Reading Cooperative Bank

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RE: EGRPRA Project – Regulatory Relief and Paperwork Reduction

Dear Sirs/Madame

First, I want to thank you all for providing this forum to underscore some of the regulatory challenges and seeking to alleviate burdensome or outdated regulations.

As more and more Fintech developers enter the payments and banking space, the industry and its regulators need to be mindful not to disadvantage the industry.
The one size fits all banking regulations are preventing community banks from developing innovative solutions and products for differing underserved markets.

First, I want to discuss the process whereby Laws become regulatory rules and guidance. There is a huge opportunity to improve transparency and compliance by simplifying guidance and allowing adequate time for banks to reply and comply; community banks do not have the staff required to read and analyze 2000 page documents to determine the adverse operational effects in their entirety; rather we wait for an examination and hope we got it right.

An example of inadequate time to comply is the Call report revision document published on February 25 along with an 89 page Instruction Booklet for a report that must be filed at the end of March. The changes include major changes to risk based capital, a one-time institutional decision to opt out of AOCI and the removal of mortgage loan servicing rights from capital. These are significant balance sheet shifts which require management forethought and decisioning. The current reporting form for the revised risk weighted assets portion of the call report was still a draft when March call reports were due and there was a lack of clarity around qualified collateral.

My first recommendation is to include the banking industry a lot earlier in the regulatory rule writing process so everyone understands the ramification to the industry and bank business model.

The following comments I will address by topic as follows;

CAPITAL

Basel III is an example where community banks were not aware of the scope of the new rules. As a $500MM bank I am not systemically significant, however, the effect of some of the elements of Basel III will impact my decisions and not for the good.

a. Servicing Assets – removing the value of servicing rights from regulatory capital depending on their business model as a mortgage bank and the size of their accumulated servicing rights. Especially a mutual bank that cannot raise capital without converting and selling out the bank. To cause a community bank to sell off its servicing rights disadvantages the model of local relationship banking. Consumers are not served if a bank sells its servicing outside of the state to a behemoth servicer to monetize the asset.

b. Goodwill and intangible assets excluded from regulatory capital – Many community banks have had to take a charge for regulatory capital for goodwill and intangibles on their books from the prior acquisition of a local property and casualty insurance company. Our regulators are encouraging us to expand into new business lines to augment earnings, however, we will be penalized if we are to do so as most complimentary business lines are comprised of intangible assets. Our bank tabled its intended acquisition due to the adverse effects of this regulation.

Basel III was intended to rein in large national and international systemically significant banks, not traditional banks.

c. The next rule that caught the industry unawares were the proscriptive rules around what is equity in a commercial real estate loan transaction. The new risk based capital rules around High Value Commercial Real Estate loans will be most difficult to comply with and will serve to erase even more capital from our books. Maybe the large banks have a field in their loan system that measures how much cash or marketable securities a borrower has put into a loan transaction, but heretofore, the measure of risk monitored was loan to value. These new rules treat CRE differently based on how the borrower or bank put the deal together. 1031 exchanges, leveraging unencumbered real estate and pledging assets has historically been an acceptable method of reducing risk in a loan transaction. Reducing risk based capital for these transactions is not reflective of the balance sheet risk that they present. I would further suggest that the Call Report data for the HVCRE will be unreliable and unequitable between banks.

d. Capital stress tests - capital planning and for that matter asset liability management and interest rate risk is performed by every institution. We understand that the regulatory agencies have their own models and tests. Right now banks guess at the scenarios that you envision; why not share the model or at least your concerns so we can be on the same page prior to an examination. Transparency around expectations would be really helpful.

Community Reinvestment Act

Having recently added a branch abutting a Gateway city has been truly educational. The products and delivery mechanism in a dense inner city largely populated with new immigrants are challenging. The Mayor refers to their economy as a cash based society; non-bank lenders are rampant charging exorbitant rates. Bringing the unbanked cash based business owner or employee into the banking system would be beneficial to all parties, however, we struggle meeting the safety and soundness expectation of credit scoring and historic financial documentation in meeting business needs and the further challenge of CTR and SAR filings for cash and unclear source of funds. The idea of bringing a cash based unbanked individual/business into the banking system, then subjecting them to CTR and SAR filings will not engender trust with the community you are attempting to serve. I would encourage regulators to start a dialogue with FinCen about how to accomplish entry to the banking system with a possible 12 month moratorium on filing to build a history to then compare against.

CRA and the Internet - The majority of our applications come over the internet where we are competing against national banks, national mortgage brokers and non bank financial companies for customers. a) CRA should be required of any entity or individual writing or brokering a loan including the entire credit union industry b) Disparate impact should not apply on the internet.

I would caution the CFPB to slow down on the crackdown on check cashers, overdrafts and payday loans to the Gateway cities, until banking rules are simplified; these programs in some cases are the only means of access to emergency funds for low to moderate income immigrants. If you can't fix your car on Wednesday, you may not have a job on Friday when the paycheck comes in.

CTR's

As it relates to CTR's; the $10,000 threshold should be raised or filing requirements lifted; law enforcement locally has confirmed that CTR reports are rarely reviewed and the data is obtainable through subpoena. Doing away with the CTR filings would reduce a significant regulatory burden and customer inconvenience.

Removing CTR filings alone would reduce, documentary, research, training, software and employee cost to my bank by over $75,000 annually for this $500MM bank.

Regulation E and Regulation D

The most harmful and useless regulation in our market area is Regulation D. The regulation handicaps banks preventing us from competing with non-bank financial providers.

Under Reg D at present, whenever our customer transfers more than 6 times from their savings or money market account into their checking account, we must notify them in writing to cease and desist or we will close their account. Not a very nice way to build a relationship and grow deposits. We participated in a study on Reg D and determined that it costs us $3000 monthly to meet the demands of this outdated regulation which represents the cost to monitor transactions on every account, violation notices and mailings. This does not contemplate the cost of lost depositors when customers are forced to close accounts. We have documented customer complaints when they cannot use or access their funds; we just make it clear that it is the federal government denying them access as we would be happy to give them unlimited access to their personal savings.

The monthly costs calculated above does not include the quarterly reports that we must provide to the Fed to calculate our reserve requirement. Our reserve requirement is $200,000. A lot of work for clearly no risk to the monetary system. It's no wonder millennials say they won't need banks and are using VENMO to trade funds with friends, not a bank.

Under Reg D if a customer walks into a physical branch or up to an ATM, they can make any number of transactions they want; unfortunately this dated regulation did not contemplate that a consumer sitting in his house in his pajamas would be able to sign into his bank's online branch and transfer money between **his** accounts on nights and weekends. This regulation would relieve significant burdens and allow banks to innovate on behalf of their customers.

If the regulation cannot be done away with, a simple fix would be to modify the language to include online or mobile application transfers to be considered in branch transactions.

PRIVACY NOTICES

The annual privacy notices annually cost our bank $15,000; consumers complain about the paper waste as we are a green certified business; and this is not green. There is a proposal to require a notice only if the policy changes, delivery at account opening and policy availability online and on request. This seems a fair resolution of a waste of time, money and productivity.

REGULATION E and ERROR RESOLUTION

Reg E is another clunky regulation that deserves a closer look in light of payment system changes, new market entrants and fraud loss issues. I sat with our Operations department to obtain more clarity around the confusing regulation; I see a lot of opportunity to smooth out the payment system and regulation.

We average $5,000 in fraud loss monthly. The Target breach alone cost us another $16,000 and a local restaurant with an employee skimmer cost us another $24,000. The cost of reissue is $6 a card, and the man-hours blocking cards and researching fraudulent items and calling customers brings the fraud costs for our debit/credit channels to well over $100,000 this past year alone.

The regulation as presently written has created adverse consumer learned behaviors. Certain consumers contact their bank to state that they have had a fraud loss when their balance is low. No documentation from the customer is required; if the bank cannot disprove their claim, we have to rebate the funds. Mastercard and Visa refuse to hold retailers accountable, so the system is rigged against us.
Our sole recourse under this rule for repeat offenders using their cards irresponsibly or misrepresenting a fraud is to close the customer's account; after being taken advantage of.

My son of 16 recently took a job at KMART- I went to pick him up and entered the store for the first time in I don't know how long. I was dismayed to see at the entrance to the stores that they have become the immigrant; unbanked provider of financial services from check cashing to wire transactions. They are a national MSB; the type of business, we decided to stop banking years ago because the regulatory requirements were too large. Clearly something is wrong here when it is too hard for us to provide banking services to this population as a Bank, but Sears/KMART can do so nationally as a nonbank provider.

EXAMINATIONS

On the matter of examinations – I would be happy to see a 24 month cycle between exams for banks rated 1 or 2. I do not support a limited call report, as the extended exam would require regulator visibility into the institution. I think a better regulatory relationship is a dialogue about strategies, management vision and direction rather than sifting through 18 months of old data. A dialogue between examinations about balance sheet and risk migration would benefit both the bank and the examination staff.

NEW MORTGAGES RULES

In general we are having difficulty approving loans today that we would have done in the past. The Ability to Re-pay rule has resulted in an increase in decline rates to single women (issue of divorce and re-employment) and approval of self-employed existing long term customers with understood irregular cashflows.

For the divorced mother, a low loan to value buyout of the family home would have allowed the bank to consider her degree (for a mother re-entering the workforce) and earning potential and family support in its decisioning; this is the basis for community based lending. Ability to Re-pay is so prescriptive that one of our 20 year bank business customer cannot refinance existing debt at a lower rate with no cash out because they sold a business in the prior year and have not yet bought their next business.

A proposal exists to exempt any loan held in portfolio from QM and should be extended to Ability to Repay. The concern during the crisis was "skin in the game". For portfolio loans, we have just that; our loan quality is the same today as it was before and during the financial crisis. The loans that are not being made are not bad loans, the rules that were written are for long distance lending by the systemically significant banks. We are community lenders; it's just different.

The increased documentation requirements for the multitude of new rules have increased our loan files from 3 inches to 5; We have two more individuals generating the same volume and have had to increase our processing and underwriting fees (in line with peer increases) by $850 a loan.

We are in the process of introducing risk premiums for any non QM loan. We will then evaluate whether we can make an adequate return on residential loans in this interest rate environment.

FAIR LENDING

Recent judicial rulings have been made regarding HUD's interpretation of disparate treatment vs. disparate impact. We have received no word from our regulators surrounding this issue. My comments above regarding single women post-divorce was found based on an internal fair lending review. It is important that our regulators advise us whether they are reviewing us for disparate impact which is harder to control than disparate impact.

GENERAL

Earnings challenges abound at Community Banks across this nation evidenced by the acceleration of mergers of smaller banks in an effort to gain scale and efficiency.

I strongly believe that smaller community banks across this nation serve their communities financial needs better than their national and regional counterparts because of their proximity. I am optimistic that this EGRPRA process will create opportunity and improve the competitiveness for these banks to avert the decline in our numbers.

Working groups in the regulatory rule making process hereafter should include banks of all sizes as advisors to identify the ramifications of proposed rules on the community bank business model; they should also allow for reasonable implementation time following concise FAQ's and implementation guidance.

Respectfully Submit

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