CBAI's 2017 Federal Policy Priorities

The Community Bankers Association of Illinois (CBAI) supports fair competition for financial services, the clear separation of banking and commerce, the dual banking system/charter choice, and opposes the concentration of financial and economic resources as evidenced by mega banks which continue to be too-big-to-fail. Based on these principles, CBAI has identified the following 2017 Federal Policy Priorities to help community banks operate successfully and better serve their customers and communities.

- **Support** Meaningful Regulatory Relief, with Tiered Regulations and Supervision for Community Banks, as Contained in the Independent Community Bankers of America's (ICBA) *Plan for Prosperity*

- **Support** the Implementation of Regulatory Initiatives to Benefit Community Banks
    - Fintech National Bank Charters (OCC)
    - Current Expected Credit Loss Model (FASB)
    - Payday and Vehicle Title (small-dollar credit) Lending (CFPB)
    - De Novo Bank Formation, the Dual Banking System and Charter Choice (FDIC, Federal Reserve, and OCC)

- **Finally** Address the Issue of Too-Big-To-Fail Banks and Financial Firms to Protect Our Financial System, Economy, and American Taxpayers from Future Bailouts

- **Support** Enacting a New Farm Bill and Abolishing (or Reigning-in) the Farm Credit System

- **Support** Taxation of Credit Unions and <u>Oppose</u> their Expansion of Powers

- **Support** Enhanced Data, Cyber and Payment Card Security (Date Security)

- **Support** Mortgage Lending and Housing Finance Reform

- **Support** Consumer Financial Protection Bureau Reform

- **Support** the Federal Home Loan Bank System

CBAI's 2017 Federal Policy Priorities

Detailed Information

Support Meaningful Regulatory Relief, Together with Tiered Regulation and Supervision for Community Banks, as Contained in the Independent Community Bankers of America's (ICBA) *Plan for Prosperity*

CBAI is hopeful that both a new Congress and Administration will support the passage of meaningful regulatory relief for community banks. The continuing decline in the number of community banks combined with an increased concentration of banking assets in the mega banks pose a threat to our financial system and economy. Community banks are suffocating under an unprecedented regulatory burden which has driven many small banks to merge out of existence. Dealing with the increased regulatory burden is diverting scarce community bankers' resources from serving their customers and communities to new compliance requirements, reviews and documentation.

The financial crisis demonstrated that the risks taken by Wall Street are very different from those taken by community banks, and regulations should reflect those differences. The regulatory burden imposed on community banks by a one-size-fits-all approach ignores the disproportionate burden of banking laws and regulations on community banks. Credit unions, Farm Credit System lenders and other non-bank financial services providers are not subject to the same laws and regulations as community banks. This unlevel playing field places community banks at a significant competitive disadvantage.

CBAI supports the ICBA's ***Plan for Prosperity***, a policy platform for the 115th Congress that promotes a regulatory environment in which community banks can thrive and contribute to their local economies. The *Plan* contains flexible priorities to ease excessive, redundant and costly regulations while supporting greater regulatory accountability to help community banks dedicate more of their resources to promoting economic growth. The steady increase in regulations over many years threatens community banks and their communities.

The ICBA ***Plan for Prosperity*** contains the following issue areas and specific recommendations.

Access to Capital

- Restore the original intent of the Basel III rule
- Create a more accurate identification of "systemic risk"

- Spur additional capital for small bank holding companies by modernizing the Federal Reserve's policy statement (SBHC designation increase from $1 to $10 billion)
- Relieve community banks from excessive Securities and Exchange Commission rules
- Repeal the Collins Amendment for non-SIFIs
- Address minority bank capital challenges

Regulatory Relief

- Balance consumer regulation through more accountable Consumer Financial Protection Bureau governance
- Eliminate arbitrary "disparate impact" fair lending lawsuits
- Ensure the viability of mutual banks through new charter and capital options
- Support rigorous cost-benefit analyses of all new rules to determine if they are justified and needed
- Modernize the Bank Secrecy Act (BSA)
- Cut the red tape in small business lending by eliminating burdensome data collection
- Target the Volker Rule on a banks' individual risk
- Preserve access to investment advice for middle-class savers

Mortgage Reform

- Create a safe harbor from onerous underwriting standards
- Establish relief from burdensome HMDA, escrow and appraisal requirements
- Preserve the ability for community banks to continue servicing mortgage loans
- Reform the closing process and accompanying paperwork

Bank Oversight and Examination

- Strengthen accountability in bank exams and create a workable appeals process
- Reform bank oversight and examination to better target risk

Tax Relief

- Lower marginal rates needed for individuals, corporations and businesses
- Incentivize credit for low- and middle-income customers and American agriculture
- Modernize Subchapter "S" constraints (increase shareholders limits from 100 to 200)
- Create limited liability corporation (LLC) option for community banks
- Repeal the estate tax
- Update the bank qualified (BQ) bond issuer limitation
- Support a five-year loss carryback that encourages lending during economic downturns
- Create a tax credit for Bank Secrecy Act (BSA) compliance costs

Agriculture and Rural America

- Address arbitrary agricultural loan concentration limits
- Institute tax relief for rural lending

CBAI urges Congress and regulators to expand and refine a tiered regulatory system based on bank size and risk profile to ensure that every law, rule and regulation clearly distinguishes and appropriately regulate community banks.

Support the Implementation of Regulatory Initiatives to Benefit Community Banks

Special Purpose Fintech National Bank Charters (OCC)

The Office of Comptroller of the Currency (OCC) has proposed issuing special purpose national banking charters to financial technology (fintech) companies. This proposal was preceded by the OCC's efforts to position itself to be a valuable resource to community banks seeking to understand the risks and benefits associated with financial innovation. The OCC's proposal, however, raised many concerns and CBAI urged the OCC to delay moving forward with chartering new fintech companies until all of the concerns have been addressed and resolved.

The very legal authority permitting the OCC to charter fintechs has been challenged by the Conference of State Bank Supervisors, on behalf of state banking regulators, which has characterized the proposal as "fatally flawed". The legal authority to charter fintechs must be indisputably established before the OCC moves forward with considering applications from fintechs.

Thirty-four Republican members of the House Financial Services Committee have written Comptroller Curry recommending that the OCC "provide a full and fair opportunity for stakeholders to see the details of the special charter [and] solicit feedback." The members of Congress went on to caution, "If the OCC proceeds in haste ... or rushes to finalize the charter ... please be aware that we will work with our colleagues to ensure Congress will examine the OCC's actions and, if appropriate overturn them."

Fintechs have the very real potential to be transformative for the entire financial service profession. A single regulator acting unilaterally in the chartering, examining, supervising and regulating fintechs is not in the best interests of the profession, consumers and the economy. The cooperation and coordination between all of the national and state banking regulators is needed on areas of responsibility for chartering and supervision so that the collective expertise and unique perspectives of all of the agencies can be focused on the critically important issues.

CBAI urged the OCC to guarantee that Fintechs will comply with all banking laws, rules and regulations, and be held to the same rigorous safety and soundness, and supervision and regulation standards currently being required of community banks and bank holding

companies. These standards must include but not be limited to frequent examination, CRA compliance, compliance with laws to protect consumers, regulatory actions for noncompliance, sanctions and prohibitions, and personal liability for Fintech directors and officers.

Fintechs cannot have all of the advantages of a national bank charter with limited requirements, regulations and liability.

CBAI will be carefully reviewing the OCC's proposed revisions and will closely monitor all of its fintech initiatives to minimize any negative impact on community banks.

Current Expected Credit Loss Model (FASB)

The Financial Accounting Standards Board (FASB) approved significant revisions to the way community banks reserve for their loan losses. This new methodology is the Current Expected Credit Loss (CECL) model. CBAI had serious concerns with this harmful proposal and supported its modification or an exemption for community banks.

FASB claimed "in the aftermath of the global economic crisis, the overstatement of assets caused by a delayed recognition of credit losses associated with loans (and other financial instruments) was identified as a weakness in the application of existing accounting standards." FASB believed a new system (CECL) was needed to better prepare financial institutions for a future crisis by implementing a model that would use more forward looking information in calculating loan loss reserves.

Community banks did not cause the financial and economic crisis. Unfortunately many community banks failed during the crisis, but these were a small percentage of the total number of community banks. The overwhelming majority survived, most successfully weathered the severe storm, and the overwhelming majority are approaching a full but delayed recovery. Apparently, the existing Incurred [loan] Loss Model worked well for 90+% of all community banks. Despite this reality, FASB proposed CECL and community bankers and the associations that exclusively represent their interests mobilized to address legitimate concerns about CECL's impact on community banks.

After significant and impressive community banker input, which included FASB meeting with ICBA and CBAI bankers, and Congressional support, FASB agreed to address community banker concerns and revised their CECL proposal. The revised Model is more flexible and scalable for community banks by allowing them to evaluate and adjust loan loss amounts using qualitative factors, historic losses, and their current operating systems such as spreadsheets, narratives and other noncomplex estimation efforts.

Community bankers and Congress must now remain vigilant, and play an active role in implementing CECL, to ensure that the regulators and auditors recognize the full extent of the significant concessions made by FASB and that they supply community banks with clear, practical and easy-to-implement methodologies for calculating expected losses which can be seamlessly incorporated into their existing processes.

Payday and Vehicle Title (small-dollar credit) Lending (CFPB)

The Consumer Financial Protection Bureau's (CFPB) proposed small-dollar credit lending rules to address its concerns about consumer abuse caused by payday and vehicle title lenders. These rules, as they were proposed however, were too broadly drafted and would ensnare sensible community bank consumer lending. CBAI recommended the proposed rules be directed only at the unfair and abusive practices of other lenders and not community banks which treat their customers and communities fairly and with respect. CBAI expressed concern that the proposed rules would not only discourage community banks from expanding their small-dollar consumer lending activities, in response to the CFPB's apparent efforts to eliminate payday and vehicle title lenders, but would actually restrict their ability to continue meeting the reasonable consumer credit needs of the customers that community banks are currently serving.

CBAI continues to urge the CFPB to exempt community banks from the flawed Payday Lending rules. In the event an exemption is not granted, CBAI will carefully review the Bureau's revisions to the final rules and will closely monitor its implementation to minimize any negative impact on community banks' small-dollar consumer lending.

De Novo Bank Formation, the Dual Banking System and Charter Choice (FDIC, Federal Reserve, and OCC)

Newly chartered (de novo) community banks are vitally important to maintaining a strong, growing, evolving and vibrant banking profession. CBAI vigorously disagreed with the Federal Deposit Insurance Corporation (FDIC) halting de novo community bank formation after the financial crisis as potential investors were apparently steered to existing "problem" banks versus new opportunities. Even in the depths of the S&L crisis (1984-1992), when 1,800 banks and savings institutions failed, an average of 196 de novos were formed annually. The FDIC approved only five de novo bank charters from 2010 to 2016, compared to 1,341 new charters between 2000 and 2008. Only now has the FDIC indicated a potential change in direction to finally get back on the right course.

CBAI has reviewed the FDIC's recently proposed *Application Handbook* for newly chartered banks. CBAI believes the *Application Handbook* contains a useful roadmap for those interested in deposit insurance for a new bank charter. CBAI noted, however, that the absence of a useful roadmap was not the barrier to obtaining deposit insurance and the dearth of de novo banks during the past seven years. The lack of new charters was the result of a decision by the FDIC, despite assurances to the contrary, to require charter applicants to prove they were virtually failure-proof rather than just having a reasonable likelihood of succeeding.

An obvious example was a requirement that extended the de novo period to seven years for examinations, capital maintenance, and other requirements. The FDIC recently reduced the requirement to three years which, when combined with the Chairman's recent comments and additional resources (including the *Application Handbook*), hopefully signals a sincere change in the position of the FDIC towards approving applications for deposit insurance for de novo charters.

CBAI will be monitoring de novo activity to confirm the FDIC's recent change in position and looks forward to a resumption of many new banks being chartered each year to help maintain the vitality of the community banking profession.

Hand in hand with restarting de novo bank formation is the importance of maintaining the dual banking system, which has served our nation well for over 150 years, where chartering and supervision is divided between the federal government and the states. Community banks should also continue to be able to choose a banking charter that best fits their unique business model. A banking system with multi-agency (state and federal) regulators and charter choice provides the necessary checks and balances on the immense power of the regulators, as well as improved rulemaking, as the benefit of each agencies expertise and experience is brought to bear on complex and controversial issues. The dual banking system and charter choice must remain valued hallmarks of our nation's banking system.

Finally Address the Issue of Too-Big-To-Fail Banks and Financial Firms to Protect Our Financial System, Economy, and American Taxpayers from Future Bailouts

The Community Bankers Association of Illinois (CBAI) urges Congress and banking regulators to significantly reform our financial system to reduce the probability and severity of a future financial crisis and its devastating impact on consumers, the financial system and the economy. It is imperative that the perception and reality of too-big-to-fail (TBTF) be erased. Taxpayer-funded bailouts of mega banks and financial firms must never happen again!

A tragic result of the recent financial crisis is that the mega banks have grown larger, more complex and interconnected, and still remain candidates for future bailouts while the number of community banks has fallen by more than half (to approximately 6,000 institutions) and unfortunately represent less than one-fifth of all banking assets. The four largest domestic TBTF banks have grown rapidly since the mid-1980s and now control more than half of the banking profession's assets, with the twelve largest holding nearly 70%. The concentration of banking assets in a handful of large banks, particularly given their reckless behavior, endangers the health and stability of our financial system and economy.

The TBTF banks, not community banks, caused the mortgage meltdown and financial crisis. Our nation and the banking profession must be protected from a repeat of the massive destruction they caused. A growing chorus for resolving TBTF has been fueled not only by outrage over their taxpayer-funded bailouts but also by their numerous violations of the law (often criminal) as evidenced by an estimated $190 billion in fines and settlements, and deferred prosecution agreements (also referred to as conditional amnesty).

These TBTF banks have demonstrated that they cannot be effectively managed, supervised, disciplined, or resolved. During the financial crisis the federal government provided the mega banks with multi-trillion of dollars in financial assistance to save them from their rightful failure. Meanwhile, community banks received little assistance, and subsequently more than 500 of them failed across America, devastating their employees, customers and communities. No bank or financial firm should ever be considered to be too-big-to-fail, and community bank should never again be judged by the banking regulators as too-small-to-matter.

CBAI welcomes and is encouraged by the growing number of credible proposals to address TBTF and reduce the risks the mega banks pose to the financial system, economy and American taxpayers. These proposals come from highly credible sources including: FDIC Vice Chairman Thomas Hoenig, Minneapolis Federal Reserve Chairman Neel Kashkari and Arthur Wilmarth - George Washington University Law School professor and a nationally recognized authority on bank regulation. These plans are in addition to a number of legislative proposals including a 21st century version of the original 1933 Glass-Steagall [separation of banking and commerce] Act. CBAI urges the thoughtful consideration of these proposals, which are aimed at preventing another financial crisis, and encourages bipartisan agreement on a long-overdue path forward to resolving the important issue of TBTF.

As the remaining rules required under the Dodd-Frank Wall Street Reform Act are being finalized by the banking regulators, CBAI urges guarding against taking a premature victory lap to celebrate the end of TBTF. The issue of TBTF cannot now fade in the rear-view mirror as was

recommended by the American Bankers Association (ABA) which, along with the Financial Services Forum, Financial Services Roundtable, The Clearing House Association, and the Securities Industry and Financial Markets Association is the “cheerleader” association for the mega banks.

No TBTF bank or financial firm, its directors, officers, or employees should ever be too-big-to-manage, too-big-to-regulate, too-big-to-trust, too-big-to-fail, too-big-to-prosecute, too-big-to-punish, too-big-to-jail, and should certainly not be too-big-to-change. These mega banks have repeatedly proven, at great cost, that they are clearly too-big-to-behave. A solution must be found to the important problems they pose to consumers, financial system and the economy.

Support Enacting a New Farm Bill and Abolishing (or Reigning-in) the Farm Credit System

The Farm Bill (The Agricultural Act of 2014) expires in 2018 and may be reauthorized in 2017. A strong Farm Bill provides stability to the volatile farm sector. A new Farm Bill should ensure a robust future by allowing community banks to continue working with their farm and ranch customers to survive low commodity prices and other challenges. Crop insurance is a successful public-private program that is critical to the ability of farmers and ranchers to survive weather disasters and repay their farm loans. CBAI supports protecting the program from further cuts or other adverse changes that would discourage farmer and rancher participation or undermine private sector delivery. CBAI also supports USDA loan guarantee programs that help community banks manage lending risks to farmers and ranchers, and encourages Congress to significantly raise volume caps and provide additional funding.

CBAI opposes the expansionist agenda of the Farm Credit System (FCS or System) which has allowed FCS lenders to become almost the equivalent of commercial banks while retaining the benefits of their Government Sponsored Enterprise (GSE) status. The funding and tax advantages of the FCS allow their lender to siphon the best loans away from, and constitute blatant discrimination against, rural community banks. If the System chooses not to follow its narrow historic mission then it should be abolished or subject to funding restrictions, taxation and rigorous oversight and regulation.

With the support and cooperation of its “cheerleader” regulator, the Farm Credit Administration (FCA), the FCS has purposely strayed beyond its original mission and scope and is increasingly engaged in inappropriate and unprecedented lending activities. Today, the FCS is a $303 billion financial institution, roughly equivalent to the country’s 12th largest bank, with significant systemic and taxpayer bail-out risks.

Examples of FCS lending activity deviating from their founding purpose includes: a $750 million loan to Verizon Wireless (because Verizon – a multinational telecommunications conglomerate – was a "similar entity" to a rural telephone company), and a $350 million credit agreement to Frontier Communications (to help finance a $2 billion acquisition from AT&T). These corporations are not agricultural in nature, are hardly struggling financially, and certainly do not warrant tax-payer subsidized funding. Further evidence of straying from its original mission is that approximately one-third of Farm Credit System loans are not made directly to farmers, and over half of all FCS outstanding loans (at the end of 2013) were in excess of $1 million while the typical loan to a young, beginning or small farmer has a median size of only $250,000.

The FCS is the only GSE that competes directly with community banks. Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System all work cooperatively with community banks. It is the epitome of unfair competition when this public sector (multi-hundred-billion dollar GSE) competes directly with the private sector (Main Street community banks). Over 100 years of lavishly subsidizing the FCS is enough.

The System's funding and tax benefits harm Illinois' community banks. CBAI calls on the FCS to follow its narrow historic mission of serving *bona fide* farmers, ranchers, young-beginning farmers, small farmers, and their farmer-owned cooperatives. If it chooses not to follow this narrow mission, the System should be abolished.

In the unfortunate event the System is not abolished, CBAI believes FCS institutions should pay taxes when exceeding a given asset threshold, lending to large borrowers, or engaging any in non-farm lending activity. FCS institutions should be required to engage in joint rulemaking with federal banking agencies when proposing regulations that could involve non-farm lending. The FCA should also include a member of a federal banking agency on its three person board. Furthermore, FCS institutions should be required to register a class of stock with the Securities and Exchange Commission (SEC) and provide full disclosure as required by the SEC Act of 1934. Finally, the FCS should publish instances of any illegal lending and any exemptions granted for such lending, and should be subject to regulatory safeguards, disclosures and controls equal to community banks and housing GSEs, including Consumer Financial Protection Bureau oversight.

CBAI also calls on Congress to hold joint committee hearings to investigate the operations, supervision, risks and financial soundness of the FCS, and its increasingly harmful impact on rural community banks. Investigative hearings will inform the financial services/banking committees about the systemic importance and bailout risks of the FCS (which is the equivalent of the 12th largest bank in the country operating outside of its purview), and the agricultural

committee about the impact of the FCS on the financial system and rural community banks (which is operating within its purview).

Support Taxation of Credit Unions and Oppose their Expansion of Powers

Credit unions are now indistinguishable from community banks and have grown to control a significant share of the banking services market. Their original business model, approved by Congress in 1934, is outdated and credit unions have long ago strayed from their founding mission of enabling people of modest means and with a common bond to pool their resources to meet their basic deposit, savings and borrowing needs.

Credit unions now provide the same financial services as community banks, and their federal tax-exempt status, in exchange for serving their original mission, is clearly no longer justified and constitutes blatant discrimination against tax-paying community banks. Credit union tax subsidies should be eliminated and credit unions should pay their fair share of income taxes.

The total assets of credit unions now exceeded $1.3 trillion. The largest credit union is $58.1 billion in assets; there are 21 credit unions with over $5 billion in assets; and the 498 largest credit unions (with $938 billion in assets) now account for 72.2% of the total system assets. These billion dollar credit unions are larger than 90% of the nation's community banks. Many of these large credit unions adhere to only loose common bond requirement or choose to operate within a well-defined local community, neighborhood or rural district. In fact, many credit unions now advertise that virtually anyone can join.

Credit unions were originally tax-exempt because of their similarity to other types of mutually owned financial institutions, notably savings banks and savings and loans. Yet the exemption for SBs and S&Ls was repealed by Congress in 1951 because they were in "active competition" with taxable institutions [community banks]. The most recent Office of Management and Budget tax expenditure analysis estimated that the tax-exemption for credit unions represents sorely needed federal tax revenues of $9.46 billion over fiscal years 2014-2018.

Credit unions have tried to expand their commercial lending powers by pressuring Congress to increase the percentage of assets cap on member business lending (MBL) and through regulatory rulemaking. Any growth will likely come at the expense of tax-paying community banks. In addition, credit unions are seeking approval to raise capital from outside investors, thereby discarding their longstanding reliance on retained earnings to support growth. This change would fundamentally alter the exclusive member-focused character of credit unions – a

condition for their original tax exemption. Credit unions should not be granted these or any additional powers as long as they remain exempt from taxation.

The National Credit Union Administration (NCUA), the “cheerleader” regulator of credit unions, has allowed credit unions to take full advantage of a loophole which allows those with low-income designations to increasingly focus on member business loans versus helping underserved customers. Credit unions with low-income designations, which are exempt from federally mandated MBL limits, doubled in the first two years after the designation change to a total of 2,107 to almost 40% of all federally insured credit unions. The NCUA and credit unions must be stopped from gaming the system to expand their powers.

The NCUA has approved rules to expand credit union membership that would significantly weaken the current common bond requirements established by the Federal Credit Union Act. It has been characterized by the NCUA itself as the most comprehensive, sweeping, and substantive policy change in this area in over 45 years, and is another example of its attempt to extend credit unions’ government-funded competitive advantages over taxpaying community banks.

The reason for the membership proposal, as explained by NCUA’s Vice Chairman, was due to a deadlocked Congress. Obviously the NCUA is trying to accomplish by administrative fiat what it has been unable to accomplish through the legislative process, completely disregarding the fact that Congress enacted limits on their industry for very good reason – to limit risky lending and to restrict these tax-exempt institutions to their founding purpose of serving individuals of modest means and with a common bond.

CBAI opposes this membership proposal and other initiatives to expand the powers of credit unions. If credit unions want to weaken (so as to virtually eliminate) their reasonable constraints and operate like banks, they should be taxed like banks and they should be required to meet all of the same regulatory requirements of community banks including complying with the Community Reinvestment Act (CRA) and Call Report filing requirements.

During the 115th Congress CBAI anticipates credit unions will continue to advocate for additional expansions of the powers. Given current budget deficits and the ever-growing federal debt, together with survey results showing community banks do a better job of serving the very customers credit unions were originally intended to serve, now is the time for Congress to end this discrimination against tax-paying community banks.

Credit unions were never meant to be tax exempt community banks!

Support Enhanced Data, Cyber and Payment Card Security (Data Security)

Community bankers and their customers are deeply concerned by wide-scale data security breaches at national retail chain stores and other entities. These far-reaching and costly incidents have resulted in community banks reissuing more than 10 million credit and debit cards at a cost of well over $100 million.

Community banks are on the frontline of defending against cyber security threats and take their role in securing data and personal information very seriously. Community banks are strong guardians of the security and confidentiality of customer information as a matter of good business practice and to comply with legal and regulatory requirements. Safeguarding customer information is central to maintaining public trust and is the key to long-term customer retention.

CBAI is alert to an emerging threat to data security from the proliferation of companies seeking access to bank customer account information and the CFPB's interest in this issue as evidenced by a recent Request for Information which is a precursor to future rulemaking. While CBAI supports responsible innovation in financial products and services, the integrity of consumer data and privacy is only as strong as the weakest link. On the one hand, community banks are financially sound and take care in protecting consumer privacy, but on the other hand, these non-bank entities are typically not well capitalized, have no real assets and are financially unable to make consumers whole in the event of a loss. They must be held responsible for ensuring the safety of the customer information they are accessing and be able to satisfy the liability for any financial harm which they cause community banks and consumers.

CBAI supports core data security principals which include the cost of data breaches being borne by that party that caused the breach (including fraud losses and the cost of card reissuance); all participants in the payment system (including merchants) should be subject to verifiable Gramm-Leach-Bliley Act-like data security standards; a national data security breach and notification standard should replace the current patchwork of state laws; and any new data security standard proposals should ensure that community banks are not burdened with having to reassess existing critical systems, and implement and comply with new regulations, only to achieve the same superior results they currently attain. In addition, policymakers must recognize that traditionally community banks have heavily relied on third party service providers (core data processors and subcontractors of technology service providers for example). Regulators must make sure that community banks are adequately protected by broadening the supervision of these service providers to ensure they comply with

nondisclosure and confidentiality requirements similar to existing requirements for community banks.

Support Mortgage Lending and Housing Finance Reform

Imprudent mortgage lending contributed significantly to the mortgage meltdown and the financial crisis. Community banks are common sense relationship lenders that did not participate in abusive and predatory lending practices. Community banks thrive on the strength of their reputations and have every incentive to make fair and reasonable loans. They do not need prescriptive regulations to compel them to do what is right for their customers.

Proposals to curb imprudent lending practices must not negatively impact responsible community bank loan products which are designed to meet the diverse needs of their customers, including borrowers with special needs and circumstances, first-time homebuyers, borrowers in rural and underserved areas, and low-to-moderate income borrowers. Regulators must recognize the difference between community bank non-traditional lending, with underwriting based on first-hand knowledge of their customers and communities, and the predatory lending practices of others.

CBAI recommends that all community bank loans which are held in portfolio for the life of the loan, including balloon payment loans, in all geographic areas, should receive automatic Qualified Mortgage (QM) status and an automatic exemption from escrow requirements for Higher-Priced Mortgage Loans (HPMLs). Community banks that hold residential mortgage loans in their portfolios have 100% of the credit risk and every incentive to ensure their loans are properly underwritten, well documented, affordable to consumers, and properly serviced throughout the life of the loans. Limiting the QM's safe harbor status for loans held in portfolio by community banks will not make the loans safer, nor will it make underwriting more conservative. It will unfortunately deter community banks from making residential mortgage loans and reduce access to credit for their customers and communities.

CBAI also recommends an increase in the "small servicer" exemption from 5,000 to the highest of 30,000 loans or $5 billion in total unpaid principal balance of mortgage serviced; an increase in HMDA reporting levels that would exclude a significant number of community banks; and a safe harbor from the newly implemented TRID. CBAI also supports broad special accommodations for community banks which would provide them with greater flexibility in serving the needs of their customers and communities, particularly in "rural" areas, and urges expanding the definition of "underserved" areas to include economically challenged areas.

Further, community banks should be permitted to use property evaluations completed by qualified bank staff in lieu of a residential property appraisal for any residential mortgage that a community bank originates and retains in its portfolio.

As it considers reforms to the housing GSEs, Congress should recognize that community banks and our economy need the continued existence of an impartial secondary market for residential mortgages that is financially strong and reliable. Fannie and Freddie may not survive in their current form; however, the financial crisis demonstrated the need for some level of government involvement in the secondary market to ensure the continued flow of credit and market liquidity during periods of severe economic stress. CBAI supports common sense reform of the housing GSEs that does not limit the full participation by community banks or disrupts the housing market, and encourages a return of private capital to reduce the reliance on government funding and help protect taxpayers from another bailout.

CBAI supports allowing community banks to sell loans through an independent entity that does not compete with community banks; there should be no appropriation of community bank customer data for the purpose of cross selling financial services; the Federal Home Loan Banks must be preserved as a community bank access point (but not the only access point) to the national secondary market; the pricing of any governmental guaranty must be fair and equal to all participants regardless of volume of loans guaranteed; the 30-year fixed-rate mortgage for creditworthy customers in all markets; and there must be no further consolidation of the housing finance system that would result in mega banks and financial firms dominating the market.

Support Consumer Financial Protection Bureau Reform

CBAI encourages the Consumer Financial Protection Bureau (CFPB) to use its statutory authority under the Dodd-Frank Act to exempt any class of providers [community banks] or any products or services from the rules it writes, but to-date the Bureau has been far too reticent to do so. The CFPB should use this authority to effectively ensure community banks can continue to provide a robust alternative to large banks and non-banks for consumers seeking to use responsible financial service providers.

Regulations promulgated by the CFPB must provide community banks with the flexibility to meet the unique needs of its customers and not burden community banks with additional and unnecessary regulatory requirements that could prevent them from serving their communities. A one-size-fits-all approach to CFPB regulations harms community banks whose business model is focused on meeting the unique needs of its local customers and communities. Community

banks should not endure any additional regulatory burden on top of the existing crushing burden they already face on a daily basis.

CBAI is concerned with the CFPB influencing marketplace behavior by targeting of financial institutions, products, services, and practices which it deems to be undesirable or inappropriate regardless of what the consumer wants. The Bureau accomplishes its objective by pressuring the targets through investigation, regulatory rulemaking and enforcement actions. Protecting consumers against fraud and abuse is important and necessary, but disregarding the consumers' preferences is an entirely different matter. CBAI believes it is inappropriate for the Bureau to exert such influence by imposing its choices on the marketplace, thus hurting the very consumers the CFPB was ostensibly created to protect.

CBAI supports reigning-in the CFPB by replacing single-Director governance with a five-member commission. This governance structure would enhance decision-making by incorporating more diverse views and experiences and include needed checks and balances. The prudential regulators should participate with the CFPB in the rule-writing process, and the Financial Stability Oversight Council (FSOC) should have the power to veto CFPB rules under a more practical and realistic standard than currently exists.

CBAI supports a broad definition of firms that grant credit being subject to the CFPB rules, and their robust supervision and examination. The focus of any enhanced regulation of financial products should be on the mega banks and financial firms and the unregulated "shadow" financial industry. CBAI also supports the CFPB's efforts to use its authority to address non-banks which serve as channels for financial products, such as emerging financial technology (fintech) companies and Wal-Mart.

The primary goal of the CFPB should be to hold all of the other financial service providers up to the same existing high standards for compliance with consumer laws, rules and regulations as are currently attained by community banks.

Maintain the Federal Home Loan Bank System

The Federal Home Loan Banks (FHLBs) have developed a strong partnership with community banks. FHLBs provide short-term liquidity, long-term funding and other financial products that serve the needs of all member-owners and help them provide lendable funds for the local communities they serve. The regional structure, special functions and purposes of the FHLBs

must be recognized and maintained by the Federal Housing Finance Agency (FHFA). The FHLB System must remain a financially sound, stable and reliable source of funding for its members.

CBAI remains concerned about FHFA rulemaking to restrict FHLB membership eligibility requirements which will have had a profound negative impact on the FHLB System and its members. The FHFA relented in recent rulemaking and exempted community banks, but a troubling precedent was set by terminating an entire class of members, and the threat to revisit the broader membership issue in the future. The proposed rule was contrary to the will of Congress which has controlled access to the FHLB System over the past 82 years. Both CBAI and Congress must be vigilant to prevent the FHFA from any restriction in FHLB membership requirements for community banks.

As the Administration and Congress consider reforming the housing finance system, the FHLB System must remain a healthy, stable and reliable source of funding for its members, it should not be relied upon as the sole aggregator or securitizer of residential mortgages for community banks, and the FHFA should not impose an ongoing housing mission asset test on community financial institutions.

March 31, 2017

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