Testimony of

Thomas P. Boyle

On behalf of the

American Bankers Association

before the

Subcommittee on Economic Growth, Tax and Capital Access

of the

Committee on Small Business

United States House of Representatives

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Chairman Walsh, Ranking Member Schrader, and members of the Subcommittee, my name is Thomas Boyle, Vice Chairman of State Bank of Countryside, Countryside, IL. State Bank of Countryside was chartered in 1975 to meet the needs of local families and their businesses. We are an $800 million commercial bank with 6 offices and 105 employees. We serve the Chicago area market, with a population of approximately 4 million people. I appreciate the opportunity to present the views of the American Bankers Association (ABA) on the state of community banking and our ability to meet the needs of small businesses in our communities. ABA represents banks of all sizes and charters and is the voice of the nation's $13 trillion banking industry and its two million employees.

At my bank, as is true of my banker colleagues around the country, we are intensely focused on building and maintaining long-term relationships with our customers. In fact, State Bank of Countryside was founded with the motto "The Family Owned Bank for Families and Their Businesses," to convey the relationship the Bank has with our customers. We view our customers not as numbers but as individuals and business owners. As a family business, we understand the financial needs and concerns faced in our customer's personal and business lives, and we believe that the success of State Bank of Countryside is inextricably linked to the success of the communities we serve. They are, after all, our friends and neighbors.

Let me give you just a glimpse of the State Bank of Countryside's close ties with our communities. Over the years the Bank has specialized in lending to in-fill builders and small, family-owned businesses ranging from plastic injection molding to the local insurance agent. We have also participated in the SBA 504 Program and continue to do so under the new refinancing guidelines. In the Spring of 2011 we used this program to finance a restaurant acquisition ($3 million).

Not only do we provide the funding to meet the credit needs for our communities, our people are truly a part of these communities. A good example of this is our relationship with Christ the King Jesuit College Prepartory Schools, which serves young men and women from Chicago's Austin neighborhood and its surrounding communities on the west side of the city. The school has a corporate work study program designed to introduce inner city students to the business world under the guidance of a professional and designated staff. The program partners with Chicago area businesses to fill one or more full time entry-level jobs, while modifying the academic schedules of the students so that they do not miss class. The students who participate in the program earn up to 65% of their tuition, which not only allows them to take ownership of their education but also builds their professional skills. Our bank has participated in this program for the past three years, and has four students who job-share a full-time teller position.

Another good example is our Small Dollar Loan Program. We launched this program in 2008 in conjunction with the Citizenship Micro-loan, which is offered to individuals applying for United States citizenship. No application fee or credit history is required, so it brings new opportunities to a potentially challenged subset of our community.

In January 2011, we partnered with Operation Hope, using their curriculum to reach children in low income schools in Chicago's inner city neighborhoods. Operation Hope provides the school contacts and our employees provide the "teaching" component that brings the students the concept of Save, Spend and Share and helps them understand the difference between "needs" and "wants." In addition, for the past decade, our employees have participated in the ABA's "Teach Children to Save" program. Each spring our employees provide 18-20 hours of classroom instruction.

I believe that these initiatives demonstrate that when a bank sets down roots, communities thrive. A bank's presence is a symbol of hope, a vote of confidence in a town's future. The health of the banking industry and the economic strength of the nation's communities are closely interwoven. We strongly believe that our communities cannot reach their full potential without the local presence of a bank – a bank that understands the financial and credit needs of its citizens, businesses, and government. However, I am deeply concerned that this model will collapse under the massive weight of new rules and regulations. The vast majority of banks never made an exotic mortgage loan or took on excessive risks. They had nothing to do with the events that led to the financial crisis and are as much victims of the devastation as the rest of the economy. We are the survivors of the problems, yet we are the ones that pay the price for the mess that others created.

Banks are working every day to make credit and financial services available. Those efforts, however, are made more difficult by regulatory costs and second-guessing by bank examiners. Combined with hundreds of new regulations expected from the Dodd-Frank Act, these pressures are slowly but surely strangling traditional community banks, handicapping our ability to meet the credit needs of our communities.

Managing this mountain of regulation will be a significant challenge for a bank of any size. The median-sized bank has only 37 employees – for them, and even for banks like mine with 105 full time employees, this burden will be overwhelming. Right now, our bank is seeking proposals from three outside compliance consulting firms to enhance what we believe to be an existing robust compliance program. But the new regulatory obligations mean more regulatory scrutiny, which can include penalties and fines. All of these expenditures take away precious resources that could be better used serving the community.

The consequences are real. Costs are rising, access to capital is limited, and revenue sources have been severely cut. It means that fewer loans get made. It means a weaker economy. It means slower job growth. With the regulatory over-reaction, piles of new laws, and uncertainty about government's role in the day-to-day business of banking, meeting local community needs is difficult at best.

Without quick and bold action to ***relieve regulatory burden*** we will witness an appalling contraction of the banking industry. Each bank that disappears from the community makes that community poorer.

In my testimony today, I'd like to focus on three key themes:

- ***New regulations increase the costs of doing business while limiting access to capital***

  Each new regulation, or change in an existing one, adds another layer of complexity and cost of doing business. The Dodd-Frank Act will add an additional, enormous burden, has stimulated an environment of uncertainty, and has added new risks that will inevitably translate into fewer loans to small businesses.

- ***New rules substitute Washington bureaucratic judgment for that of local bankers***
  Increasingly, the government has inserted itself in the day-to-day business of banking. The government should not be in the business of micro-managing private industry. Traditional banks tailor products to borrowers' needs in local communities, and prescriptive rules inevitably translate into less access to credit and banking services.

- ***The consequences for consumers, small businesses, and the economy are severe***
  The Dodd-Frank Act will raise costs, reduce income, and limit potential growth, all of which drives capital away from banking, restricts access to credit for individuals and business, reduces financial resources that create new jobs, and retards growth in the economy.

I will discuss each of these in detail in the remainder of my testimony.

I. New Regulations Limit Access to Capital While Increasing the Costs of Doing Business

Capital is the foundation upon which all lending is built. Having sufficient capital is critical to support lending and to absorb losses when loans are not repaid. In fact, $1 worth of capital supports up to $10 in loans. Most banks entered this economic downturn with a great deal of capital, but the downward spiral of the economy has created losses and stressed capital levels. Not surprisingly, when the economy is weak, new sources of capital are scarce.

The timing of the Dodd-Frank limitations on sources of capital could not have been worse, as banks struggle to replace capital used to absorb losses brought on by the recession. While the market for trust preferred securities (which had been an important source of capital for many community banks) is moribund at the moment, the industry needs the flexibility to raise capital through various means in order to meet increasing demands for capital. Moreover, the lack of readily available capital comes at a time when restrictions on interchange and higher operating expenses from Dodd-Frank have already made building capital through retained earnings more difficult.

These limitations are bad enough on their own, but the consequences are exacerbated by bank regulators piling on new requests for even greater levels of capital. In conversations with fellow community bankers, I often hear how regulators are pressing many banks to increase capital-to-assets ratios by as much as 4 to 6 percentage points – 50 to 75 percent – above minimum standards.

For many banks, it seems like whatever level of capital they have, it is not enough to satisfy the regulators. This is excess capital not able to be redeployed into the market for economic growth.

Thus, to maintain or increase capital-to-assets levels demanded by the regulators, these ***banks have been forced to limit, or even reduce, their lending.*** The lack of access to capital has caused many banks to become smaller in order to ensure the banks maintain specific capital ratios. The result: loans become more expensive and harder to get.

Ever-increasing demand for more capital puts a drag on the economy at the worst possible time for our nation's recovery. Moreover, it works at cross-purposes with banks' need for the strong and sustainable earnings that will be the key to addressing asset quality challenges. ***Therefore, anything that relieves the increasing regulatory demands for more capital will help banks make the loans that are needed for our nation's recovery.***

At the same time the Dodd-Frank Act decreases access to capital, it increases compliance burdens. The Dodd-Frank Act will have an enormous and negative impact on all community banks and their ability to make small business loans. Already there are nearly ***2,000 pages*** of new proposed rules and there will be many thousands more as the 200+ rules under the Act are promulgated. This is on top of the 50 new or expanded regulations affecting banks over the two years leading up to the enactment of the Dodd-Frank Act. This flood of new regulations is so large that regulators are urging banks to add new compliance officers to handle it.

State Bank of Countryside is typical of many community banks in the U.S., and I know how demanding the crush of paperwork is for my staff. It is hard enough to deal with one new regulation or a change in an old one, but with reams of new proposals and reams of final regulations, it is overwhelming. We used to close many of our loans internally with our loan officers assuring compliance with all the requirements. Now, we are very likely to seek outside help to ensure that we are in compliance through increased testing of the loan portfolio.

Managing compliance with these new requirements adds time and costs – all of which makes it more difficult and costly to make loans to our customers. It is a sad commentary when our investment dollars this year and next – and probably longer – will be spent on compliance with the Dodd-Frank Act rather than making new loans, products and services available. There are many community banks smaller than mine, and I cannot imagine the pressure they face with fewer employees. The cumulative burden of hundreds of new or revised regulations may be a weight too great for many smaller banks to bear.

Businesses – including banks – cannot operate in an environment of uncertainty. Unfortunately, Dodd-Frank increases uncertainty for banks, and as a consequence, raises credit risks, raises litigation risks and costs (for even minor compliance issues), leads to less hiring or even a reduction in staff, makes hedging risks more difficult and costly, and restricts new business outreach. All of this translates into less willingness to make loans.

One major uncertainty is the additional regulatory requirements that will be expected once the Bureau of Consumer Financial Protection (CFPB) becomes fully operational. One of the claims was that small banks would be exempt from the new CFPB. ***But small banks are <u>not</u> exempt.*** All banks – ***large and small*** – will be required to comply with rules and regulations set by the CFPB, including rules that identify what the CFPB considers to be "unfair, deceptive, or abusive." Moreover, the CFPB can require community banks to submit whatever information it decides it "needs." There are also many other new regulatory burdens flowing from the Dodd-Frank Act empowerment of the CFPB which will add considerable compliance costs to every bank's bottom line. Adding such a burden on banks that had nothing to do with the financial crisis constitutes massive overkill. In the end, this cumulative burden will only impede fair competition among trusted providers seeking to serve responsible customers.

Much needs to be done to reverse the burdens Dodd-Frank threatens to impose through the CFPB. We support the efforts of the House Financial Services Committee, which passed three bills that would help:

- ***H.R. 1121***, which establishes a five-member, bipartisan commission to lead the CFPB, instead of a single director.
- ***H.R. 1315***, which clarifies that the Financial Stability Oversight Council (FSOC) must set aside any CFPB regulation that is inconsistent with the safe and sound operations of U.S. financial institutions. In addition, the bill would change the vote required to set aside regulations from two-thirds of the FSOC's voting members to a simple majority.
- ***H.R. 1667***, which delays the transfer date to for the CFPB until a Senate-approved director is in place.

In addition to these important initiatives, ABA recommends the following steps as only a beginning:

- Eliminate the expansive definition of "abusive" practices since appropriate use of existing unfair and deceptive practices authority is more than adequate;

- Prohibit Attorneys General from enforcing federal standards subject to federal supervision, or at least limit such actions to remedy only conduct occurring after the last CFPB or prudential regulator examination; and
- Prevent States and prudential regulators from augmenting or interfering with consumer protections otherwise covered by CFPB rules.

II. Individual Rules Substitute Washington Bureaucratic Judgment for That of Bankers in Local Communities

Increasingly, the government has inserted itself in the day-to-day business of banking. Micro-managing private industry should not be the role of government. Inevitably it leads to negative unintended consequences. The most egregious example is the price-controls for interchange fees being promulgated by the Federal Reserve under the Durbin Amendment.

The loss of interchange income will certainly mean higher costs of using debit cards. Greater mortgage restrictions and the lack of certainty on safe harbors for qualified mortgages means that community banks may no longer make mortgage loans or certainly not as many. Higher compliance costs mean more time and effort devoted to government regulations and less time for our communities. Increased expenses often translate into layoffs within the bank, and although we have not had any layoffs, our full time employees are down by 7 due to a hiring freeze.

Banks have always accepted the operational, reputational, and financial risk associated with developing new products and services and making them available to millions of consumers. Now financial institutions risk losing their investments of billions of dollars into improvements of existing products and services, and the creation of new ones, through government price controls. Why would any business invest in an innovative product knowing the government ex post facto will interfere and completely dismantle its free-market business model by imposing price controls? The Durbin Amendment serves as a strong ***disincentive*** for innovation and investment by financial institutions in other emerging payment systems and financial products and services. In the end, it is the American public who suffers.

III. The Consequences for Consumers, Small Businesses, and the Economy are Severe

Banks have to be profitable and provide a reasonable return to investors. If they do not, capital quickly flows to other industries that have higher returns. The Dodd-Frank Act, in combination with intense regulatory over-reaction, has increased expenses, decreased potential revenue, and limited community bank access to capital. Added to greater uncertainty about new regulatory and legal risks, these pressures directly take resources away from the true business of banking – making loans in local communities – the loans that should be going to families in my community and their family businesses.

Certainly, I want my bank to be successful, as do all of my fellow bankers throughout the country. Every day, we are facing new challenges that threaten our very existence. But for community banks, it goes beyond just our parochial interests. We are very much a part of our community. It is why every bank in this country volunteers time and resources to make their communities better. If the relentless pressures on our small banks are not relieved, the loss will be felt far beyond the impact on any bank and its employees. It will mean something significant has been lost in the community once served by that bank.

Thus, jobs and local economic growth will slow as impediments inevitably reduce the credit that can be provided and the cost of credit that is supplied. Fewer loans mean fewer jobs. Access to credit will be limited, leaving many promising ideas from entrepreneurs without funding. Capital moves to other industries, further limiting the ability of banks to grow. Since banks and communities grow together, the restrictions that limit one necessarily limit the other.

Lack of earning potential, regulatory fatigue, lack of access to capital, limited resources to compete, inability to enhance shareholder value and return on investment, all push community banks to sell. The Dodd-Frank Act drives all of these in the wrong direction and is leading to consolidations. The consequences for local communities are real.

State Bank of Countryside will survive these changes. I fear that many other community banks may not. I have spoken to many bankers throughout the country who describe themselves as simply miserable. Some have already sold their banks; others plan to do so once the economic environment improves. The Dodd-Frank Act was intended to stop the problem of too-big-to-fail, yet now we have even bigger institutions; ironically, the result may be that some banks will be too-small-to-survive the onslaught of the Dodd-Frank rules.

Conclusion

An individual regulation may not seem very oppressive, but the cumulative impact of all the new rules plus the revisions of existing regulations is oppressive. The regulatory burden from Dodd-Frank and the excessive regulatory second-guessing must be addressed in order to give all banks a fighting chance to maintain long-term viability and meet the needs of local communities everywhere.

It is important to understand that our bank – indeed, any small business – can only bear so much. Most small banks do not have the resources to easily manage the flood of new rules. Higher costs, restrictions on sources of income, limits on new sources of capital, regulatory pressure to limit or reduce lending in certain sectors, all make it harder to meet the needs of our communities. Ultimately, it is the customers and community that suffer along with the fabric of our free market system.