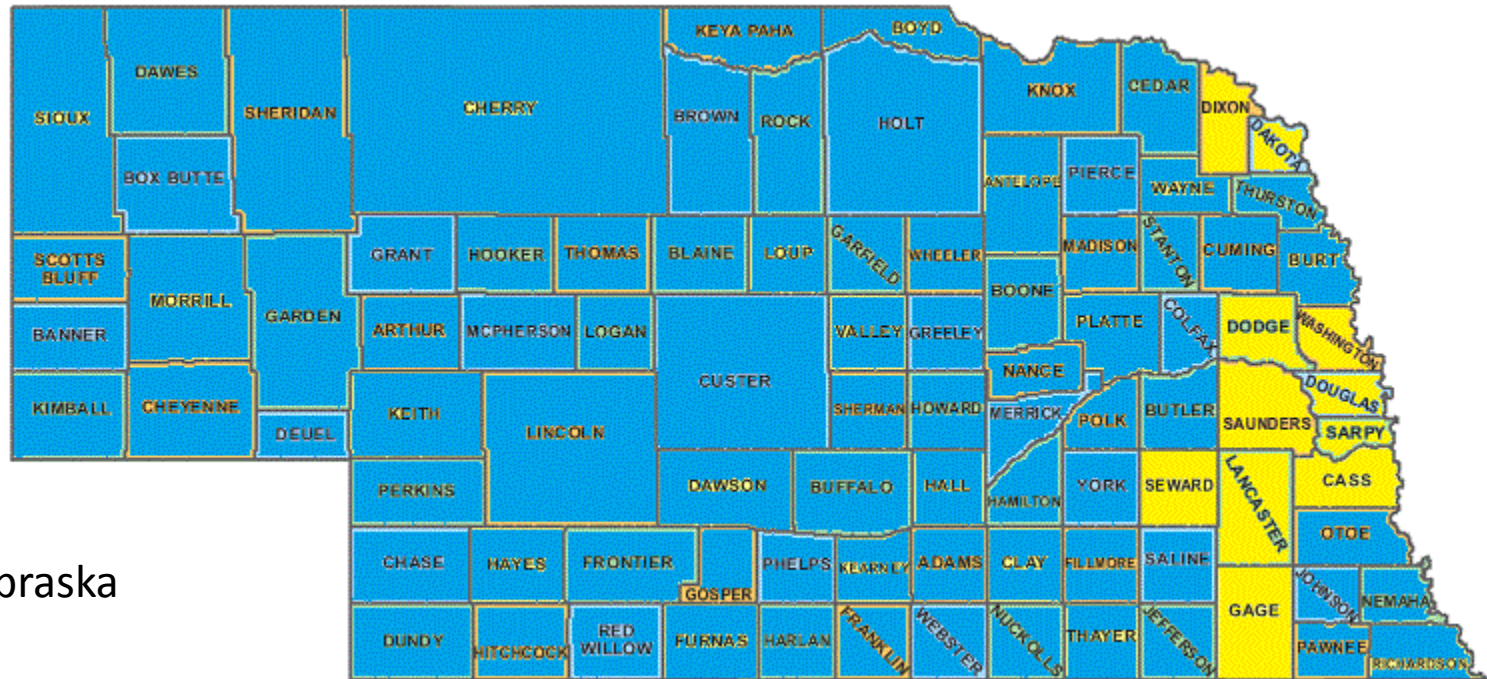


Montana



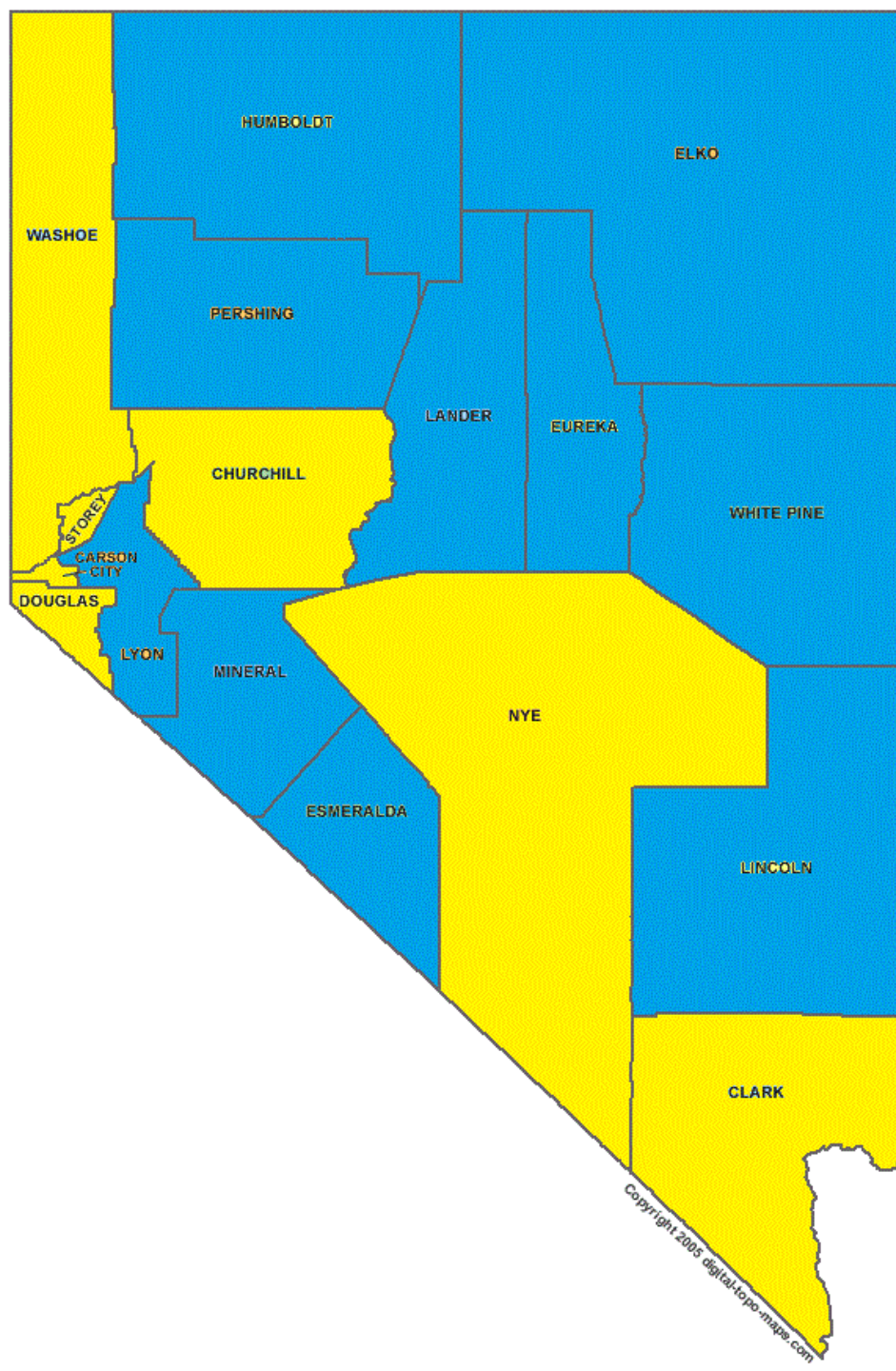
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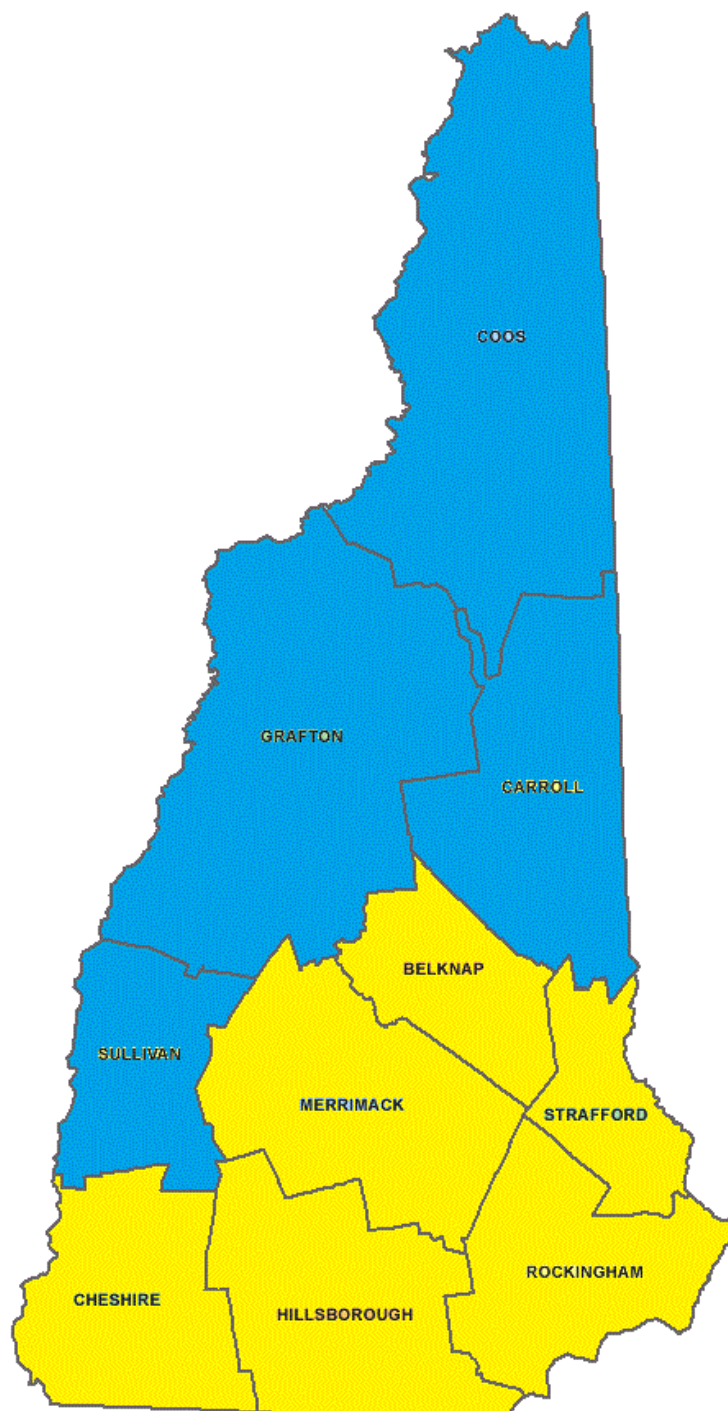
Nebraska

# Nevada

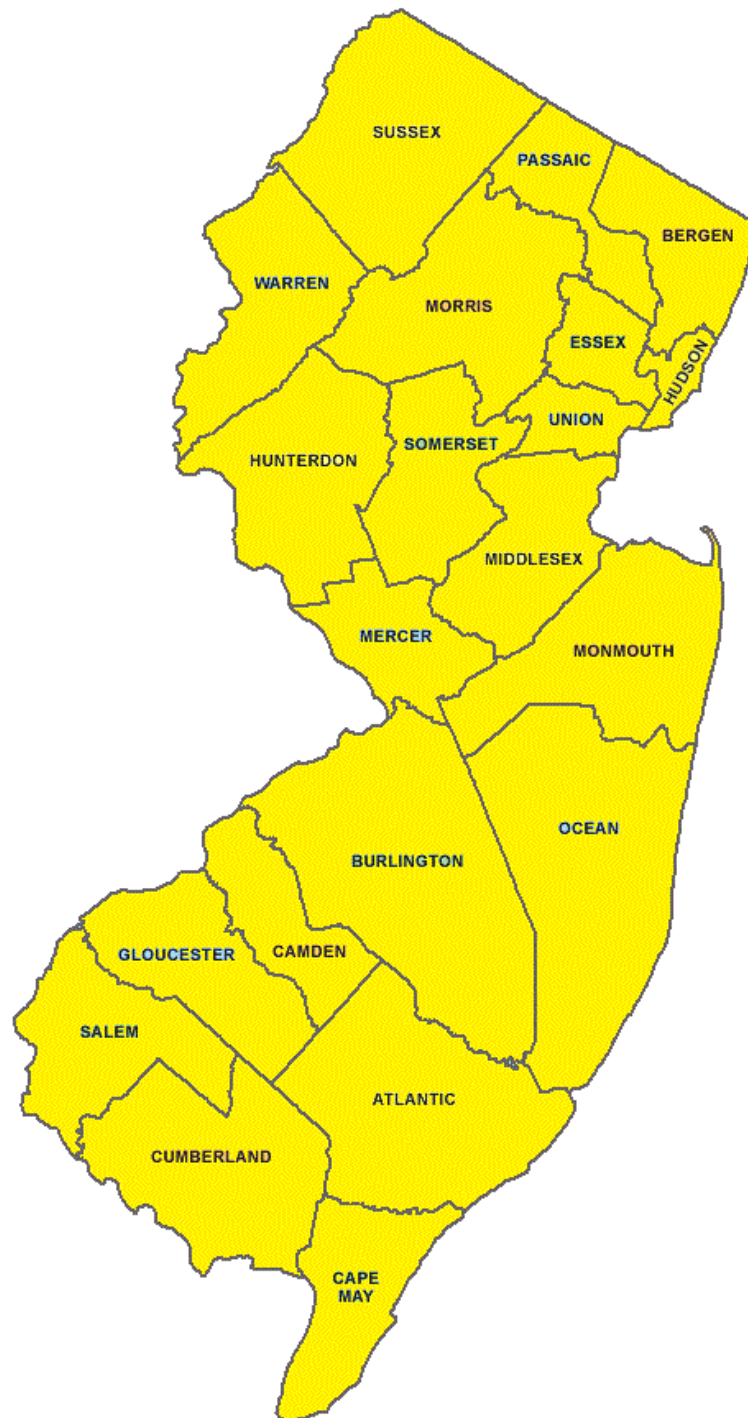




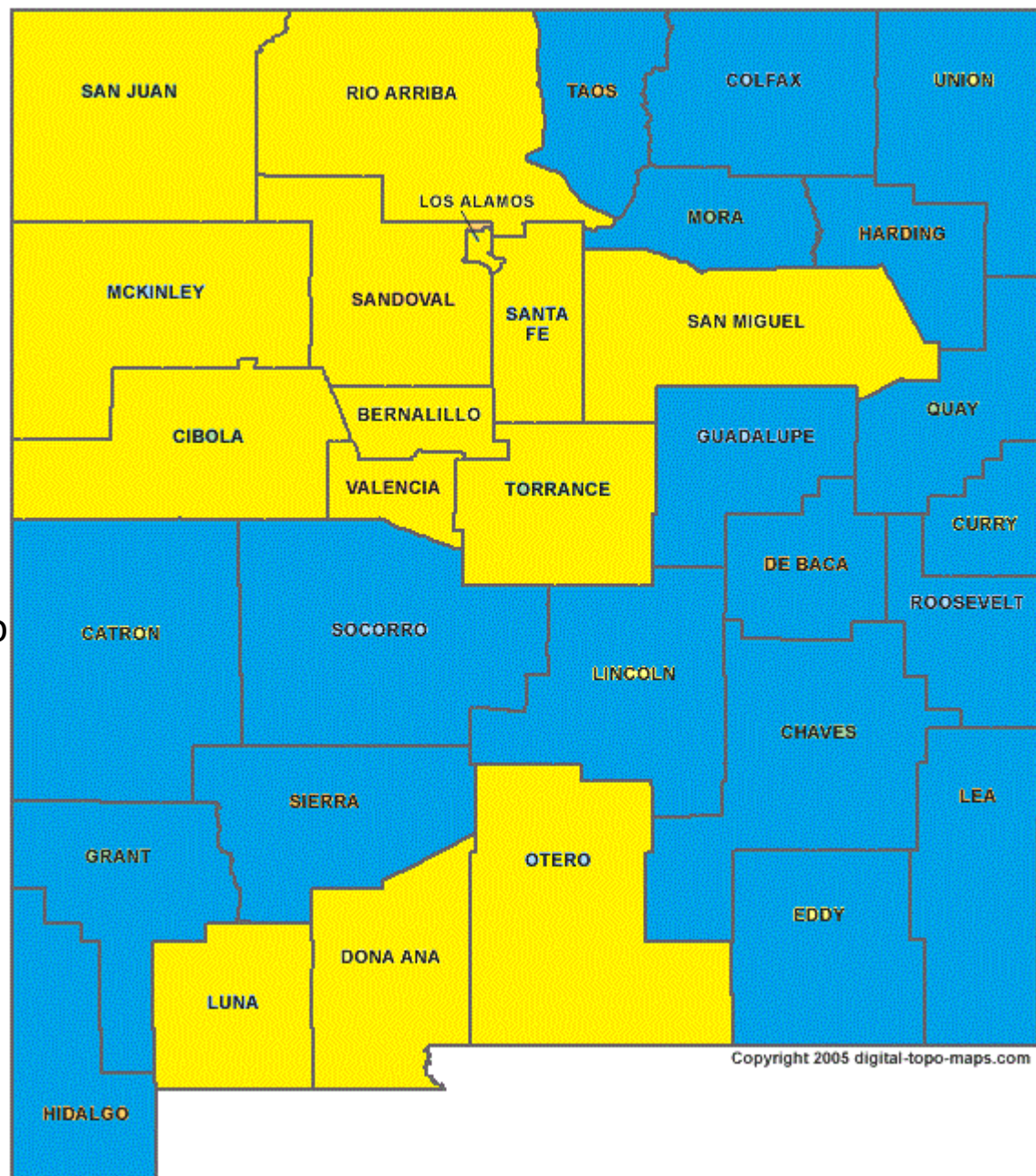
# New Hampshire



# New Jersey



New Mexico



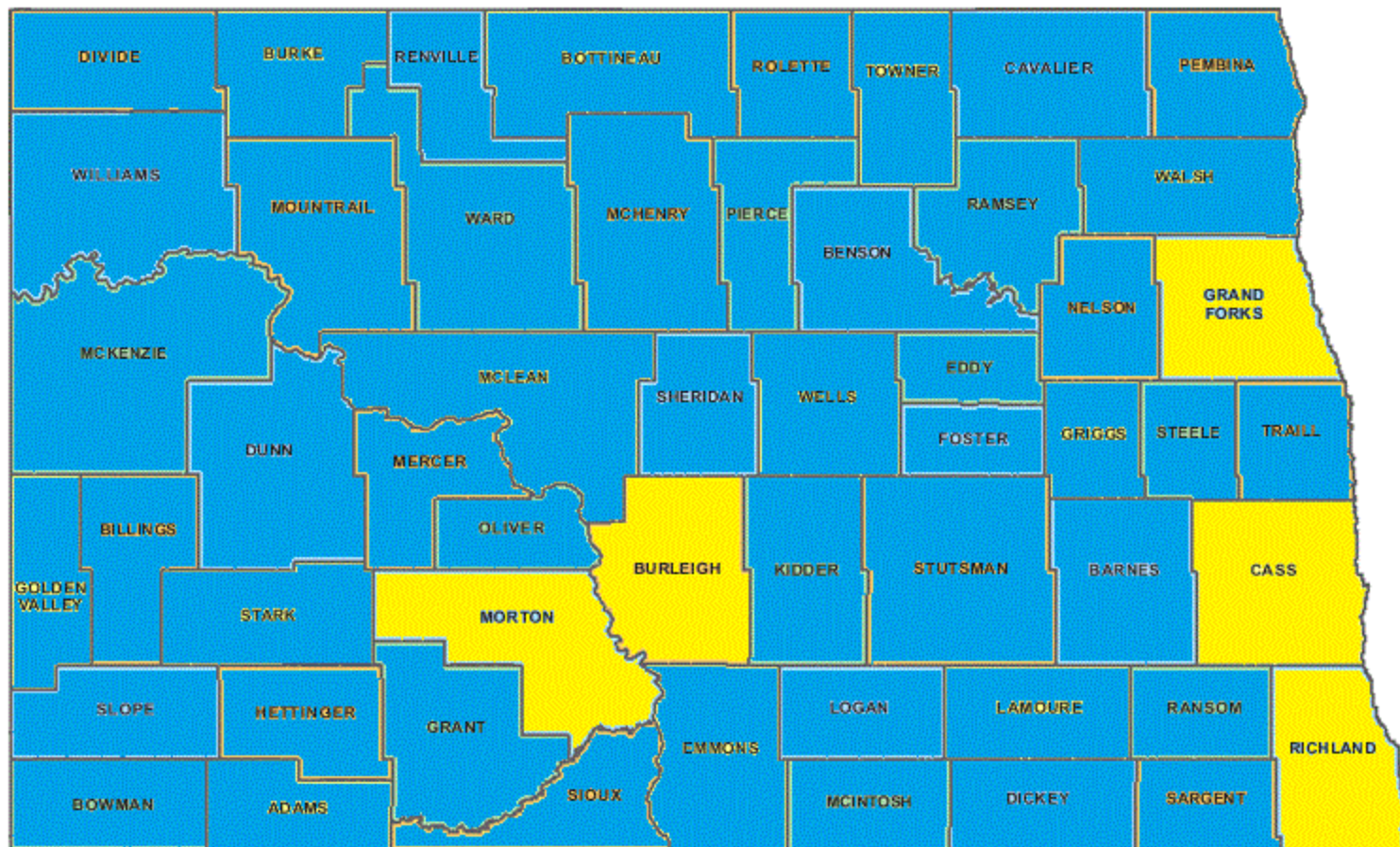
A map of New York State showing its 62 counties. The counties are color-coded: 12 are highlighted in blue, and the remaining 50 are yellow. The blue counties are: St. Lawrence, Franklin, Clinton, Essex, Hamilton, Warren, Lewis, Jefferson, Oswego, Oneida, Madison, Chenango, Otsego, Delaware, Greene, Sullivan, Ulster, and Albany. The yellow counties are: Niagara, Orleans, Monroe, Wayne, Oswego, Onondaga, Hamilton, Warren, Lewis, Jefferson, Oswego, Oneida, Madison, Chenango, Otsego, Delaware, Greene, Sullivan, Ulster, Albany, Rensselaer, Columbia, Dutchess, Putnam, Westchester, Rockland, Bronx, New York, Queens, Kings, Richmond, Nassau, Suffolk, Chautauque, Cattaraugus, Allegany, Steuben, Schuyler, Tompkins, Cortland, Broome, Tioga, Chemung, Seneca, Yates, Livingston, Ontario, Cayuga, Schenectady, Saratoga, Montgomery, Fulton, Herkimer, Schoharie, and Washington.



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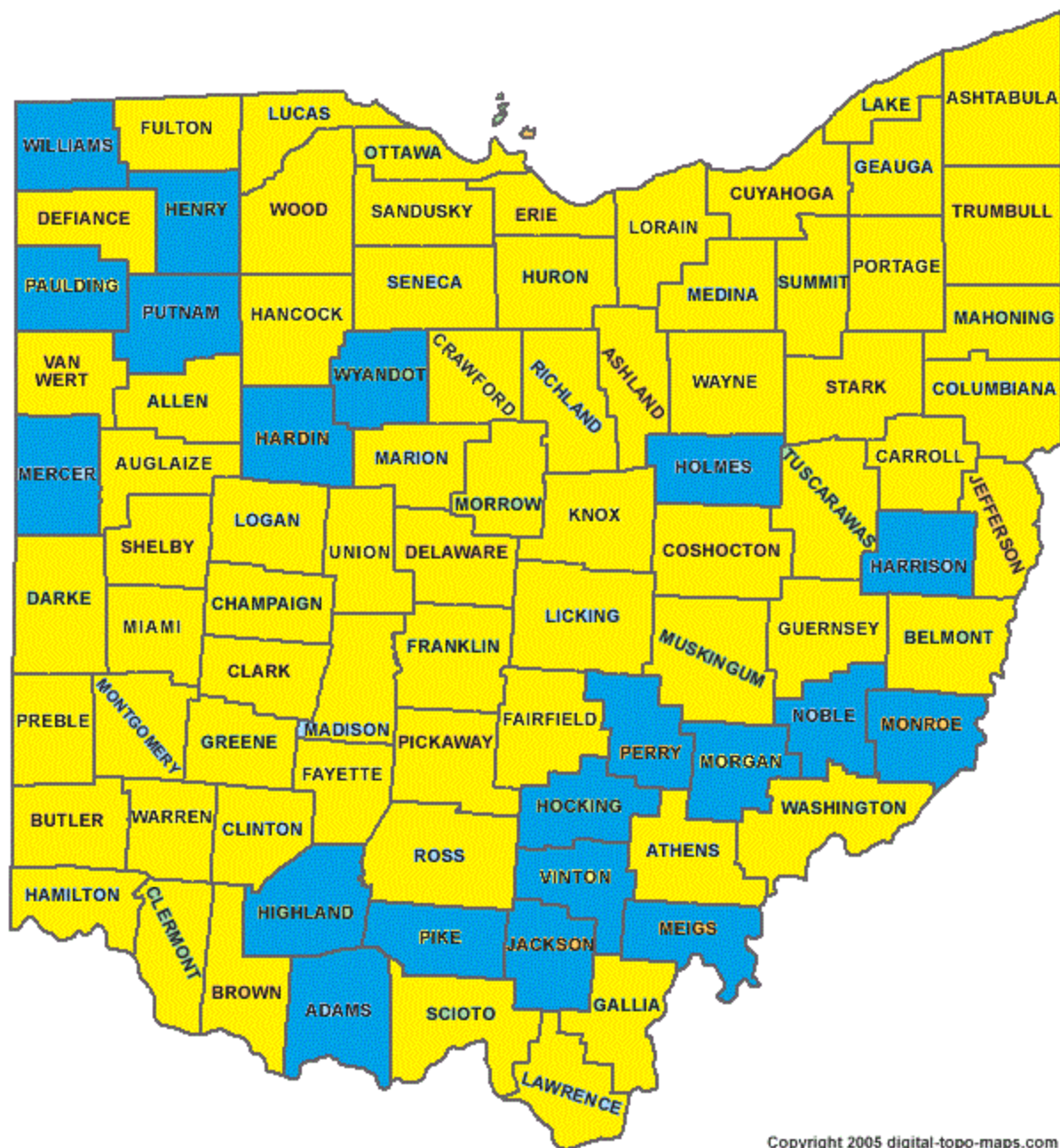
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# North Dakota

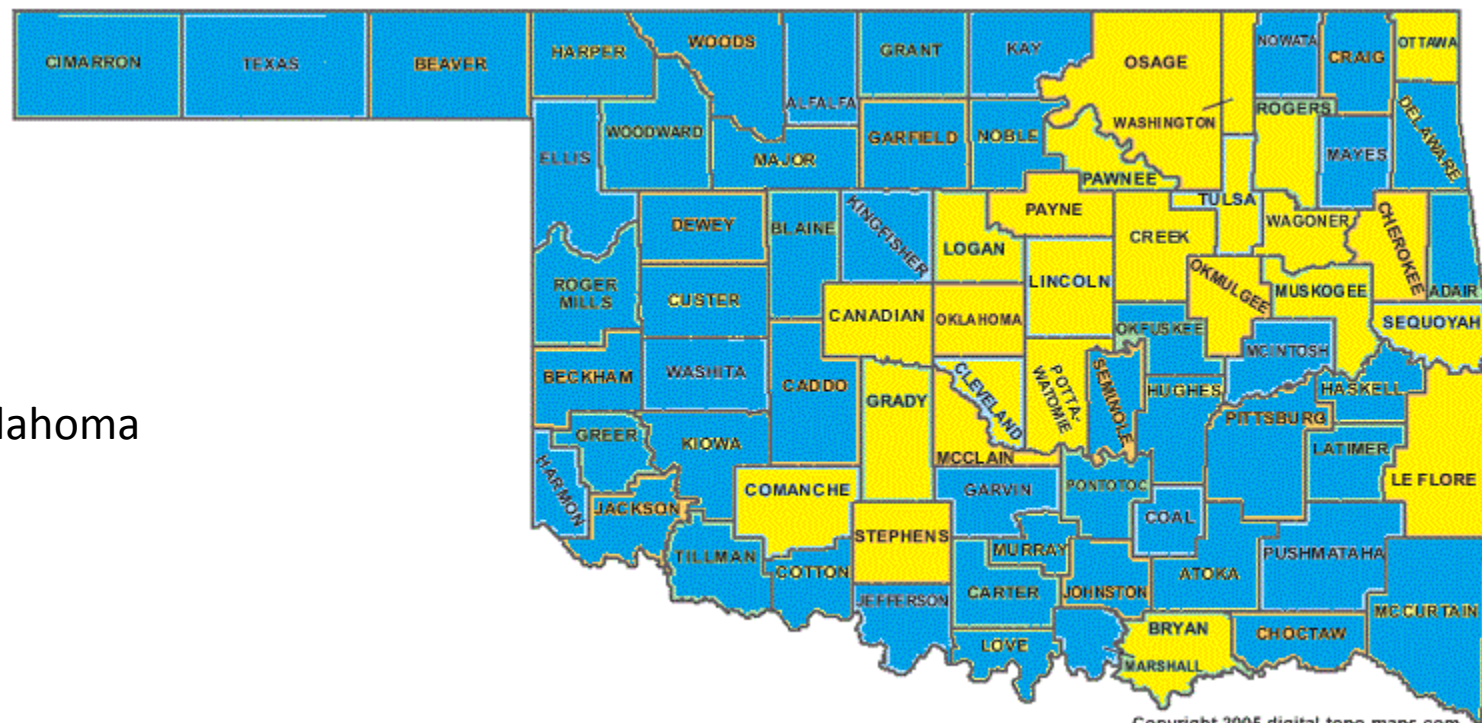




Ohio

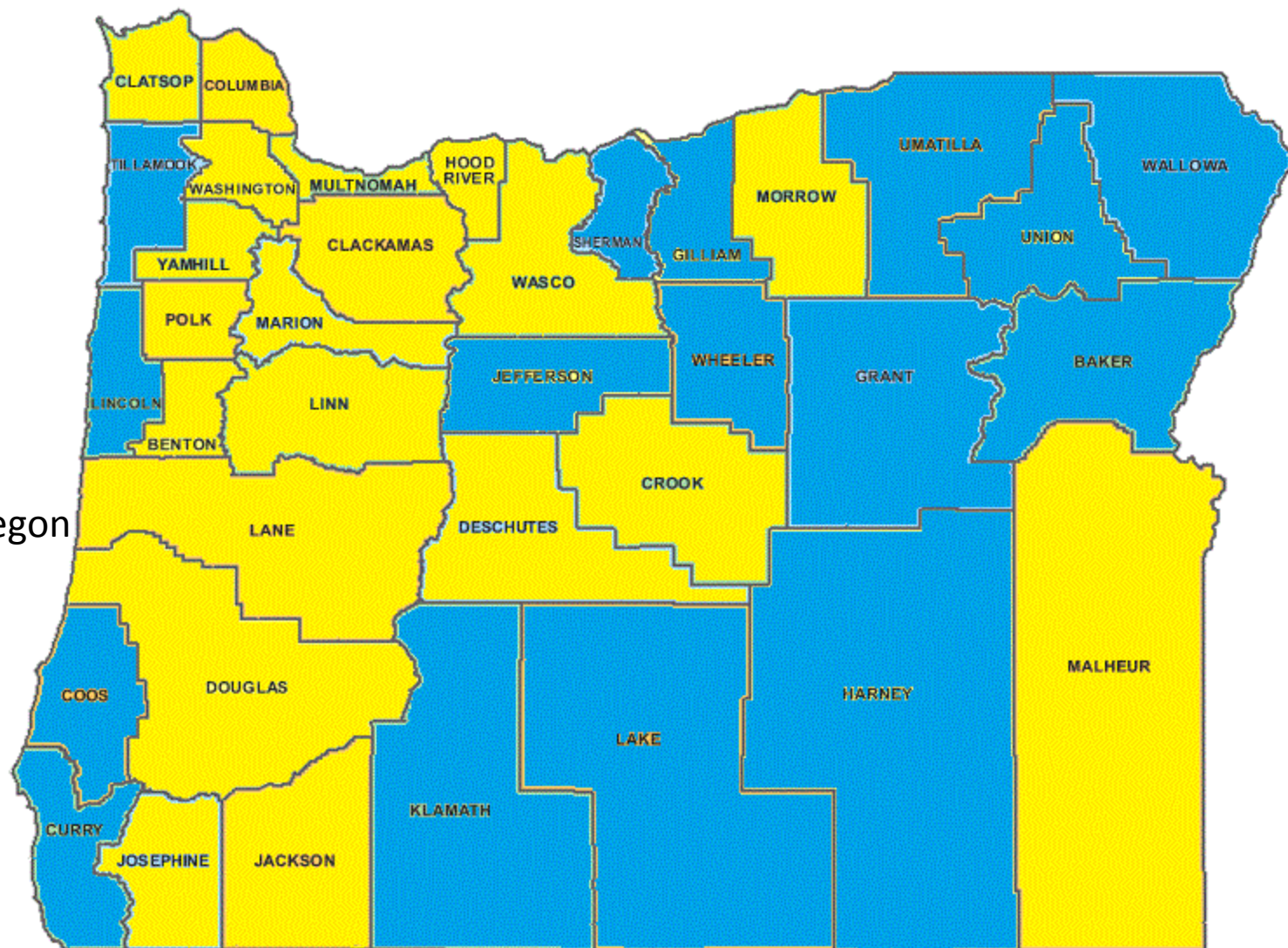


Oklahoma

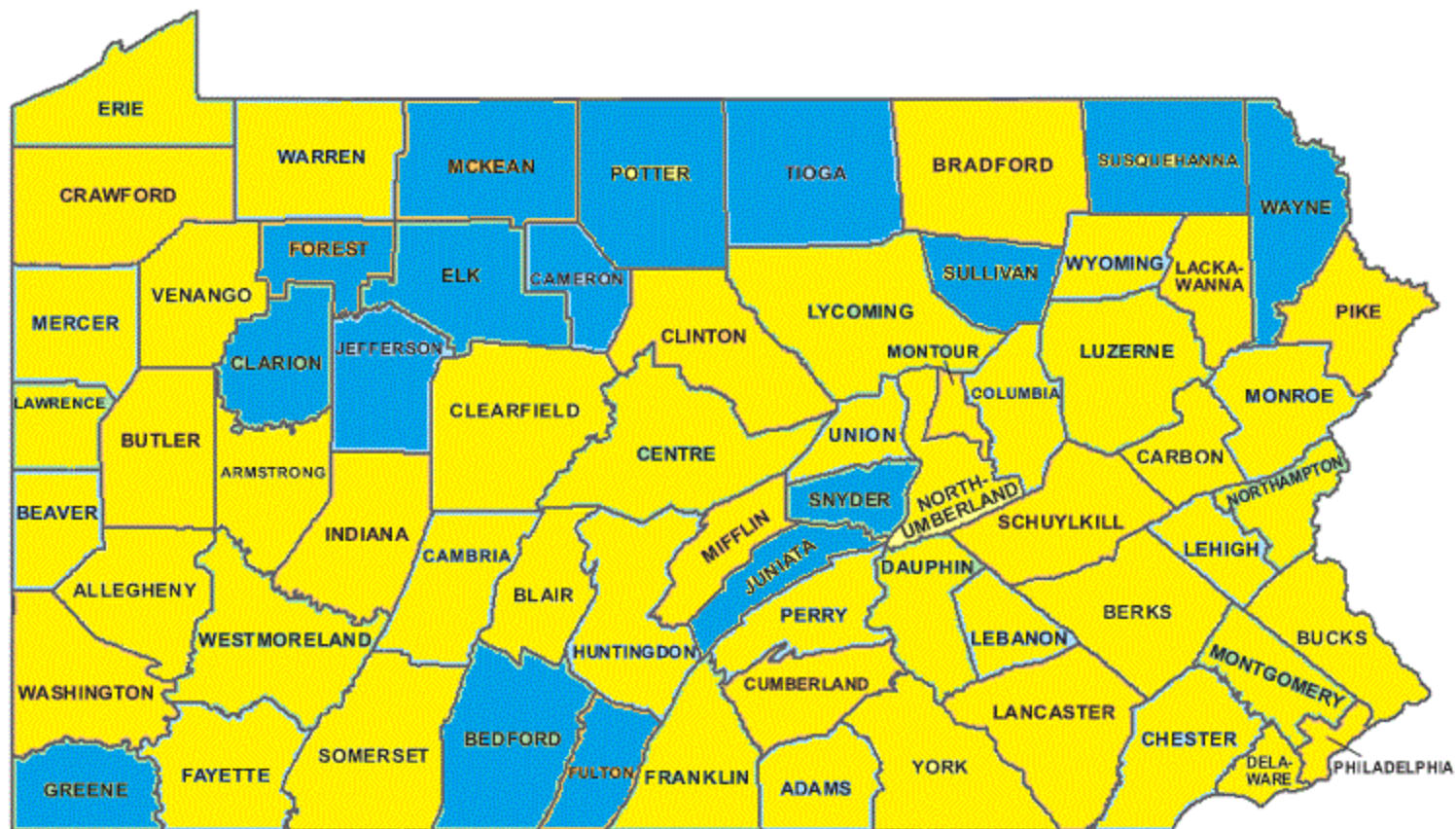


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Oregon

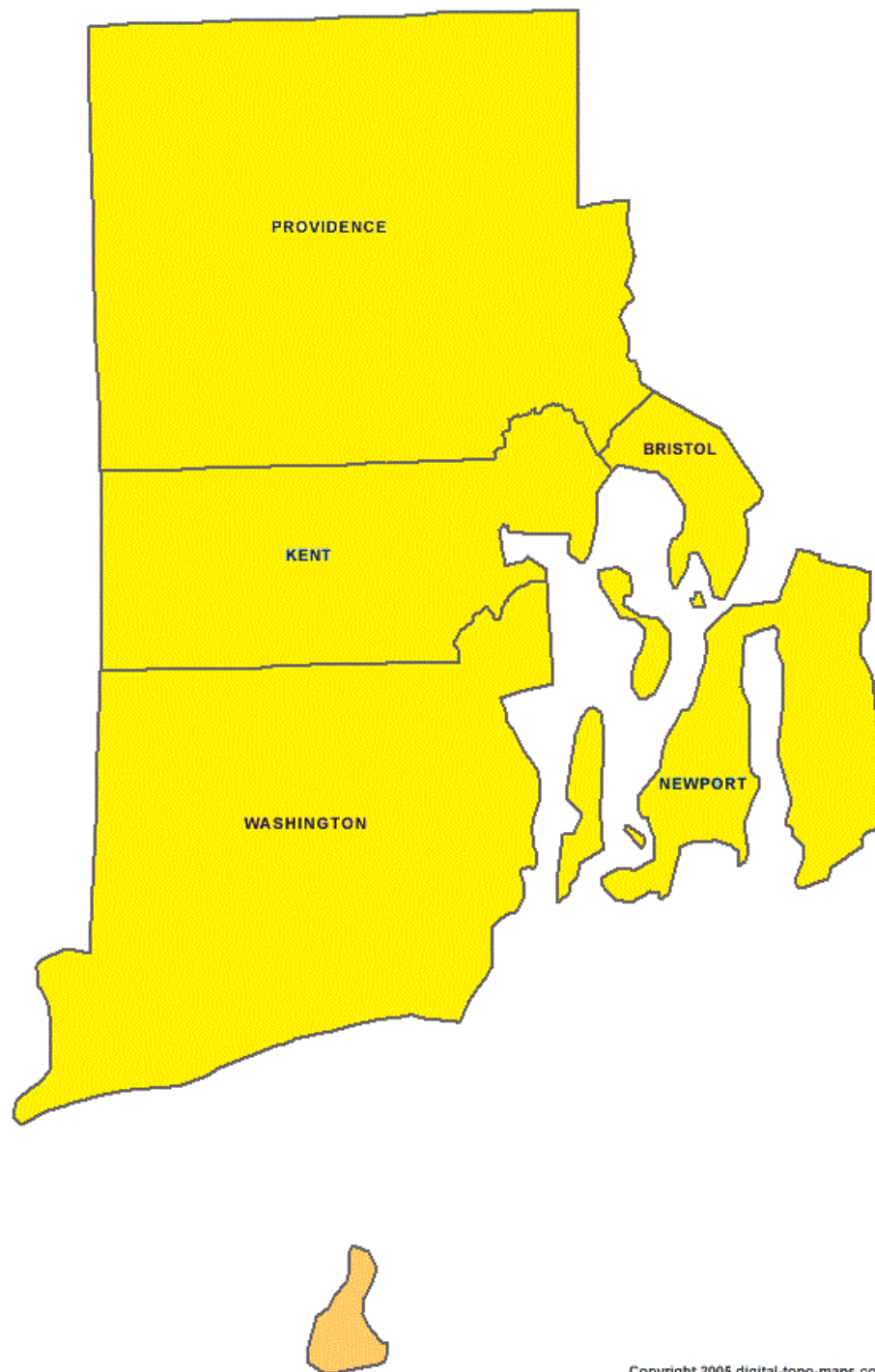


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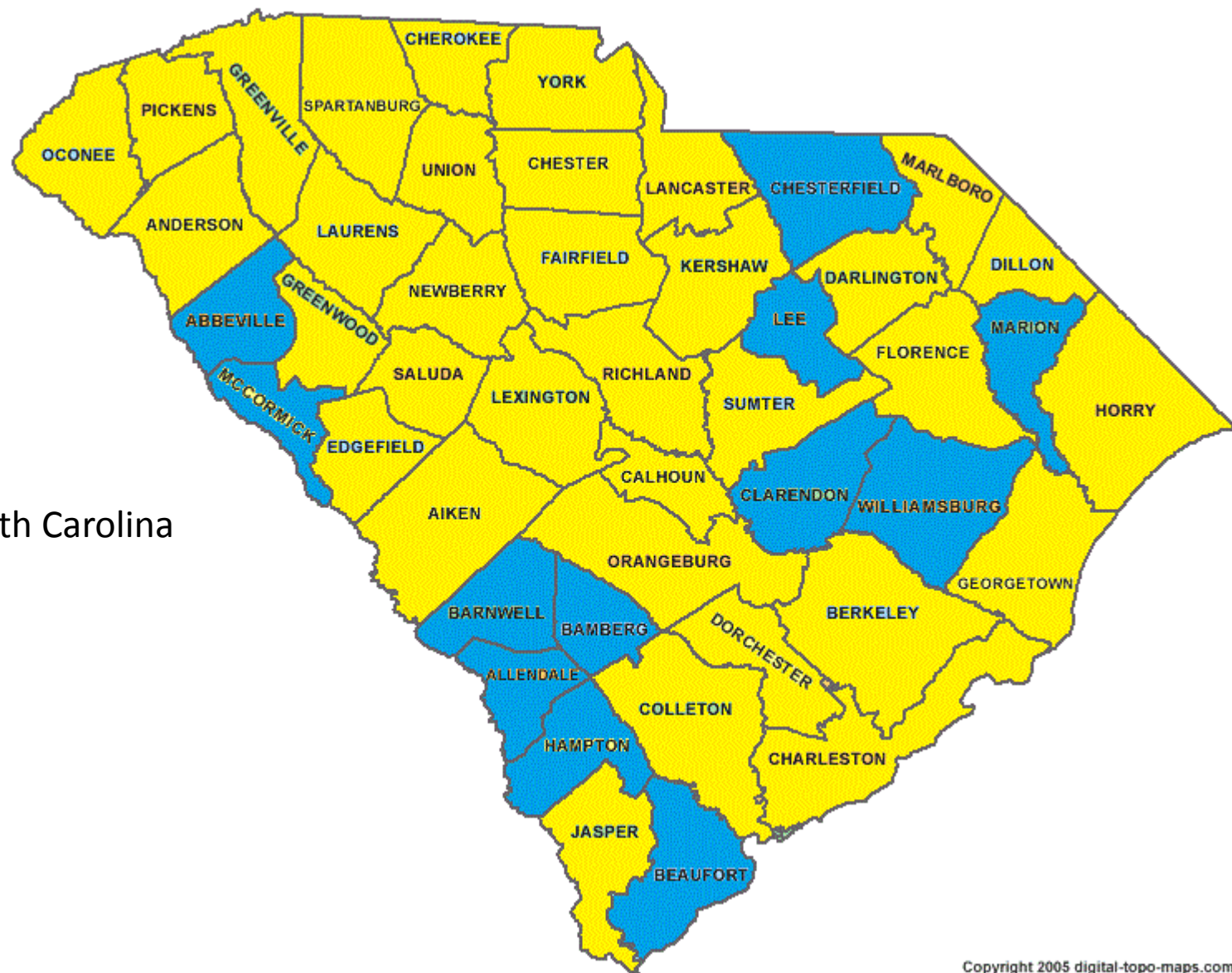
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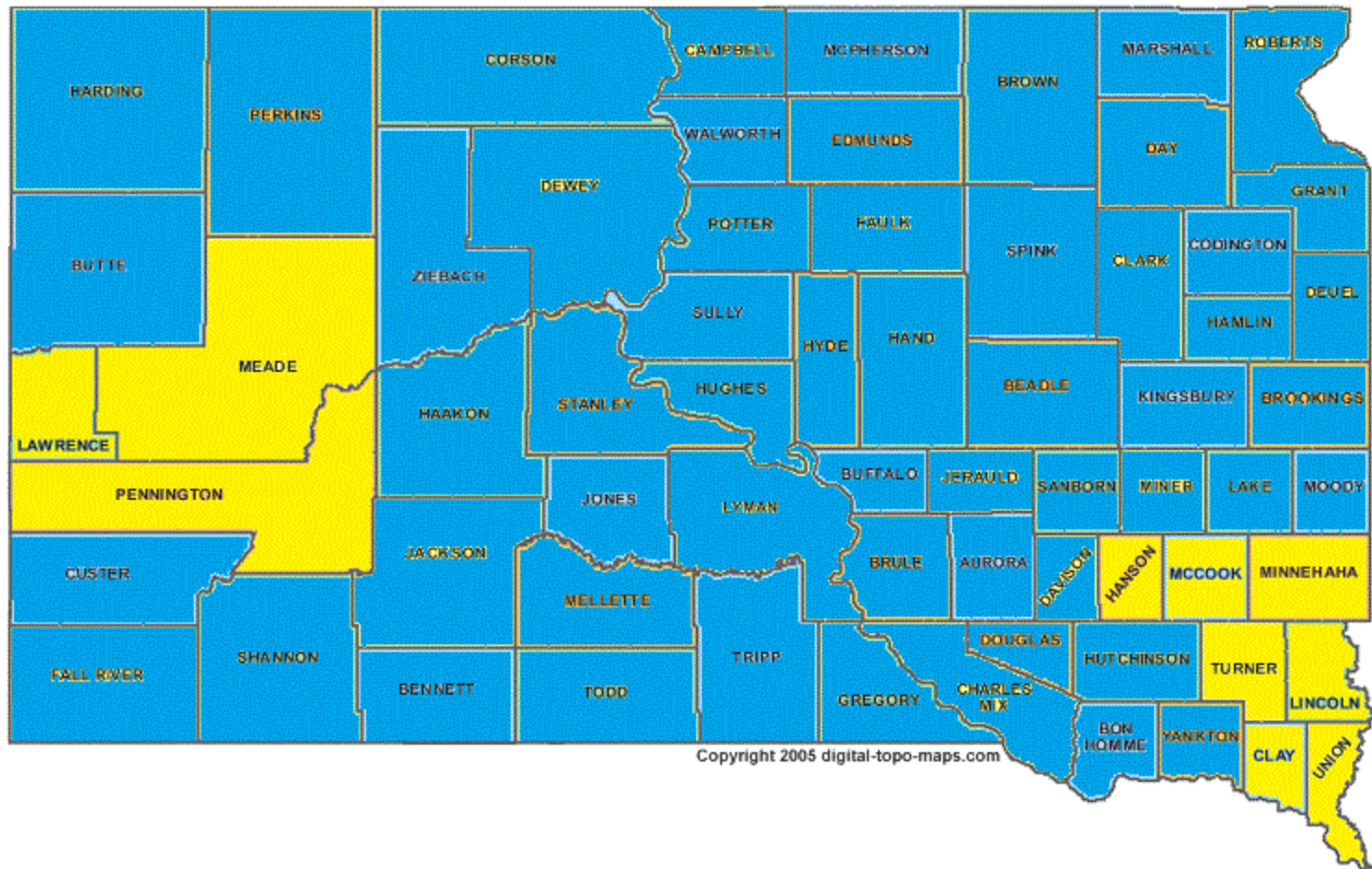


## South Carolina

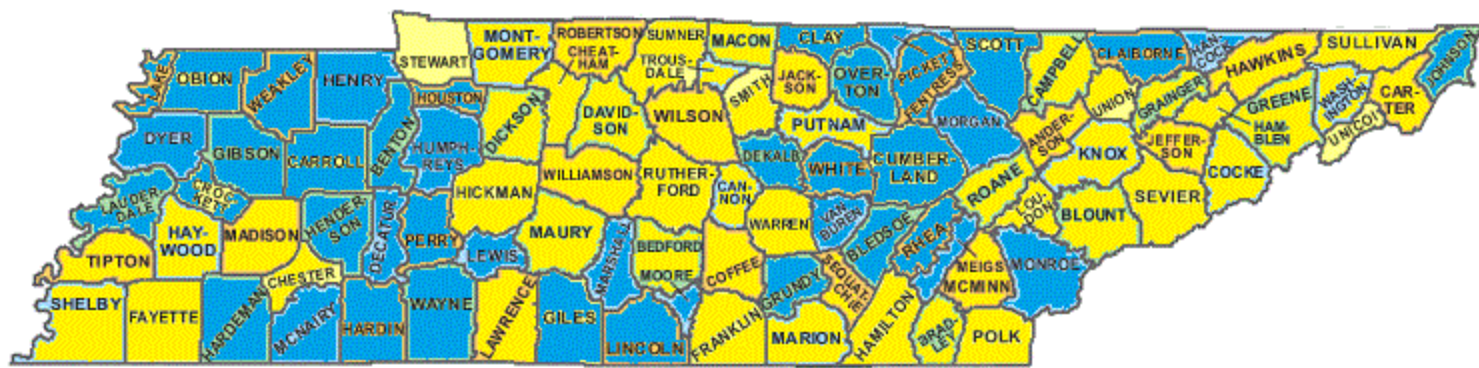




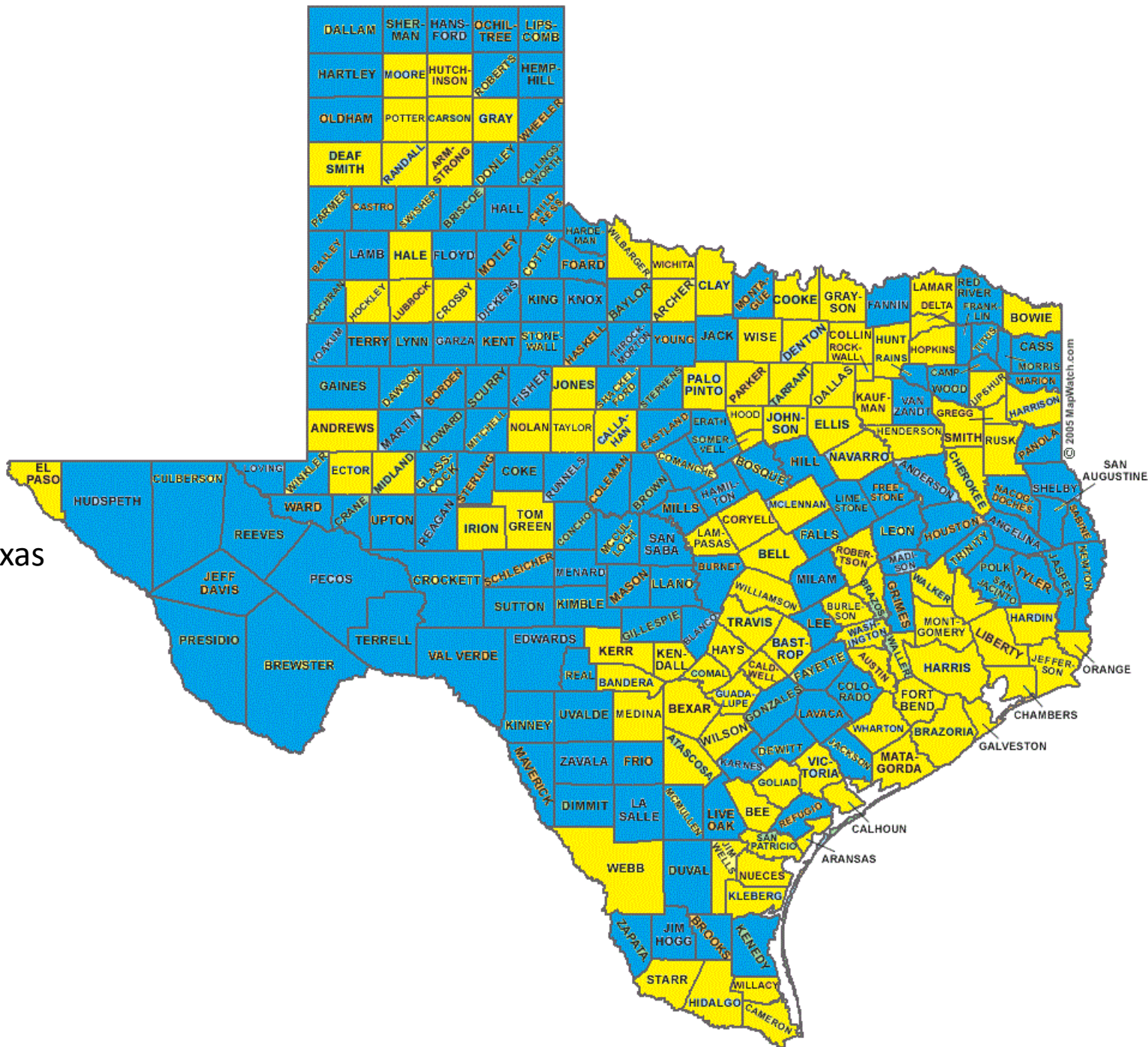
# South Dakota



Tennessee

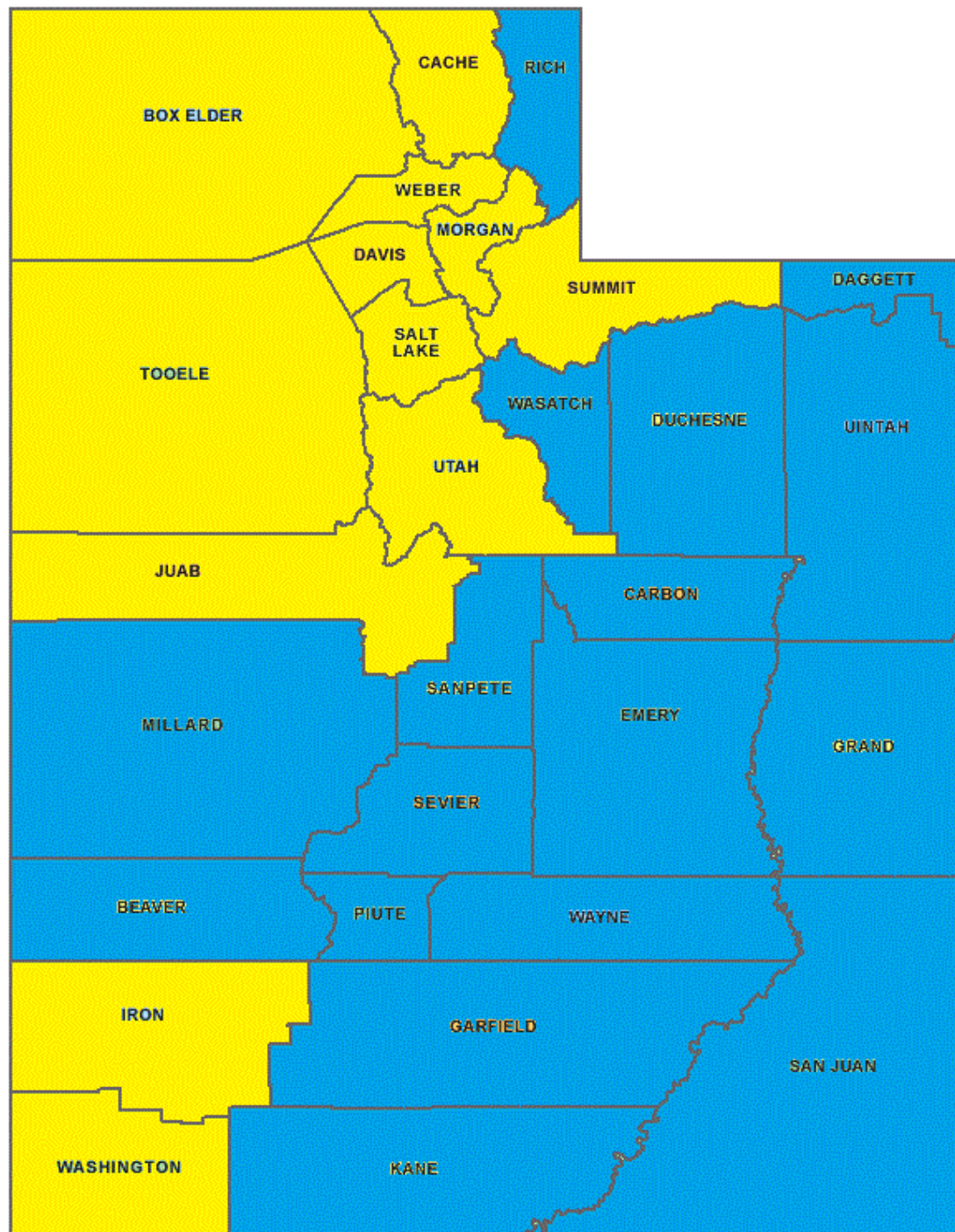


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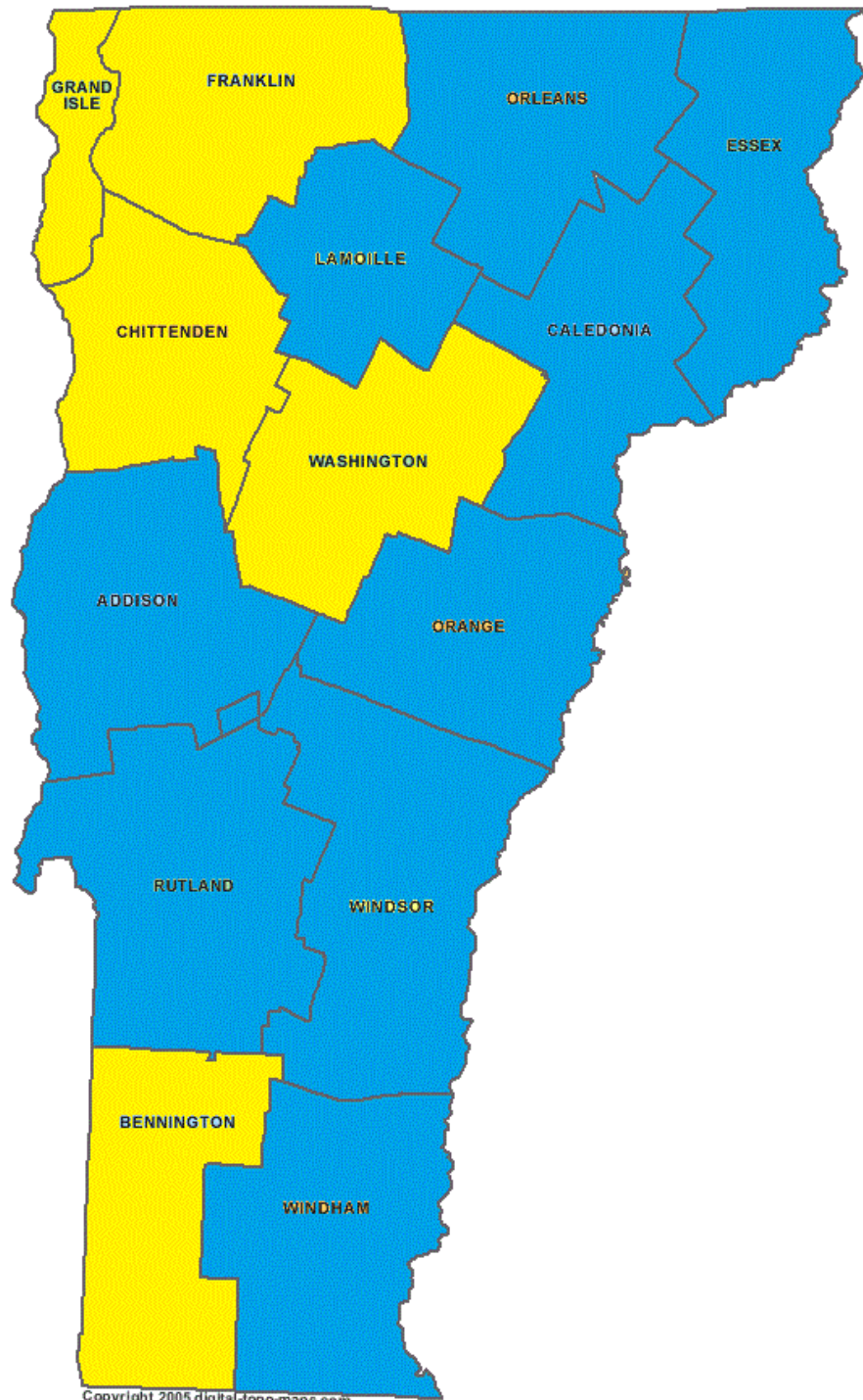




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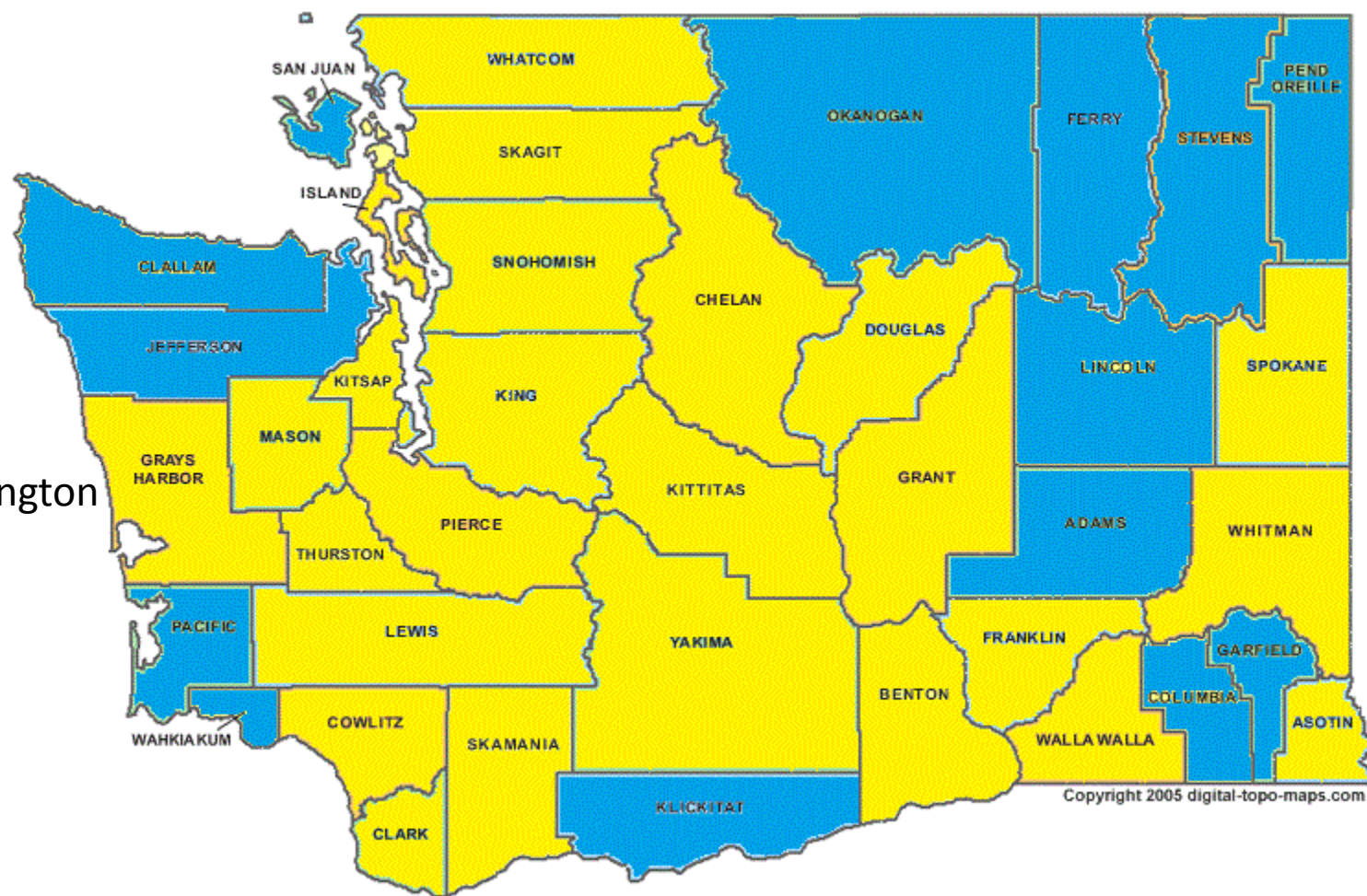
Vermont



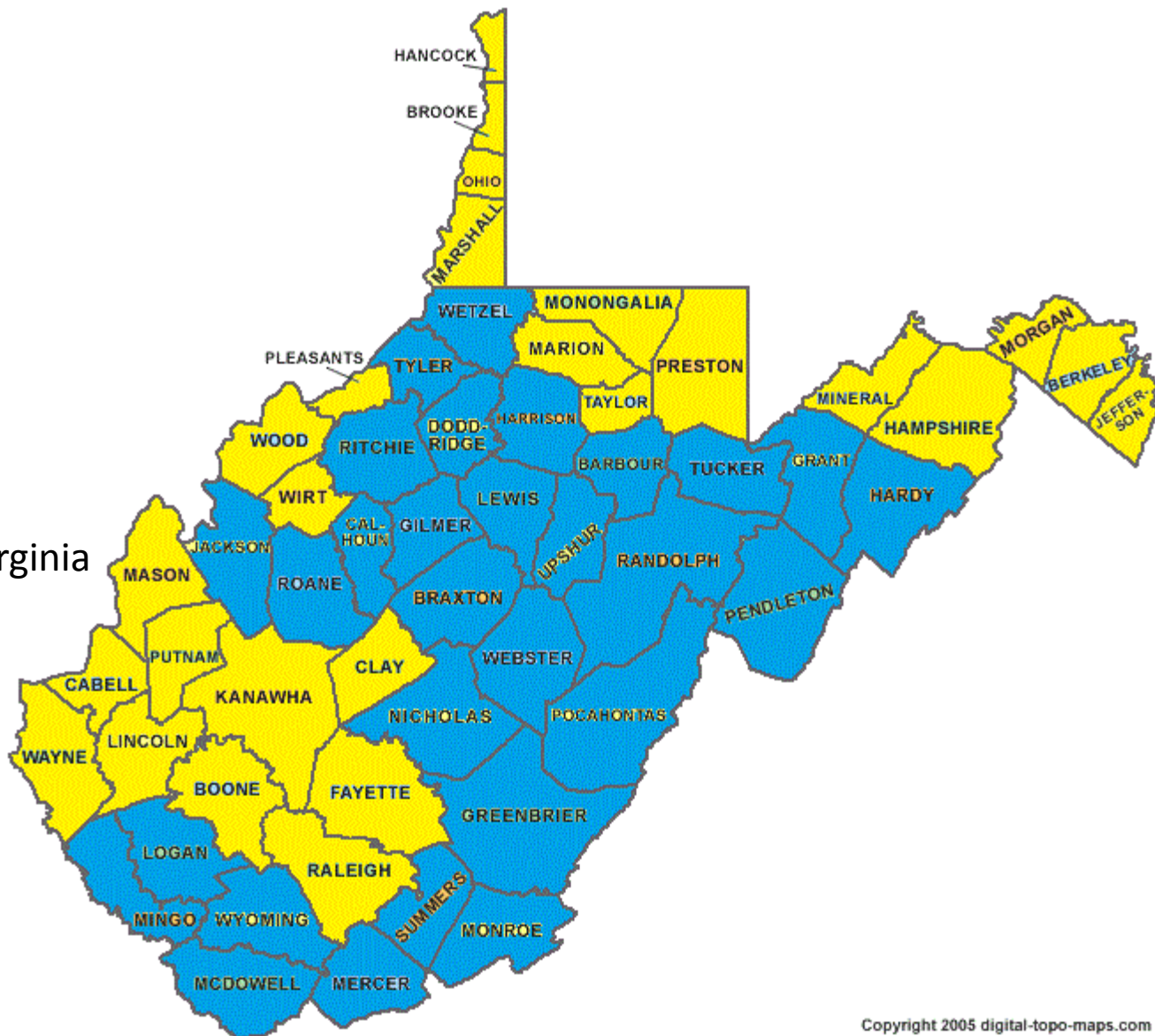
**Virginia: To Be Provided**



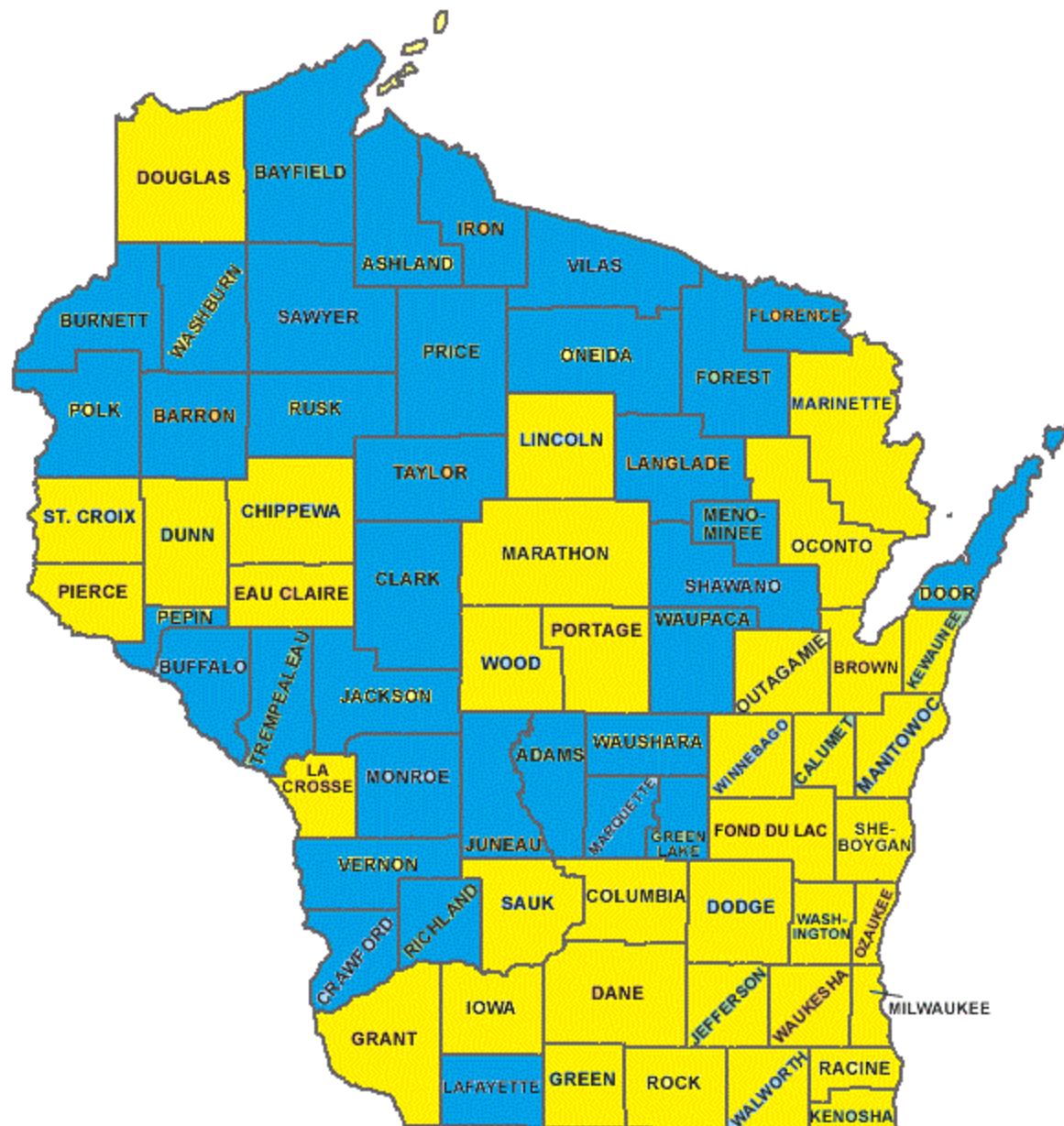
Washington



# West Virginia



Wisconsin



Wyoming

