Testimony of

B. Doyle Mitchell, Jr.

President and CEO of Industrial Bank

Washington, D.C.

On behalf of the

Independent Community Bankers of America

Before the

United States House of Representative

Committee on Small Business

Subcommittee on Investigations, Oversight and Regulations

Hearing on

"Regulatory Landscape: Burdens on Small Financial Institutions"

December 3, 2013

Washington, D.C.

Chairman Schweikert, Ranking Member Clarke, and members of the subcommittee, my name is Doyle Mitchell, and I am President and CEO of Industrial Bank, a $350 million asset bank headquartered in the District of Columbia. Industrial Bank was founded in 1934, in the depth of the Great Depression, and is the oldest and largest African American-owned commercial bank in the metropolitan Washington, D.C. area. We have over 120 employees. I testify today on behalf of the nearly 7,000 community banks represented by the Independent Community Bankers of America. Thank you for convening this hearing on the "Regulatory Landscape: Impact on Small Financial Institutions."

In addition to being a member of ICBA, I am also the Chairman of the National Bankers Association, a trade association for the nation's minority and women-owned banks. While many community banks serve rural areas and small towns, there is also an important segment of community banks like mine that serve urban areas and that were founded to serve minority communities that were historically and many times currently, ignored by other financial institutions.

America's 7,000 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. The recent FDIC Community Banking Study showed that in one out of every five counties in the United States, the only physical banking offices are those operated by community banks.[1] Community banks provide 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. Federal Reserve data shows that while overall small business lending contracted during the recent recession, lending by a majority of small community banks (those of less than $250 million in assets) actually increased, and small business lending by banks with asset sizes between $250 million and $1 billion declined only slightly. By contrast, small business lending by the largest banks dropped off sharply. The viability of community banks is linked to the success of our small business customers in the communities we serve, and we don't walk away from them when the economy tightens.

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, if adopted by Congress, 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. The Plan for Prosperity is attached to this testimony, as is a list of the 23 bills that have been introduced in the House and Senate to date that incorporate Plan for Prosperity provisions.

---

[1] FDIC Community Banking Study, December 2012. Page 3-5. (http://www.fdic.gov/regulations/resources/cbi/study.html)

New Rules Threaten Community Bank Mortgage Lending

A primary focus of the Plan for Prosperity is mortgage lending regulatory relief. Every aspect of mortgage lending is 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. In particular, community bankers are deeply concerned by the Consumer Financial Protection Bureau's (CFPB's) new "ability-to-repay" rule which will expose lenders to litigation risk unless their loans meet the definition of "qualified mortgage" or "QM." However, a staple of community bank mortgage lending, balloon loans, are explicitly excluded from QM status unless they are made in rural areas under an unreasonably narrow definition of "rural." Many community banks are not willing to assume heightened litigation risk and will exit the mortgage lending business particularly in rural markets. While ICBA supports the CFPB's amendments to the QM rule which make accommodations for community banks, they do not go far enough to preserve access to credit for community bank customers.

The "ability to repay" rule is scheduled to take effect January 10, 2014 and thousands of community banks, more than 50 percent, will not be prepared or are uncertain of their readiness to comply by that date. Even the most negligible regulatory change can require many months to change systems, update policies and procedures, revise underwriting requirements, and train staff. Bankers must ensure that vendors and suppliers are prepared as well. Changes of the magnitude of the "ability-to-repay" rule are particularly challenging for community banks given their limited staff and legal and compliance resources. Many community banks may be forced to suspend their mortgage lending until they become compliant. This would have a significant adverse impact on the recovering housing market. Other community banks may exit the mortgage business altogether. For this reason, ICBA is urging the CFPB to extend the mandatory compliance date and allow optional compliance for a period of 9 to12 months. We hope that members of this committee will support that request.

The CLEAR Relief Act

In addition to this administrative extension request, ICBA is seeking legislative solutions, included in the Plan for Prosperity, that would simplify community bank compliance with the CFPB "ability-to-repay" rule and other new mortgage and non-mortgage rules. While, as noted above, 23 bills have been introduced that embody Plan for Prosperity provisions, I would like to use this testimony to highlight the single bill that best captures the full scope of the Plan: the Community Lending Enhancement and Regulatory Relief Act (CLEAR Relief Act, H.R. 1750), introduced by Rep. Blaine Luetkemeyer, a former community banker and current member of the Small Business Committee as well as the Financial Services Committee. The CLEAR Relief Act has over 80 cosponsors with strong bipartisan representation. A Senate companion bill has similar bipartisan support. The CLEAR Relief Act contains eight Plan for Prosperity provisions, including:

Qualified Mortgage Status for Community Bank Portfolio Loans

The CLEAR Relief Act solution to compliance with the "ability-to-repay" rule is simple, straightforward, and will preserve community bank mortgage lending: QM status for community bank loans held in portfolio, including balloon loans in rural and non-rural areas and without regard to their pricing. This

provision would apply to all lenders with less than $10 billion in assets. 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.

Escrow Requirement Exemption for Community Bank Portfolio Mortgages

The CLEAR Relief Act would exempt community bank loans held in portfolio from new escrow requirements for higher priced mortgages. This exemption would also apply to all lenders with less than $10 billion in assets. Again, portfolio lenders have every incentive to protect their collateral by ensuring the borrower can make tax and insurance payments. For low volume lenders in particular, an escrow requirement is expensive and impractical and, again, will only deter lending to borrowers who have no other options.

Small Servicer Exemption

The CLEAR Relief Act would raise the CFPB's small servicer exemption threshold from 5,000 loans to 20,000. 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. These rigid standards reduce 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.

A higher exemption threshold would preserve the role of community banks in mortgage servicing, where consolidation has clearly harmed borrowers. Community banks above the 5,000 loan threshold have a proven record of strong, personalized servicing and no record of abusive practices. To put the 20,000 threshold in perspective, consider that the five largest servicers service hold an average portfolio of 6.8 million loans[2] and employ as many as 10,000 people each in servicing alone.

Appraisal Exemption for Smaller Mortgages

The CLEAR Relief Act would reinstate the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) exemption for independent appraisals for loans of $250,000 or less. 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

[2] Source: Office of Mortgage Settlement Oversight (www.mortgageoversight.com).

many community banks to use local appraisers and forced them to hire appraisal management companies at significant expense. The CLEAR Relief Act would provide relief from these costs, which are passed on to the borrower and increase the cost of credit.

Modernize the Federal Reserve's Small Bank Holding Company Policy Statement

The CLEAR Relief Act requires 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. This past November, the House Financial Services Committee passed out of committee a bill increasing to $1 billion, the Small Bank Holding Company Policy Statement. We applaud passage of this bill and urge House leaders to give this bill floor consideration.

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

The CLEAR Relief Act would exempt from the internal control attestation requirements of Section 404(b) of the Sarbanes-Oxley Act banks with assets up to $10 billion. The current exemption threshold applies to companies with less than $75 million in market capitalization. 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.

Eliminate Redundant Privacy Notices

The CLEAR Relief Act provides that a financial institution is not required to mail an annual privacy notice to its customers if it has not changed its privacy policies. Most community banks do not have the scale to automate the annual privacy notice mailings. For these banks, the mailings are a manual, labor intensive process. Eliminating this requirement when a bank has not changed it privacy policies, will conserve resources without putting consumers at risk or reducing their control over the use of their personal data.

This provision of the CLEAR Relief Act is also contained in a separate bill introduced by Rep. Luetkemeyer, the Privacy Notice Confusion Elimination Act (H.R. 749), which passed the House in March.

There are additional provisions of the CLEAR Relief Act. Together they provide a strong, clear legislative response to the threat of mistargeted regulation to the community bank charter.

Closing

I encourage you to reach out to the community bankers in your district. Ask them about the current regulatory environment and whether the CLEAR Relief Act, the Right to Lend Act, and the other Plan for Prosperity bills attached to this testimony would help them better serve their communities. We're confident that they will agree with us. Your cosponsorship of the CLEAR Relief Act and the other Plan for Prosperity bills would be greatly appreciated by community bankers and ICBA.

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 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. 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 the sensible regulatory reforms outlined above. We encourage Congress to consider ICBA's Plan for Prosperity as a guide to achieving these reforms.

Thank you again for the opportunity to testify today.

Attachments

- **Plan for Prosperity Bills**

Bills Containing ICBA Plan for Prosperity Provisions

The Community Lending Enhancement and Regulatory Relief Act of 2013 (H.R. 1750)
The Community Lending Enhancement and Regulatory Relief Act of 2013 (S. 1349)
The Protecting American Taxpayers and Homeowners Act (H.R. 2767)
The Terminating Bailouts for Taxpayer Fairness Act of 2013 (S. 798)
The Portfolio Lending and Mortgage Access Act of 2013 (H.R. 2673)
The Financial Institutions Examination Fairness and Reform Act (H.R. 1553)
The Financial Institutions Examination Fairness and Reform Act (S. 727)
The Eliminate Privacy Notice Confusion Act (H.R. 749)
The Privacy Notice Modernization Act (S. 635)
The Municipal Advisor Oversight Improvement Act (H.R. 797)
The Municipal Advisor Relief Act (S. 710)
The Consumer Financial Protection Commission Act (H.R. 2402)
The Responsible Consumer Financial Protection Regulations Act (H.R. 2446)
The Consumer Financial Protection Safety and Soundness Improvement Act (H.R. 3193)
Responsible Financial Consumer Protection Regulations Act (S. 205)
The Holding Company Registration Threshold Equalization Act (H.R. 801)
The Holding Company Registration Threshold Equalization Act (S. 872)
Mutual Community Bank Competitive Equality Act (H.R. 1603)
The Financial Regulatory Responsibility Act of 2013 (S. 450)
The SEC Regulatory Accountability Act (H.R. 1062)
The Right to Lend Act (H.R. 2323)
The S Corporation Modernization Act (H.R. 892)
To enhance the ability of community financial institutions to foster economic growth and serve their communities (H.R. 3329)