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May 14, 2015

Robert deV. Frierson, Secretary
Board of Governors
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Robert E. Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW
Washington, DC 20219

Re: Regulatory Publication and Review Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), Docket No. FFIEC-2014-0001; Fed Docket No. R-1510

Dear Sirs or Madam:

The OCC, the Federal Reserve Board, and the FDIC are conducting a review of the regulations they have issued to identify outdated, unnecessary or unduly burdensome regulation on insured depository institutions. This review is required under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA) and will be conducted over a two year period. The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the second notice that was published by the banking agencies under EGRPRA to help identify those regulations that are

[1] The Independent Community Bankers of America®, the nation's voice for more than 6,000 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.

With 52,000 locations nationwide, community banks employ 700,000 Americans, hold $3.6 trillion in assets, $2.9 trillion in deposits, and $2.4 trillion in loans to consumers, small businesses and the agricultural community. For more information, visit ICBA's website at www.icba.org.

outdated, unnecessary or unduly burdensome which are included in the categories of Banking Operations, Capital, and Community Reinvestment Act.

**The EGRPRA Process**

ICBA commends the banking agencies for scheduling six outreach meetings around the country to gather input from community bankers. So far, the three outreach meetings in Los Angeles, Dallas, and Boston have been well attended and the panel discussions have discussed a wide range of burden reduction recommendations. The issues that community bankers keep bringing up include (1) call report reform and in particular, having a community bank short form call report, (2) a two-year exam cycle for well-rated community banks, and (3) increasing many of the dollar or asset threshold requirements under the Bank Secrecy Act, Community Reinvestment Act, and the requirements for appraisals for real estate-related loans.

ICBA urges that these recommendations be implemented by the regulators or, in those instances where a statutory change is required, that the regulators recommend in their EGRPRA report to Congress that Congress adopt the change. In our first EGRPRA comment letter, ICBA called for (1) call report reform, (2) increasing the asset threshold under the Small Bank Holding Company Policy Statement to $5 billion, (3) reducing the regulatory requirements for de novo banks, and (4) simplifying and reforming Regulation O.

We also pointed out in our first comment letter that if the new EGRPRA process is to be successful, there must be a strong commitment by the heads of the banking agencies to do what is necessary to eliminate regulation that is outdated, unnecessary or unduly burdensome. This goes beyond merely streamlining, tweaking regulations or eliminating duplication. Rather, the mandate requires the agencies evaluate the costs and benefits of each regulation and carefully consider the input they receive from community bankers. Furthermore, even if there are some benefits to having a regulation, it should be eliminated under the EGRPRA process if it can be shown to be unduly burdensome.

In our first EGRPRA letter, we cited a number of studies on the impact of regulation on community banking, including one by the Mercatus Center at George Mason University[2] and another by KPMG[3]. Since our first letter, several other studies, including one by the Harvard Kennedy School for Business and Government[4] and another by the University of New Orleans[5], have confirmed that community banks have been adversely impacted by government regulation.

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[2] "How are Small Banks Faring Under Dodd-Frank?" Hester Peirce, Ian Robinson, and Thomas Stratmann. Mercatus Center Working Paper. February 2014

[3] The KPMG study can be found at: http://www.kpmginfo.com/industryoutlooksurveys/2014/pdfs/KPMGBankingIndustrySurvey_072414.pdf

[4] "The State and Fate of Community Banking" Marshall Lux and Robert Green, February, 2015

[5] "National and Regional Trends in Community Banking" Kabir Hassen and Will Hippler, III, March 31, 2015

**ICBA urges the regulatory agencies as part of the EGRPRA process to conduct their own empirical study of the regulatory burden on community banks to quantify the burden and confirm what these studies show—that the burden is significant and is driving community banks out of the business of banking.** Such a study could also identify those regulations that are the most burdensome. The FDIC attempted to conduct such a study as part of its 2012 Community Bank Study. In the appendix to that study, the FDIC summarized its interviews with community bankers concerning regulatory compliance costs but failed to quantify the costs, after concluding it would be too difficult.

**We urge the FDIC, the OCC, and the Federal Reserve to confirm what community bankers are also saying anecdotally—that each new regulation not only reduces the franchise value of their banks but also impairs their ability to lend to the communities they serve.**

**Specific Comments on the Three Categories of Regulations**

ICBA has a number of specific recommendations regarding the three categories of regulation that are currently subject to comment-- Banking Operations, Capital, and Community Reinvestment Act.

**Bank Operations**

**Regulation D.** Regulation D governs reserve levels and the types of deposit accounts that a bank must be reserved against. A bank must maintain reserves based on a specified percentage of "transaction accounts" but not on its "savings deposits." Regulation D limits the number of transfers that may be made from a savings deposit account to six per month. Provided the account meets these limits, it is not considered a transaction account for Regulation D purposes. As a result, the bank does not have to hold reserves against it.

Frequently, community banks have sweep arrangements that link money market deposit accounts (MMDAs) to transaction accounts. Even with the repeal of Regulation Q—allowing banks to pay interest on transaction accounts—community banks still offer interest bearing MMDAs as savings accounts to their customers to avoid the reserve requirements that would be imposed on an interest bearing transaction account. When they enter into such arrangements, Regulation D requires the bank to monitor the account to ensure that customers do not violate the six transfers a month rule. This monitoring can be an extensive regulatory burden.

**ICBA believes that Regulation D should be updated to allow up to ten transfers per month for a savings account or a non-"transaction account."** This additional flexibility would relieve some of the regulatory burden associated with monitoring MMDAs under Regulation D and having to contact the customer when violations occur. Ten transfers per month is also a reasonable number of withdrawals for an account to be defined as a "savings account." When we asked community bankers to comment on these regulations, one community banker related the following:

> "We have concerns about the Regulation D restrictions on savings accounts, especially with money market accounts being classified as savings accounts and the time spent monitoring these accounts for excess transfers. We wish we didn't offer MMDAs to consumers for the very reason of having to monitor these accounts for the excess transfers, mailing notices to these customers, and keeping up with how many times they have violated the transaction limits and changing their account type if they continue."

Another community banker noted that "customers do not understand these limitations, and blame the bank when we attempt to enforce the restrictions on transfers per month." ICBA believes that raising the transaction limit from six transactions to ten would relieve some of these regulatory burdens and customer frustrations with Regulation D. It would also allow community banks to continue offering these linked MMDAs to customers.

**Regulation S.** This regulation establishes the rates and conditions for reimbursement of costs directly incurred by financial institutions in assembling or providing financial records to a government authority. The costs and reimbursements are listed in a schedule included as part of the regulation. For instance, under the schedule, banks are reimbursed at $.25 a copy for reproduction of records and $22 per hour for clerical and technical work. There are also numerous exceptions under Regulation S so that a bank is not reimbursed if they receive an IRS summons or an administrative agency subpoena.

ICBA recommends that the reimbursement schedule in Regulation S be updated to reflect the true costs of complying with a request from a governmental authority, including bank personnel and overhead costs. As one community banker put it, "the Regulation S reimbursement rates are ridiculously low and do not adequately compensate for staff time in responding to such requests." Also, the reimbursement exceptions should be narrowed so that community banks can be adequately reimbursed for the work associated with complying with burdensome governmental requests for documents. Updating the reimbursement schedule and narrowing the exceptions would help alleviate the regulatory burden associated with complying with Regulation S.

**Regulation CC**. This regulation deals with the availability of funds to accountholders and the disclosure of funds availability policies. ICBA only has one comment concerning Regulation CC-- the extended hold notice process under the regulation. Banks must provide this notice in person or by mail following the use of an extended hold on an account as provided under Section 213.9 of Regulation CC.

Too often, community banks are criticized in their exams for not complying with the extended hold notice requirements. This often happens when examiners are hyper-technical about complying with Regulation CC. As one banker put it:

> "The extended hold notice process needs significant revision. During bank examinations, a single error or even a couple will result in documentation within



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the final exam report. This is a notice that is of little use to consumers, and too often is disregarded or not read."

ICBA urges the regulators to be more flexible in their examination of the extended hold notice process under Regulation CC. If extended hold notices are of little use to consumers and are often discarded (just like the annual privacy notices under Regulation P), then the regulators should consider revising Regulation CC to eliminate or substantially simplify them.

**Capital**

**PCA Requirements and Basel III.** With respect to the Prompt Corrective Action (PCA) regulations, ICBA believes the 2011 GAO report on PCA[6] provided some useful recommendations for improving PCA. We indicated to GAO at the time they were preparing their report that PCA may discourage potential investors from investing in a troubled bank because of concerns that the bank's closure will wipe out their investment. We suggested a more flexible PCA framework so that troubled banks can attract new capital and improve their chances for recovery and survival. **Furthermore, we noted that large banks with capital deficiencies are more likely to receive financial assistance or time to recapitalize than smaller banks and, therefore, that PCA should treat smaller banks the same as larger banks.** For instance, the U.S. Treasury was quick to bail out the larger banks in the financial crisis to avoid the PCA process, but community banks were not so fortunate. Hopefully, Titles I and II of the Dodd-Frank Act and in particular, the new Orderly Liquidation Authority will provide an orderly process to resolve a large bank failure and eliminate the disparity in treatment between resolving large and small banks.

However, ICBA is more concerned about the Basel III capital rules than the PCA regulations. Basel III was never intended to apply to community banks by the Basel Committee on Banking Supervision. It was designed to apply to the largest, internationally active, interconnected money center banks. ICBA supports legislation that would exempt banks with assets under $50 billion from being subject to Basel III.

Basel III's implementation of the capital conservation buffer is especially troublesome, particularly the far reaching impact on the nation's community banks organized as Subchapter S corporations. These corporations, with their pass-through taxable earnings structure, will have difficulty in raising new capital as potential investors will be fearful of the risk of having to pay federal income taxes on earnings that cannot be remitted to the investor. The capital conservation buffer should be modified to allow community banks to distribute no less than 35% of their reported net income for a reporting period.

Basel III also provides punitive treatment for a community bank's allowance for loan and lease losses, even though the allowance is the first line of defense against credit losses.

[6] See "Modified Prompt Corrective Action Framework Would Improve Effectiveness" General Accountability Office, June 2011

Regulators should allow for full inclusion of a community banks' allowance in regulatory capital regardless of the size of the allowance. Additionally, the first 1.25% of the allowance should be included in tier 1 capital. ICBA notes that the NCUA has recently proposed for the inclusion of the entire balance of the allowance in credit union total capital balances.

Basel III has also severely curtailed a community bank's ability to service mortgage loans when those loans are sold to GSEs and third parties. Bank regulators have yet to prove that mortgage loans serviced by community banks played any part in the recent financial crisis. In fact, mortgage servicing by community banks moves servicing to a customized, high-quality, effective servicing function from the commoditized, low-touch function performed by the largest banks and the non-bank mortgage servicers. Regulators should encourage more community bank mortgage servicing, not less. ICBA supports a community bank exemption from the Basel III treatment of MSAs. More specifically, ICBA believes that financial institutions in the United States with consolidated assets of $50 billion or less should be allowed to continue to be subject to the Basel I MSA regulatory capital risk weights and deduction thresholds.

Many community bankers feel that Basel III has imposed an onerous and unnecessary regulatory burden. For instance, the FFIEC had to issue another 60 pages of call report instructions for 2015 because of the Basel III changes that went into effect at the beginning of the year. The new Basel III risk weighting system, particularly with regard to HVCRE, equity exposures, and securitizations, has vastly complicated the work of not only community bank call report preparers, but CFOs and third party service providers that provide financial advice and IT services to the bank. In addition to having a community bank short form call report, regulators should simplify Basel III for community banks to relieve them of the regulatory burden of understanding all the complex risk based capital rules. ICBA believes that the first quarter 2015 call reports would likely show little difference in capital ratios for most community banks whether they used Basel I or Basel III. Yet the amount of time that community banks took to prepare the Schedule RC-R of the call report was a significant regulatory burden.

**Community Reinvestment Act**

The Community Reinvestment Act (CRA) was enacted in 1977 to prevent redlining and to encourage banks and savings associations to help meet the credit needs of all segments of their communities, including low- and moderate-income neighborhoods and individuals. Today, CRA and its implementing regulations require the bank regulators to assess the record of each bank in fulfilling its obligation to the community and to consider that record in evaluating and approving applications for charters, bank mergers, acquisitions, and branch openings.

The bank regulators evaluate a bank's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations. The CRA regulations use a tiered approach to evaluating

banks. Different evaluation methods are used based on the bank's size and how it operates. The regulations provide:

- Small banks—currently those with assets of less than $1.221 billion—that are not intermediate small banks are assessed under a streamlined method that focuses generally on their lending performance.
- Intermediate small banks—a subset of "small banks" with assets between $305 million and $1.221 billion—are assessed under the small bank lending test and a community development test that evaluates community development lending, qualified investments, and the community development services they provide to their communities.
- Large retail banks are evaluated under three tests. All lending activity, including community development loans, is evaluated under the lending test. Qualified investments are evaluated under the investment test. Retail and community development services are evaluated under the service test.

Even though these asset thresholds are adjusted annually based on the Consumer Price Index, the thresholds do not reflect the extensive consolidation and growth that has occurred in the industry since 1977 when CRA was adopted. Accordingly, ICBA recommends the asset thresholds be increased to reflect the consolidation and growth of the community bank industry.

**For "small banks," we recommend increasing the asset threshold to include all banks with assets less than $5 billion that are not "intermediate small banks." For "intermediate small banks," we recommend increasing the asset threshold to include banks with assets between $1.5 billion and $5 billion. "Large banks" would include all banks with assets of $5 billion or more. Once changed, all of these asset thresholds should be subject to annual adjustments based on the percentage increase in total assets of all insured depository institutions.**

By expanding the number of banks that fall under the definition of "small bank" and "intermediate small bank," the regulators would significantly diminish the CRA regulatory burden for most community banks. Small banks with less than $1.5 billion in assets would have CRA evaluations focused mostly on their lending performance and banks between $1.5 billion and $5 billion would have evaluations focused on a combination of lending, investments, and community development services. Raising these thresholds should not impact the ability of the regulators to adequately assess community banks for their CRA performance.

ICBA also recommends further changes in CRA asset thresholds. In general, the banking agencies conduct a CRA evaluation of a bank every three years. However, section 712 of the Gramm-Leach-Bliley Act (GLBA) mandates that small banks may be evaluated less frequently. A bank with assets of $250 million or less that received an overall CRA rating of outstanding or satisfactory at its last CRA evaluation is evaluated not more than once every 60 months or 48 months, respectively.

**We recommend that the GLBA provision be amended to cover banks with assets of $1 billion or less.** It has been more than 15 years since GLBA was enacted and during this time, the industry has gone through extensive consolidation so that a $1 billion dollar community bank today is equivalent to what a $250 million bank was in 1999. Furthermore, the bank regulators have the option to examine banks for CRA prior to their next exam date and frequently do so whenever a bank merger occurs or a branch is opened. **Lengthening the CRA exam schedule for banks with assets less than $1 billion that have outstanding or satisfactory CRA ratings to five years or four year respectively would go a long way toward reducing the community bank regulatory burden associated with the Community Reinvestment Act.**

**Conclusion**

ICBA commends the banking agencies for scheduling six EGRPRA outreach meetings around the country and encourages them to focus on the issues that community bankers frequently raise in their panel discussions--(1) call report reform, (2) a two-year exam cycle for well-rated community banks, and (3) increasing the various dollar or asset thresholds in BSA, CRA and in those regulations that deal with appraisals for real estate-related loans. ICBA also urges the regulatory agencies as part of the EGRPRA process to conduct their own empirical study of the regulatory burden on community banks to quantify the burden and confirm what many studies are showing—that the burden is significant and is driving community banks out of the business of banking.

With respect to the category of regulations dealing with Bank Operations, ICBA recommends updating Regulation D to allow up to ten transfers per month for a savings account or a non "transaction account." ICBA also recommends that the reimbursement schedule in Regulation S be updated to reflect the true costs of complying with a request from a governmental authority, and that extended hold notice requirements of Regulation CC be eliminated or substantially simplified.

With respect to the category of regulations dealing with Capital, ICBA supports a more flexible and even-handed PCA regime where small banks are treated the same as large banks. We have serious concerns with Basel III risk based capital requirements. Basel III's implementation of the capital conservation buffer is especially troublesome, particularly because of the impact on Sub S banks. The regulators should allow for full inclusion of a community banks ALLL as regulatory capital regardless of the size of the allowance. Additionally, the first 1.25% of the allowance should be included in tier 1 capital. We also believe that Basel III has also severely curtailed a community bank's ability to service mortgage loans when those loans are sold to GSEs and third parties. Basel III is far too complex and should be substantially simplified for community banks.

With respect to the Community Reinvestment Act, ICBA supports much higher asset thresholds for the definition of "small bank" and "intermediate small bank" to reflect consolidation in the community banking industry. We also support allowing community banks with assets up to $1 billion or less that received an overall CRA rating of

outstanding to be evaluated every five years and those with an overall CRA rating of satisfactory to be evaluated every four years.

ICBA appreciates the opportunity to comment on the second notice that was published by the banking agencies under EGRPRA to help identify those regulations that are outdated, unnecessary or unduly burdensome. If you have any questions or would like additional information, please do not hesitate to contact me by email at Chris.Cole@icba.org.

Sincerely,

/s/Christopher Cole

Christopher Cole
Executive Vice President and Senior Regulatory Counsel