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April 20, 2004

Public Information Room
Office of the Comptroller of the Currency
250 E Street, SW
Mailstop 1-5
Washington, DC 20219
Attention: Docket No. 04-05

Robert E. Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429
Attention: EGRPRA Burden Reduction Comments

Ms. Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Attention: Docket No. R-1180

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
Attention: No. 2003-67

Re: EGRPRA Review of Consumer Lending Related Rules

Dear Sir or Madam:

The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the regulatory burden imposed by consumer lending regulations. This review is being conducted under the Congressional mandate established in the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA).

Overview

Regulatory Review. The ICBA strongly supports the comprehensive review of regulations by the federal banking regulators under EGRPRA. The ICBA believes this is an important step and is working closely with member banks to identify regulations that are appropriate candidates for elimination, streamlining or revision. Community bankers

[1] The ICBA represents the largest constituency of community banks in the nation and is dedicated exclusively to protecting the interests of the community banking industry. We aggregate the power of our members to provide a voice for community banking interests in Washington, resources to enhance community bank education and marketability, and profitability options to help community banks compete in an ever-changing marketplace.

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work diligently to serve their customers' best interests, but find that regulations – especially consumer lending regulations – consume valuable resources and can interfere with good customer service. Initial banker feedback indicates that consumer lending and disclosure regulations (including the Truth in Lending right of rescission) are among the most burdensome. (Others include: Bank Secrecy Act and anti-money laundering compliance, Community Reinvestment Act, and privacy notices.[2]) For this reason, careful review of the regulations subject to the current comment period is particularly important.

The Impact of Cumulative Regulatory Burden on Community Banks. The ICBA supports a bank regulatory system that fosters the safety and soundness of our nation's banking system. However, recent statutory and regulatory changes have greatly increased the cumulative regulatory burden for community banks that are often disproportionate to the risks they pose. These recent changes include the privacy title of the Gramm-Leach-Bliley Act; the anti-money laundering/anti-terrorist financing provisions of the USA-PATRIOT Act; and the accounting, auditing and corporate governance reforms of the Sarbanes-Oxley Act.

Regulatory and paperwork requirements impose a disproportionate burden on community banks with their limited human, financial and other resources. This diminishes their ability to serve their communities, attract capital and support the credit needs of their customers. Credit unions and other nonbank institutions that perform "bank-like" functions and offer comparable bank products and services are not subject to the same laws and regulations as community banks. This places community banks at a competitive disadvantage and increases costs to consumers.

For these reasons, the ICBA also strongly urges the agencies to constantly assess regulatory burden, incorporating careful and accurate cost-benefit analysis into all facets of the regulatory process, in addition to the current review.

For example, consumer activists complain about predatory lending but disregard the fact that depository institutions, that are almost never guilty of predatory practices, must already comply with a staggering load of disclosures, reporting and other requirements that predators ignore. These rules drive up lending costs, and low- and moderate-income borrowers are driven into the arms of the very predators who already ignore regulations. Each individual requirement may not be burdensome, but the cumulative impact of consumer lending rules, by driving up costs and slowing processing time for loans from legitimate lenders, helps create a fertile ground for predators. It's time to acknowledge that unduly burdensome consumer protection regulations may be part of the problem.

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[2] The ICBA applauds the steps regulators are taking to alleviate burden by increasing the asset size limit for eligibility for the streamlined small bank CRA exam, studying ways to simplify privacy notices, eliminating unnecessary Currency Transaction Reports, and improving the call report process.

Current EGRPRA Review

Truth in Lending (Federal Reserve Regulation Z)

Right of Rescission. Perhaps one of the most troublesome issues of current regulatory requirements is the right of rescission under Regulation Z. Bankers have identified the right of rescission as one of the top ten regulatory complaints. Most of the problems this particular right is designed to rectify originate with non-depository creditors, not banks, a fact that should be considered. Moreover, banks and thrifts are closely examined and supervised, another key point to factor into the equation, especially for addressing this particular element of regulatory burden.

Bankers report that consumers rarely exercise the right of rescission. However, consumers do resent having to wait three additional days to receive loan proceeds after the loan is closed, and they often blame the bank for "withholding" their funds. Even though this is a statutory requirement, inflexibility in the regulation that makes it difficult to waive the right of rescission aggravates the problem. The restrictions should be rationalized to reflect consumer desires and modern-day realities. If not outright repealed, depository institutions should at least be given much greater latitude to allow customers to waive the right.

Identification of the Creditor. In addition to the right of rescission, community bankers have identified other problems under Regulation Z. In many lending arrangements the bank is not the only party involved in making the loan, creating difficulty and confusion in determining which entity is actually responsible for making the requisite disclosures. For example, banks often enter arrangements with car dealers to offer loan products but do not control the dealer's actions. These arrangements take a variety of formats and involve the bank in the credit at different stages of the process. However, the bank is likely to be held responsible for what the car dealer does or does not disclose, no matter when the bank became involved in the loan. The responsibility for disclosures when more than one creditor is involved should be more clearly outlined and defined so that banks understand when and to what extent they are expected to control the actions of counter-parties to a loan transaction.

Advertisements. Another problem under the Truth-in-Lending Act regulation involves how loan products may be advertised. From one perspective, advertisements help educate consumers about available loan products, but existing restrictions on what may be included and what must be included if a certain trigger term is used often limits the information actually included in advertising materials, meaning that consumers get less – not more – information. In some cases, the amount of information included can be virtually meaningless. While the intent is to encourage consumers to visit the bank to get more detailed information, the practical implications and market realities suggest that limiting information has the opposite effect. These restrictions should be greatly relaxed, if not eliminated. Banks are subject to the unfair and deceptive restrictions in section 5 of

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the Federal Trade Commission Act, and that standard should be more than sufficient for *all* bank advertising.

Finance Charges. The definition of the finance charge under Regulation Z is a primary example of unclear regulatory requirements. Assessing what must be included – or excluded – is not easily determined, especially when fees and charges may be levied by third parties. And yet, the calculation of the finance charge is critical in properly calculating the annual percentage rate (APR). Even if that hurdle is overcome, actually calculating the APR and knowing when it is permissible to use estimates is also confusing to bankers that work with these issues every day. Explaining them to customers that are not as familiar with banking is not easy and may actually be more confusing to customers. This process desperately needs simplification so that *all* consumers can understand the APR. These calculations are especially frustrating in an increasingly competitive environment where non-depositories use sleight-of-hand to exclude certain items from the APR (bankers often point to auto dealers' advertisement of 0% APRs). The regulation and disclosures ought to be tested against focus groups made up of average consumers and revised until easily understood by consumers.

New or Revised Disclosures. Once initial disclosures have been provided, there may be a lapse in time between loan approval and loan closing, especially for real estate loans. As a result, there can be changes in the structure of the final loan, and is not always clear when these changes mandate new disclosures. Similarly, it is not always clear when a change in an existing account relationship, as with a credit card account, requires a change-in-terms notice. Clearer rules or guidance on when new disclosures must be made is needed.

Real Estate Loans. Real estate loans create their own additional problems under Regulation Z. For example, the requirements for the early disclosures under Regulation Z are not in synch with the requirements under HUD's RESPA requirements, and yet woe to the banker that does not get it right. The requirements should be coordinated.

Many consumers complain about the volume of documents required for real estate loan closings, and the volume and extent of disclosures has gotten so extensive as to provide little meaningful information. If a simplification process is to succeed, one set of coordinated rules for real estate loans is needed – not a variety of regulations issued by different agencies.

Real estate mortgage transaction disclosures should be simple and easy to understand, clearly specifying the obligations and responsibilities of all parties. Disclosures should focus on the information consumers want most: the principal amount of the loan, the simple interest rate on the promissory note, the amount of the monthly payment and the costs to close the loan. Information should be provided to consumers at the appropriate stage of a transaction to allow them to make informed decisions. One set of rules should govern all mortgage lenders, and regulation, supervision and enforcement must be consistent across the industry.

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Credit Card Loans. For credit card loans, the requirements under Regulation Z and Regulation E (Electronic Funds Transfers) should be reconciled. Instead of two different regulations, it would be easier if the Federal Reserve established one regulation for credit cards that covered all requirements. In addition, regulatory restrictions requiring resolution of billing-errors within the given and limited timeframes are not always practical. The timeframes should be expanded to allow banks to investigate and resolve errors. Moreover, the rules for resolving billing-errors are heavily weighted in favor of the consumer, making banks increasingly subject to fraud as individuals learn how to game the system, even going so far as to do so to avoid legitimate bills at the expense of the bank. There should be increased penalties for frivolous claims and more responsibility expected of consumers.

Restitution. Recognizing the complexity of the disclosure requirements, if there have been inadvertent errors by the bank in making disclosures, greater flexibility should be allowed so banks do not have to review large numbers of consumer files and possibly make restitution of only a few cents: the costs for such actions certainly far outweigh the minimal benefits to the individual consumer.

Equal Credit Opportunity Act (Federal Reserve Regulation B)

Regulation B creates a number of compliance problems and burdens for banks. Knowing when an application has taken place is often difficult because the line between an inquiry and an application is not clearly defined. To answer customer questions about loan products, bankers must have sufficient information to respond correctly, and yet having too much information can lead to an "application" that triggers additional responsibilities on the part of the bank. While bankers want to provide customer service, the regulations make it difficult, and almost mandate a written application in all instances. This should be rationalized to reflect modern technologies and to prevent barriers to customer service.

Spousal Signature. A related issue that creates problems for all creditors is the issue of when to require the signature of a spouse. This can be especially problematic for small business loans when the principal of the business and his or her spouse guarantee the loan. Instead of allowing banks to accommodate customer needs and provide customer service, the requirements make it difficult and almost require that all parties – and their spouses – come into the bank personally to fill out the application documents. This makes little sense as the world moves toward new technologies that do not require physical presence to apply for a loan.

Adverse Action Notices. Adverse action notices present another problem—one that promises to be aggravated by new requirements under the Fair and Accurate Credit Transactions (FACT) Act. It would be preferable if banks could work with customers and offer them alternative loan products if they do not qualify for the type of loan for which they originally applied. However, doing so may trigger requirements to supply adverse action notices. And knowing when to send an adverse action notice is not always readily

determined. For example, it may be difficult to decide whether an application is truly incomplete or whether it can be considered "withdrawn."

Moreover, the requirements for adverse action notices under Regulation B are not always in synch with the requirements under the Fair Credit Reporting Act (FCRA). And, while there may be more than one reason that the loan was denied, determining what reason to provide on the adverse action notice form may not be simple. A simple straightforward rule on when an adverse action notice must be sent – that can easily be understood – should be developed.

The real danger is that it could become much easier for banks to deny an application instead of working with customers to find a suitable loan product. In such cases, it will be low- and middle-income loan applicants or those that are marginal or have problem credit histories that will be most negatively affected.

Other Issues. Regulation B's requirements also complicate other aspects of customer relations. For example, to offer special accounts for seniors, a bank is limited by restrictions in the regulation. And, most important, reconciling the regulation's requirements not to maintain information on the gender or race of a borrower and the need to maintain sufficient information to identify a customer under section 326 of the USA PATRIOT Act is difficult and needs better regulatory guidance.

Home Mortgage Disclosure Act (HMDA) (Federal Reserve Regulation C)

Exemptions. The HMDA requirements are the one area under the current regulatory review that does not provide specific protections for individual consumers. Rather, HMDA is primarily a data-collection and reporting requirement and therefore lends itself much more to a tiered regulatory requirement that places fewer burdens on smaller institutions. The current exemption for banks with less than $33 million in assets is far too low and does not make sense in today's banking environment, especially when there are banks with well over $1 *trillion* in assets. This exemption should be increased to at least $250 million, if not higher.

A second problem is the definition of an MSA (metropolitan statistical area). Since the definition of an MSA also determines which banks must report under HMDA, the banking agencies should develop a definition that applies to banks. Instead, banks are subject to a definition created by the Census Bureau for entirely different reasons. As a result, banks in rural areas and that should not be covered by HMDA reporting requirements may be captured by rules that do not reflect the reality of banking. Although the ICBA has often been a proponent of consistency in regulatory definitions, HMDA reporting requirements should be developed by the banking agencies and not subject to rules developed by other agencies that are establishing definitions for completely different criteria.

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Volume of Data Required. For banks that are subject to HMDA requirements, the volume of the data that must be collected and reported is clearly burdensome, and has been identified by bankers as one of the top ten regulatory burdens. Consumer activists are constantly clamoring for additional data, and the recent changes requiring collection and reporting of yet more data succumb to their demands without a clear cost-benefit analysis. All consumers ultimately pay for the data collection and reporting. Moreover, collecting some of the information, such as data on race and ethnicity, can be offensive to some customers who hold the bank responsible. Clearly, better cost-benefit analysis is needed in assessing the volume of data required under HMDA, with clear demonstration of the utility that justifies the costs involved.

Specific data collection requirements are difficult to apply in practice and therefore add to regulatory burden and the potential for error. Bankers report expending precious resources to constantly review and revise the HMDA data to ensure accurate reporting. Some of these problems are:

- Knowing which loans are refinancings
- Assessing loans against HOEPA (the Home Owners Equity Protection Act)
- Determining the date the interest rate on a loan was set
- Comparing Treasury yields against loan rates when maturity of loan does not match existing Treasury securities
- Determining physical property address or census tract information in rural areas
- Determining lien status (first, second, third)
- Coordinating reasons for denial with requirements for Reg B adverse action notice
- Constant review and updating of information collected for reporting

These problems should be addressed, whenever possible by eliminating the data requirement, and regulatory guidance in this area should be clear and easily applied. The current complexity and difficulty in applying existing guidance to daily operations merely adds to the level of burden and cost.

Finally, bankers report encountering conflicts between the data required under HMDA and the data that must be collected and reported under ECOA. The two data collection requirements should be reconciled and coordinated so that there is only one set of data-collection rules that apply to the race, age, ethnicity and gender of borrowers.

Flood Insurance

Flood insurance is another one of the top ten regulatory problems identified by bankers. The current flood insurance regulations create difficulties with customers, who often do not understand why flood insurance is required and that the federal government – not the bank - imposes the requirement. The government needs to do a better job of educating consumers to the reasons and requirements of flood hazard insurance.

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For bankers, it is often difficult to assess whether a particular property is located in a flood hazard zone since flood maps are not easily accessible and are not always current. Even once a property has been identified as subject to flood insurance requirements, the regulations make it difficult to determine the proper amount, and customers do not understand the relationship between property value, loan amount and flood insurance level. Once flood insurance is in place, it can be difficult and costly to ensure that the coverage is kept current and at proper levels. As a result, many banks rely on third party vendors to assist in this process, but that adds costs to the loan. Flood insurance requirements should be streamlined and simplified to be understandable.

Additional Comments

It would be much easier for banks, especially community banks that have limited resources, to comply with regulatory requirements if requirements were based on products and all rules that apply to a specific product consolidated in one place.

Second, regulators require banks to provide customers with understandable disclosures and yet do not hold themselves to the same standard in drafting regulations that can be easily understood by bankers.

Third, banks must constantly document everything to demonstrate compliance. For example, even though regulations may not require customer signatures on documents, banks feel constrained to obtain the signature for everything to demonstrate compliance. A good example is the Truth-in-Lending disclosures under Regulation Z.

Finally, many consumer-lending rules also require banks to post notices in branch lobbies, in addition to providing individual notices to customers. These notices, sometimes called "federal wallpaper" have become so extensive that they take up a great deal of space and yet are ignored by the great majority of consumers that enter the branch; the agencies should survey the public to assess whether these notices are truly worth the cost and whether they provide any benefit to the typical consumer.

Proper Allocation of Regulatory Resources. Outside of specific problems with the regulations being reviewed, additional problems are associated with examination for compliance with these and other regulations. Community banks and large, national or regional banks pose different levels of risk to the banking system. The ICBA strongly urges Congress and the agencies to continue to refine a tiered regulatory and supervisory system that recognizes the differences between community banks and larger, more complex institutions. A tiered regulatory system allocates the costs of regulatory/paperwork burden relative to the risk of the institution and helps restore equity in regulation, leveling the playing field and enhancing customer service. Just as banks are urged to focus resources to address the greatest risks, regulators and examiners should reallocate resources to the largest banks that pose the greatest systemic risk. ICBA strongly supports a better allocation of supervisory and regulatory resources away from community banks and towards larger institutions that present systemic risk.

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From time to time, Congress and the agencies have instituted welcomed regulatory and supervisory policies that lighten the regulatory and paperwork burden for community banks. Examples include: less frequent safety and soundness exams for small, healthy banks; streamlined, risk-focused exam procedures for noncomplex banks; streamlined CRA exams for small banks; and less frequent CRA exams for small, well-rated banks. Nonetheless, bank regulators devote disproportionate resources to examination and supervision of community banks. For example, one agency, the Federal Reserve, devotes 75% of supervision time to banks with less than $10 billion in assets, yet these banks only hold 30% of aggregate assets and are unlikely to pose systemic risk. Legislators and regulators should address these disparities to better allocate examiner resources and reduce unnecessary burden for community banks.

It also is critical that the regulatory agencies redouble efforts to ensure that the directions given to banks by examiners on consumer lending compliance is consistent with directions from agency headquarters, as too frequently this is not the case now. And, examiners must be allowed and encouraged to distinguish inadvertent errors that may occur under a good faith compliance program from a pattern or practice of violations.

Conclusion

ICBA members are integral to their communities. Their close proximity to their customers and their communities enables them to provide a more responsive level of service than megabanks. However, regulatory burden and compliance requirements are consuming more and more resources, especially for community banks. The time and effort taken by regulatory compliance divert resources away from customer service. Even more significant, the community banking industry is slowly being crushed under the cumulative weight of regulatory burden, causing many community bankers to seriously consider selling or merging with larger institutions, taking the community bank out of the community.

The ICBA urges the Congress and the regulatory agencies to address these issues before it is too late. This is especially true for consumer lending rules, which, though well intentioned, too often merely increase costs for consumers and prevent banks from serving customers. The fact that banks and thrifts are closely examined and supervised should be taken into account in the regulatory scheme, and depository institutions should be distinguished from non-depository lenders.

The ICBA strongly supports the current efforts of the agencies to reduce regulatory burden, and looks forward to working with the agencies to ameliorate these burdens and in developing a report to Congress on how statutory changes might be made to ensure that the community banking industry in the United States remains vibrant and able to serve our customers and communities.

Thank you for the opportunity to comment. If you have any questions or need any additional information, please contact Robert Rowe, ICBA's regulatory counsel at 202-659-8111 or robert.rowe@icba.org.

Sincerely,

Dale L. Leighty
Chairman