WHO'S IN YOUR WALLET? DODD-FRANK'S IMPACT ON FAMILIES, COMMUNITIES, AND SMALL BUSINESSES

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

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WHO'S IN YOUR WALLET? DODD-FRANK'S IMPACT ON FAMILIES, COMMUNITIES, AND SMALL BUSINESSES

Thursday, July 19, 2012

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Randy Neugebauer [chairman of the subcommittee] presiding.

Members present: Representatives Neugebauer, Fitzpatrick, Pearce, Posey, Renacci, Canseco, Fincher; Capuano, Baca, Miller of North Carolina, and Carney.

Ex officio present: Representative Frank.

Also present: Representative Green.

Chairman NEUGEBAUER. The Subcommittee on Oversight and Investigations will come to order. Today's hearing is entitled, "Who's in Your Wallet? Dodd-Frank's Impact on Families, Communities, and Small Businesses." I want to thank our witnesses for being here today, particularly Mr. Purcell, who is from the 19th Congressional District of Texas.

Thank you for being here this morning.

There are a lot of different ways that the government can get in your pocket, and I think most people think about taxes as the primary way because basically the government gets to determine how much of your hard-earned money you get to keep. But what I think a lot of people underestimate is the cost of other ways that the government does that through regulations.

I think one of the things that this Congress has been trying to focus on for a number of months now is jobs in this country. We still have a number of Americans who are out of work and we are looking for ways to help get those people back to work.

For example, in my State of Texas, about 98 percent of the employers in Texas are small businesses. I will tell you, in the 19th Congressional District, that is probably a higher number, because we just have a bunch of really hard-working small business people, many multi-generational businesses that have worked hard to build those businesses up. We don't have a big Toyota plant in the 19th Congressional District. But these small businesses are a major job creator for us.

And so what small businesses rely on is access to capital, and obviously our community banks have been the primary provider of that capital. When you look at the small business loans in this country, most of those loans are under $100,000. And while that is not a small amount of money, for many banks that would be a relatively small loan.

But to those businesses it is a very important loan, and so we want to make sure that as we move forward, we are not part of the problem of inhibiting the financial communities, particularly our community banks, from providing important lending opportunities, but also serving the customers. I was talking to someone the other day, and in many of the smaller communities across my district, with the consolidation that has happened in the agricultural business, there is a smaller number of farmers farming a lot more acres. And so a lot of those communities that used to be a lot larger because there were more farm families are smaller now. And in many cases, the small community bank is one of the last large corporate citizens in those communities, and is important not only as a provider of capital but for other financial services for those individuals.

What I am hoping to accomplish with this hearing today is that I think there has been a lot of focus on Wall Street, but what we really know is that Main Street is where ultimately all of the cost and burden of regulation tends to fall. We don't think about the fact that we raise the cost of the asphalt in the parking lot at the supermarket if we begin to tinker with some of these markets, or that the cost of buying or financing a car, the cost of your groceries, the commodities, and the availability of certain banking services where in many cases those used to be provided free now are at a cost.

And so, there are costs to that. What I would hope to accomplish with this hearing today is to begin to identify some of these costs because I think on both sides of the aisle, we want to make sure that if we want to have regulation, we need to understand the consequences of that regulation. But also, we have had a lot of discussions about the cost and the benefit. You can make a car really, really, really safe, but if it costs $100,000 to make a car really, really safe, then how many people can afford the car?

So I look forward to our discussion and our panel. I think we have a great panel today, and I want to thank you again for being here.

And with that, I will now yield to the ranking member of the subcommittee, Mr. Capuano.

Mr. CAPUANO. Thank you, Mr. Chairman.

And again, I want to thank the witnesses for being here as well. I know that some of you had to travel a long distance and I appreciate your efforts.

I look forward to this hearing and the other hearings that are scheduled this week, as well. Again, Dodd-Frank—I don't think anyone would suggest that Dodd-Frank was a perfect bill, certainly not by my measure, but perfection is really never the measure of anything. If it was, none of us would be elected, except of course for Randy—he might be, but the rest of us wouldn't be.

And so therefore, we have to look for the cost-benefit analysis, as was said. But at the same time, costs are easy to measure. How much does it cost to hire a new person to do regulation? And that is a fair and important thing to look at.

Benefits, on the other hand, are a little bit more difficult to measure. What are the benefits not just to the individual institution but also the economy as a whole? That is almost impossible to measure.

And I fear that some people are suffering under a little problem of amnesia. Secretary Geithner wrote a nice little article in The Wall Street Journal a couple of months ago that talked about the amnesia of people who forget how we got to where we are, what inspired Dodd-Frank. It didn't just come out of nowhere; it came out of a response to an economic crisis that was caused by a massive unregulated banking industry.

And I don't mean the regular banks like we all think of banks, but people who were totally unregulated in competition with regulated banks. They, as far as I am concerned, were more at fault than the regulated banks and they are now subject to some regulation.

They took excessive risk. They had no-document loans—just giving out loans to people with no documentation whatsoever. Totally unacceptable. Predatory lending. Credit default swaps squared, and tripled, and all kinds of things which I have actually not yet met a human being who really understands.

Off-balance sheet investments that nobody could find. Cozy relationships with regulators. Cozy relationships with credit rating agencies.

All of that led us to the second worst recession in American history. Let's not forget, we lost $19 trillion of household wealth—$19 trillion. It wasn't a small little bump, it was a big one: 9 million jobs lost, 10 million homes in foreclosure.

It required some sort of a reaction and Dodd-Frank was an attempt to do that. I don't think anyone would suggest that we have it perfect nor that anyone could get it perfect on the first draft.

And let's not forget that most of Dodd-Frank has not been implemented yet. It has not been implemented because of the normal course of time it takes to implement any new law and because of the attempts to cut back. As we are expanding the requirement responsibilities of the SEC, we are also—not we, but some people are proposing to cut their budget by 12 percent.

Also, massively increasing and expanding the responsibilities of the CFTC, and suggesting to cut their budget by over 40 percent. That is ridiculous. Of course you can't get things done when you are facing those situations.

Seventy-five years ago, this country faced the worst economic problem that we have ever had and immediately thereafter, in the middle of it, a lot of people cried, "Oh, my God. These regulations are going to kill everything," before most of them were implemented, by the way. And when they were implemented through the SEC and the other regulations that happened for 75 years we had the most stable economic environment in the history of mankind. We had the greatest expansion of economic wealth in the history of mankind.

And then we got into this thing: all regulation is evil; all regulation is terrible. Let me be very clear: No one in their right mind wants or supports excessive, overly burdensome regulation. No one that I know of would advocate for that, including me.

However, no one in their right mind should forget what we just went through and therefore argue that nothing should have happened. No one in their right mind should say that we should have too little regulation.

It is always an attempt to find a balance, and that is what I hope these hearings come up with is an attempt to yes, costs, but also some benefits—try to figure out what we have right, what we have wrong, and try to keep the good without throwing out the bad.

And with that, Mr. Chairman, I yield back. And thank you very much for having this hearing.

Chairman NEUGEBAUER. Yes. I thank the gentleman.

And now the vice chairman of the subcommittee, Mr. Fitzpatrick, is recognized for 2 minutes.

Mr. FITZPATRICK. Thank you, Mr. Chairman.

We are here today to examine how Dodd-Frank affects our constituents. Our constituents are everyday people who don't work on Wall Street, and who don't deal in complicated financial products or sit at trading desks of investment banks.

The law may have been designed to rein in Wall Street and regulate wealthier financiers, but the fact of the matter is that this 2,300-page bill reaches into the pockets of just about every American. A lot of people may be surprised to learn that Dodd-Frank rules govern commodities and could cause prices to rise in everything from airline tickets to a six-pack of beer.

There are also the effects of increased regulations on small financial institutions. Access to credit and even the ability to maintain a simple checking account could be jeopardized. Higher fees, increased costs, and reduced services are all naturally occurring byproducts of increased regulation, and these costs are not going to be borne simply by the customers of financial institutions but they are going to be felt across the economy because this bill crosses into so many areas of American life.

We should all expect a well-regulated financial system that is free of fraud and abuse and includes robust consumer protections. The 2008 crisis was an event that exposed flaws in our markets and should absolutely have led to policy changes. However, as happens so often in Washington, this opportunity to work together on needed reform resulted in a bill rife with unintended consequences.

So I look forward to today's hearing, and continuing to work with all of our colleagues on financial reform that does more good than harm.

I yield back.

Chairman NEUGEBAUER. I thank the gentleman.

And now the ranking member of the full Financial Services Committee, Mr. Frank, is recognized for 3 minutes.

Mr. FRANK. Thank you, Mr. Chairman. I am struck by what seems to me to be a nice irony in the title, "Who's in Your Wallet?" Borrowing—given the looseness of intellectual property constraints here—from Capital One's slogan, "What's in Your Wallet?" And we learned from one of the agencies that many on the panel wish never existed, the Consumer Financial Protection Bureau (CFPB), that what was in the wallet of many consumers were the hands of Capital One. So references to who is in whose wallet and for what purpose are very relevant to today's hearing.

The CFPB, in coordination with the OCC, just fined Capital One, which agreed to have—the fact that it had violated basic consumer rules. So yes, there are all kinds of people in the wallet.

I see the testimony here from the U.S. Chamber of Commerce. Deja vu. In 2006, I was the chairman-in-waiting of this committee and in December, I was asked to come to a session of the U.S. Chamber of Commerce in which the point was—this is 2006—we are overregulating the financial industry. And we were told that we had to cut back, that if we did not cut back on Sarbanes-Oxley, the likelihood of IPOs ever being issued in America would be substantially diminished. And of course, they could not have been more wrong.

One of the things we were told at the time by the Chamber and others was we should emulate the light touch regulation of the British Financial Services Authority, the people who have done, by their own admission, a fairly poor job of of not regulating when they should have regulated.

I look here and I see complaints that we are overregulating mortgages, and there is a complaint from some of the people, I think, in the credit unions and elsewhere that we are being too tough in requiring payment standards for people who are taking out mortgages. I confess that I am surprised to hear that complaint. Given the unfortunate role that was played by laxity in mortgage standards in helping to bring this crisis about, I am surprised by that.

I have also heard—I haven't seen it yet here—some complaints that the bill's requirement that those who securitize mortgages retain some of the risk is retarding mortgages. In fact, it is not in effect yet and it is not retroactive so it clearly cannot be blamed for retarding anything. But this resistance to tightening up mortgage standards is just odd to me, given what happened.

And then, from the Chamber we also have complaints about the overregulation of derivatives, as if there never was an AIG, as if the problems that recently surfaced with JPMorgan Chase and others hadn't existed.

We have done some refinements and I will do some more, but this wholesale rejection of regulation of the financial industry, I would have to say to my friends at the Chamber, going back to 2006, they remind me of the Bourbon, when the Restoration came in the 19th Century in France, and people said, they have forgotten nothing because they learned nothing. The notion that people would be repeating the argument in 2006 is really quite startling to me.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from Texas, Mr. Canseco, is recognized for 2 minutes.

Mr. CANSECO. Thank you, Mr. Chairman.

Mr. Chairman, before I came to Congress last year, I spent most of my life in the private sector in banking, in real estate, and in law. One thing that continues to amaze me is the complete disconnect between what goes on in Washington and the realities on the ground in our economy.

Two years ago, we were given a lot of promises about Dodd-Frank, but the one that sticks out the most is the one that this bill would "bring greater economic security to families and businesses across the country." All it takes is a 5-minute conversation with a community banker, a small businessman, or a credit-worthy family who can't get a loan to comprehend just how badly this promise has been broken.

The authors of Dodd-Frank told us that they had crafted reforms that were absolutely necessary, but when you pile hundreds of new rules on top of existing rules and give greater authority to the same regulators that missed the last crisis, calling it "reform," suffice it to say that is a little ambitious.

Mr. Chairman, the more we hear about Dodd-Frank the less there is to like, and I look forward to our committee's continued examination of this bill during today's hearing, and I yield back.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from California, Mr. Baca, is recognized for 2 minutes.

Mr. BACA. Thank you very much, Chairman Neugebauer, and Ranking Member Capuano, for calling this hearing.

And I also want to thank the witnesses for being here this morning. Thank you all.

It has been almost 2 years since the passage of the Dodd-Frank legislation, yet we have not had an opportunity to implement all aspects of the Frank-Dodd legislation. So as we begin to look at it, it seems like from the other side of the aisle they want less regulations, but we have to keep in mind that the regulations are good because we have to protect the consumer and the stockholders, such as what happened with JPMorgan in that area. If we don't have these regulations, then what is going to happen?

It is important that we continue to protect them, to assure that the consumer is protected, and the stockholders are protected in the area. And I think having the regulations are very important.

And while our economy has not yet fully recovered from the financial crisis that got us in this mess, I am proud that we now have the tools to prevent another crisis. That means having the tools to have the oversight and making sure that we have the enforcement. We have not done a lot of the enforcement that needs to be done.

And it is easy to say, let's not have these regulations. Well, look at what happened with the Supreme Court making the decision on independent expenditures that can be given out. Now, you have all kinds of independent expenditures that are going on, and everybody says, "I wish we could regulate them."

We need regulations. Regulations are important to a lot of us.

And again, when the situation was made about buying a car, or not having access to credit, we want to make sure that the individuals who are getting credit are able to pay for whatever they are borrowing to, as well, because that is taxpayer money that is being used, and we have to protect taxpayer money.

Instead, Congress needs to work together and—we need to all work together in trying to get our fiscal house in order, to com-promise by making spending cuts, find new resources of revenue to support our economy. With that in mind, I hope that we can strike a tune instead of focusing on partisan talking points, and that seems like what you have heard on both sides here.

Over reform, we need to stop the abuse and work together on trying to find solutions to make sure that we protect the American consumer and so they have more confidence in us.

With that, I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from New Mexico, Mr. Pearce, is recognized for 2 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

I am listening with interest to our friends on the other side of the aisle. I think my objection to what is occurring in Dodd-Frank is that regulators were sitting in the room with MF Global as they were making the decisions and no one said a word. Then, with JPMorgan, 57 regulators were in that building.

I think if we were to tighten up the regulations that were in place, and then if we need more that would be fine. But what I am hearing now in New Mexico is that the safety and soundness interviews are no longer preeminent. They have been replaced by the compliance reviews, and they are telling me if they make a clerical error, they could face a $50,000 fine for a clerical error on something in New Mexico.

Nobody in New Mexico caused the problem on Wall Street, and yet they are getting stuck with this regulation which causes—just this past weekend, I was visiting a small cabinetmaker in Grants, New Mexico. Grants is just decimated. Their economy is in horrible shape, and yet this guy—whose family started this little cabinet shop, his father did—couldn't get a $50,000 loan. He has plenty of equity, and he has never been late on payments, but he couldn't get a $50,000 loan to just kind of get him through these rough periods. So they are sitting there hiring fewer people, and laying people off.

We hear that across New Mexico and I will guarantee that none of the problems on Wall Street originated there, but when it came time to regulate, we regulated the Main Street small banks and we let, say, Fannie Mae and Freddie Mac go completely unregulated. And so those are my objections. I agree with the friends on the other side of the aisle that we should be sitting here discussing it, but let's hold the regulators accountable that are in the room allowing things to go on before we start laying on new regulations to people who weren't even involved in the problems.

I yield back my time. I thank the chairman for giving me the opportunity to speak.

Chairman NEUGEBAUER. I thank the gentleman.

I ask unanimous consent to make a letter from the Credit Union National Association a part of the record today. Without objection, it is so ordered.

We will now turn to our panel: Mr. Michael Flores, chief executive officer for Bretton Woods, Incorporated; Mr. Jim Purcell, chief executive officer, the State National Bank of Big Spring, Texas; Ms. Lynette Smith, president and chief executive officer, Washington Gas Light Federal Credit Union; Mr. Jess Sharp, managing director, Center for Capital Markets Competitiveness, U.S. Chamber of Commerce, on behalf of the Chamber and also the Coalition for Derivatives End-Users; Mr. Garrick "Gary" Johnson, president, American Flooring Installers, LLC, on behalf of the Ohio Hispanic Chamber of Commerce; Mr. David Min, assistant professor of law at the University of California Irvine School of Law; Ms. Deyanira Del Rio, chair of the board of directors, Lower East Side People's Federal Credit Union; and Mr. Gregory Smith, chief operating officer and general counsel, Colorado Public Employees' Retirement Association.

Without objection, your written statements will be made a part of the record, and you will be each recognized for 5 minutes to summarize your testimony.

Mr. Flores, you are recognized for 5 minutes.

STATEMENT OF MICHAEL FLORES, CHIEF EXECUTIVE OFFICER, BRETTON WOODS, INC.

Mr. FLORES. Thank you, Mr. Chairman.

And good morning, members of the committee.

My firm provides consulting and research services to commercial banks, credit unions, and alternative financial services providers. I have more than 30 years of experience in banking and consulting and have published several articles and studies on the financial services industry, including issues addressing overdrafts, short-term credit alternatives, and general purpose reloadable prepaid and payroll cards.

Because this hearing is about the consequences of Dodd-Frank on communities, small businesses, and individuals, I am here to describe both my analysis of the issue as well as to relate comments from my clients about their assessment.

In general, while there is a need to address the causes of the financial meltdown in 2008, there are aspects of Dodd-Frank that are having a disproportionate and negative impact on financial services providers that played no role in the financial crisis. Small businesses and the 60-plus million low- to moderate-income consumers are particularly impacted.

Contrary to making financial services more available, affordable, and consumer friendly, the increased restrictions and compliance costs are reducing services to small businesses and consumers, which ultimately has a negative impact on the economic well-being of the communities they serve. Additionally, many of the 6,700 community banks and 7,000 credit unions are burdened with legacy operating costs and dated technologies that inhibit their ability to profitably serve their customers. Local small businesses and LMI consumers—low- to moderate-income consumers—suffer as a result.

Resources that could be used to update technologies and create more efficient operations are now allocated to regulatory and compliance purposes. Both transaction accounts and credit options are impacted. Our own studies indicate that it is unprofitable for most banks and credit unions to individually underwrite loans under $5,000.

The traditional options of overdrafts, credit card advances, and home equity loans are less viable today because of the poor economy and regulations. With the reduction of overdraft and interchange fees, many banks have eliminated free checking accounts. The reduction of interchange fees has actually resulted in what I would term a wealth transfer from consumers to merchants.

I contacted several of my clients to solicit their feedback on these issues. I have listed their quotes in my written testimony but will summarize the thoughts here.

The consensus of the responses include, and it has been mentioned here by the Members: a substantial increase in compliance costs for banks and credit unions; increased fees for small businesses and consumers; decreased products and services; an increase in the number of underbanked, and now the new term "debanked" individuals; and a decrease in the number of branches in low- to moderate-income markets as banks attempt to reduce expenses.

Other more specific comments include, "Of the almost 400 rulemakings required by the law, only a quarter have been finalized, while 36 percent have not even been proposed." A significant decline in traditional wholesale purchasers of residential mortgages from mortgage bankers and brokers reduces access to mortgage credit, particularly for those without an established relationship with a bank."

Something very specific but mentioned several times was that the requirement to get new appraisals and updated credit reports on renewals and existing loans creates extra costs to the consumer. This requirement is regardless of the market or strength of the customer.

People talked about Section 1071 of Dodd-Frank having a chilling effect on small business lending. There are others that deal with unaffiliated network routing requirements on government benefits on prepaid cards as well as now the requirement to get State money transmitter licenses for prepaid card program managers. The remittance rule is going to drive up costs and reduce competition for consumer remittances to foreign countries.

And of course, the limited functionality of prepaid cards from large issuers—those banks over $10 billion in assets. As a matter of fact, Congressman Frank, in a letter to Fed Chairman Bernanke dated February of this year, states that the Board's decision to condition the reloadable prepaid card exemption from interchange fee restrictions on the card being the only means of access to the underlying funds associated with the card might inadvertently result in consumers not having access to useful features and services.

Dodd-Frank has layered significantly more regulations over existing regulations to the point of making the traditional business model for community banks and credit unions almost unworkable. At the same time it is creating roadblocks to innovators such as alternative financial services providers who are working diligently to address the underbanked segment of our society.

In essence, some provisions of Dodd-Frank are solutions looking for problems—problems that do not exist for the majority of financial institutions in this country.

Thank you, and I look forward to answering your questions.

[The prepared statement of Mr. Flores can be found on page 55 of the appendix.]

Chairman NEUGEBAUER. Thank you, Mr. Flores.

Mr. Purcell, you are recognized for 5 minutes. Thank you.

STATEMENT OF JIM R. PURCELL, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, THE STATE NATIONAL BANK OF BIG SPRING, TEXAS

Mr. PURCELL. Thank you, Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee. I am Jim Purcell, CEO of the State National Bank in Big Spring, Texas.

In order for you to understand a little bit about me, I was raised on a ranch in eastern New Mexico. I was about 20 miles from the town of San Jon, and for those who do not know where San Jon, New Mexico is, it is a bastion of 300 or 400 people and it is right between—or was when I was there—"Rest Stop" and "Resume Speed." So, it was not a very large place.

When I started the first grade, my teacher had some things to teach us, and one of the first things was, what do you do when you come to a railroad crossing? You stop, look, and listen.

I would humbly urge you to do the same with regard to this bank regulation, and more particular, to the Dodd-Frank Act. Currently this Act, and inclusion of the CFPB, has and will have implications on community banks across America, much more than what was stated when it was passed and much more than I could have dreamed would affect us.

In quoting Senator Dodd, "Community banks which were not responsible for the crisis will pay lower premiums for deposit insurance and continue to work with their existing regulators. And in a nation with more than 6,000 banks, the bulk of the bill's new regulations apply only to a few dozen of the largest ones."

Jennifer Kelly, Senior Deputy Comptroller for Mid-Size and Community Bank Supervision of the OCC stated, "Regardless of how well community banks adapt to Dodd-Frank Act reforms in the near to medium term, these new requirements will raise costs."

The President's Executive Order of January 18, 2011, urged independent agencies to propose a regulation only upon a reasoned determination that its benefits justify its cost. When the stated goals by both the proponents and opponents of Dodd-Frank disclosed that community banks weren't the problem and shouldn't be affected, we should have a clear starting point to undo the harm and consequences of this legislation.

State National Bank is over 100 years old. We have survived droughts, depressions, and recessions, and our motto after the 1930s bank holiday was "time-tried and panic-tested." We have had examples of time-tried and panic-tested recently in the last 4 or 5 years.

We have had customers who went out of business in the 1950s drought, and then came back in the 1970s and paid their obligations. We have had customers who sold all of their collateral and paid what they could on their notes in the mid-1980s during the Texas bad days and they are continuing to make payments with no collateral, never missing a payment for 24 years.

We have relied on our handshake for over 100 years. That is a commitment of trust and loyalty and commitment both to our customers and from our customers.

In the past, we have wired money to Europe, to a stranded foreign exchange student or to a retiree whose purse was stolen. We didn't know the exchange rate in Spain or France. We didn't know the fee that was being charged upon receipt. But we did know our customer needed help and we provided that.

This month, we had a customer who had a family problem and a need in Mexico. We could not wire him the money because we did not know the exchange rate or the fees which we would be charged if we abided by the proposed rule.

Our bank, through the years, has made consumer real estate loans to purchase and occupy the home in which they would live. We never sold the loans; we serviced the loans. We didn't charge any application fees, origination fees, or any other type of fee.

They were typically 5-year balloon notes, which under the proposal would not be allowed. We would have the customer put up 20 percent, and we would put up 80 percent.

If a customer paid his own taxes and insurance, if he paid as agreed, we would renew the loan, keeping the payment schedule the same. That is how it was then; that is not how it will be under the proposals.

Now, our customers have a dilemma: Where do we turn? Loyalty, service, our bank knowing our character, simple solution for simple needs will be the sacrifices.

They will end up getting toll-free numbers, and application fees. They will get to speak to more people with one problem than what we even employ at our bank.

And then the next question comes, do we move all of our business to that megabank? Our bank's compliance costs continue to increase with the CFPB. We are starting with 40 years worth of regulation and adding to that.

But who pays the price? When you disregard the needs of the community and the customer to make everyone the same, who suffers? The customer pays the price of additional compliance or the product will be sacrificed.

I would like to ask you to do the same thing that my first grade teacher, Ms. Olen, said: Stop, look, and listen. If we continue to disregard reality and stack regulation upon regulation with no thought of the consequences, we will not be able to cross the proverbial track to serve our customers.

I thank you for the time, and I hope that this makes a difference.

[The prepared statement of Mr. Purcell can be found on page 78 of the appendix.]

Chairman NEUGEBAUER. Thank you, Mr. Purcell.

Ms. Smith, you are recognized for 5 minutes.

STATEMENT OF LYNETTE SMITH, PRESIDENT AND CHIEF EXECUTIVE OFFICER, WASHINGTON GAS LIGHT FEDERAL CREDIT UNION, ON BEHALF OF THE NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS (NAFCU)

Ms. LYNETTE SMITH. Good morning, Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee. My name is Lynette Smith and I am testifying on behalf of NAFCU.

I serve as the president and CEO of Washington Gas Light Federal Credit Union in Springfield, Virginia. We have 8,000 members and we are $87 million in assets. Thank you for the opportunity to testify here today about the impact the Dodd-Frank Act has had on credit unions.

Credit unions were not the cause of the financial crisis. Still, they are significantly impacted by Dodd-Frank, such as being subject to the rulemaking authority of the new CFPB.

We are very concerned that efforts in Dodd-Frank to reign in bad actors and greed on Wall Street will inevitably have a negative impact on credit unions, especially when it comes to regulatory and compliance burdens. One of the biggest impacts Dodd-Frank has had on credit unions comes from the debit interchange price cap. Market forces have already seen some credit unions begin to have higher debit card costs and declining interchange revenue.

Many of the regulations flowing out of Dodd-Frank are well-intended. However, for credit unions, they are often a solution in search of a problem.

I cannot overemphasize how burdensome and expensive Dodd-Frank-related compliance costs will be for credit unions. We can only hope Congress will urge regulators to do more robust cost-benefit analysis of potential regulations and look for areas to streamline. More importantly, we hope that they will follow up once the regulations are in place and make changes if these costs are too high.

Washington Gas Light has a staff of 17. My employees and I already spend countless hours trying to comply with the never-ending changes to laws and regulations.

My credit union is healthy, growing, and we have very good loan demand. Still, rather than looking to hire a new loan officer, the growing compliance burden means that I must first look to hire a compliance officer. While we still try to make the loans to our members' needs, the staff time dedicated to compliance means that members have to wait longer for their loans.

Under the Dodd-Frank Act, the Financial Stability Oversight Council has a duty to facilitate regulatory coordination. We hope that you will take this duty seriously, for it is not any single regulation but an accumulation of regulations from numerous regulators operating independently of each other that magnifies the regulatory burden credit unions face today.

Attached to my written testimony is a letter NAFCU sent to Treasury Secretary Geithner last month on this issue. The CFPB remittance rule is nearly 800 pages and only exempts those making fewer than 25 transfers per year.

A NAFCU survey found that nearly 84 percent of those credit unions that provide remittances make more than 25 transfers a year and a majority of those barely break even or will have to operate at a loss. The new compliance costs for this rule may force many of the credit unions and financial institutions to eliminate this service.

The CFPB recently released its semi-annual regulatory agenda, which outlines 27 different areas where potential rulemaking may occur in the future. It will be very challenging for my staff because we are limited in resources. I am not sure how I will keep up.

In conclusion, while credit unions were not the problem, the Dodd-Frank Act impacts credit unions in many ways and it is increasing their regulatory burden. Congress must continue vigorous oversight and look for ways to act on regulatory relief. Regulators, on the other hand, must also accept responsibility for this regard and the newly created FSOC should make regulatory coordination part of its focus.

Thank you for your time, and for the opportunity to testify here before you today. I will welcome any questions you may have.

[The prepared statement of Ms. Smith can be found on page 100 of the appendix.]

Chairman NEUGEBAUER. Thank you.

Mr. Sharp, you are recognized for 5 minutes.

STATEMENT OF JESS SHARP, MANAGING DIRECTOR, CENTER FOR CAPITAL MARKETS COMPETITIVENESS, U.S. CHAMBER OF COMMERCE, ON BEHALF OF THE U.S. CHAMBER OF COMMERCE AND THE COALITION FOR DERIVATIVES END-USERS

Mr. SHARP. Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee, it is a pleasure to be here with you this morning.

My name is Jess Sharp. I am the managing director of the U.S. Chamber's Capital Market Center, and I am here today representing more than 300 end-user companies and dozens of trade associations that have been active in the Coalition for Derivatives End-Users. The Coalition represents companies across the economy in manufacturing, agriculture, energy, and other sectors all united in one respect: They use derivatives to manage risk, not to create it.

Throughout the legislative and regulatory processes of the Dodd-Frank Act, the Coalition has advocated for strong regulation that brings transparency and stability to the derivatives market while avoiding needless costs on end users.

So how do end users use derivatives and why is that relevant to consumers? Many auto manufacturers, for example, use derivatives to manage commodity, foreign exchange, and interest rate risk resulting from the design, manufacture, sales, and financing of vehicles. The price of commodities used in production, such as aluminum and copper, fluctuate with the market, so companies can use derivatives to lock in prices and long-term supply arrangements sometime years in advance of delivery.

On the revenue side, manufacturers that export their products need to hedge currency exposure that arises from production costs being in U.S. dollars and revenue in pesos, or Canadian dollars, or Euros, and they can use derivatives like foreign exchanges swaps to do that.

Auto manufacturers and other big equipment manufacturers—for instance, in the construction or agriculture world—also finance the sale of their products. Derivatives enable these companies to match the interest rate characteristics of the funding available from the capital markets to put together their loan portfolios with the financing needs of their customers.

The energy company members of the Coalition also rely on derivatives heavily because of the nature of the business of energy production and transmission. For example, in the case of electricity, which must be produced and consumed simultaneously, cannot be stored, and has huge exposure to fuel markets in coal, natural gas, and uranium, those physical energy markets are volatile and unpredictable, but hedging with derivatives allows energy companies to lock in prices and provide thousands of customers with electricity and natural gas at a low fixed price.

So these are just a few examples of the ways in which end users use derivatives, and I want to talk quickly just about the impact of Dodd-Frank and sort of where we are today. As I said at the top, the Coalition has been supportive of increased transparency in the OTC market and we are fully supportive of the overall move toward clearing and exchange trading. That is not something with which we have argued.

However, we do remain concerned that a few regulations that were never intended by Congress to affect Main Street companies will make derivatives either more expensive or altogether unavailable for end users.

Now, the good news is we have seen very, very strong bipartisan support for measures that would shield Main Street businesses from this kind of regulatory overreach. This committee has been a very good ally for end users.

And I would like to thank you for your hard work in passing two bills in particular through the House that have addressed some of these unintended consequences, or would if enacted. The first, H.R. 2682, which this committee approved unanimously and the full House approved 370 to 24, creates an exemption for margin requirements for nonfinancial businesses.

Imposing unnecessary margin requirements on these nonfinancial end users would divert working capital away from productive business use. And again, despite clear evidence that Congress did not intend for regulators to impose margin requirements on end users, the prudential banking regulators have proposed to do so, and this would be a huge capital drain from the economy and could be a jobs issue, as well.

And I would point out that this week, Chairman Bernanke did address this issue in testimony and said that he would be supportive of the legislation that has passed the House.

A survey by the Coalition, just to put a fine point on the impact here, found that imposing a 3 percent margin requirement on OTC derivatives could cause the loss of 100,000 to 120,000 jobs and reduce capital spending by up to $6.7 billion, and that is just extrapolated to the S&P 500. So the passage of H.R. 2682 in particular will help shield Main Street businesses from these huge cash calls that they are very concerned about, which could be a reality if these regulations are finalized as is.

The second bill, H.R. 2779, which this committee also approved unanimously and passed the full House 357 to 36, prevents internal interaffiliate trades from being subject to regulatory burdens that were intended to market-facing swaps and will ensure that companies are not forced to abandon hedging through central risk mitigation centers. These centralized risk mitigation centers generate economic savings by allowing U.S. companies to manage commercial risk more efficiently and secure better pricing for derivatives transactions. And this savings can be either passed on to consumers or they can use that savings to grow their businesses and create jobs.

The overwhelming bipartisan and collegial process that led to the passage of these two bills in the House demonstrates that these two bills provide noncontroversial approaches to helping grow businesses and improve the economy through end-user companies. So, we are hopeful that the Senate will take up and pass these bills quickly.

Ensuring that congressional intent is followed is paramount here, and if legislation is not enacted to clarify the statute's intent, end users could use the critical management tools, and that is bad for Main Street businesses, it is bad for their customers, and it is bad for the economy.

Thank you. I am happy to respond to your questions.

[The prepared statement of Mr. Sharp can be found on page 84 of the appendix.]

Chairman NEUGEBAUER. Thank you, Mr. Sharp.

Mr. Johnson, you are recognized for 5 minutes.

STATEMENT OF GARRICK "GARY" JOHNSON, PRESIDENT, AMERICAN FLOORING INSTALLERS, LLC, ON BEHALF OF THE OHIO HISPANIC CHAMBER OF COMMERCE

Mr. JOHNSON. Good morning, Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee. My name is Gary Johnson, and I am the owner, president, and CEO of a small but fast-growing construction business in Toledo, Ohio. It is called American Flooring Installers.

I am testifying today on behalf of the Ohio Hispanic Chamber of Commerce, where I am currently the chairman. The primary objective of our Chamber is to promote the development and continued growth of Hispanic businesses in the Ohio community. It is a pleasure to appear before you today.

In my testimony this morning, I want to tell you a little bit about my company and also provide you with a personal account of some of the ways in which I am using financial products and services to run and grow my business. I know that I am here to talk about the effects of regulation, but I hope to tell you about how my business works, and how I use financial products, to help you consider proposals for new regulations.

My company currently has 23 full-time employees and we had gross revenues in 2011 of approximately $1.8 million. I am looking forward to hiring additional workers and we are on track to double our revenues again this year. One part of meeting that goal is the financial products and services that we and our customers use.

A healthy financial sector is important for business of all sizes, especially businesses like mine. In the business community, many of us are concerned about the new financial sector law enacted by Congress, which is indirectly hurting small businesses through tighter lending practices and new increased fees and routine financial services for businesses and consumer banking customers.

Among the subjects that always seem to come up when I talk to other Chamber members is the challenge of cash flow. Many of us believe that the challenge is exacerbated by the law enacted by Congress in response to the financial crisis.

While less regulation in some areas has contributed to the necessity for government to act, overregulation has made it extremely hard to obtain the necessary funding needed to grow many small businesses. We are concerned that overregulation is making it harder for banks to make credit card loans to us and harder for our customers to use payment cards.

These cards are essential for cash flow on both the expense and revenue side of small business. Other options, such as lines of credit, either take too long to obtain or simply are not available. When I accept credit cards from my customers, I get paid faster, and the time-value of money means I get paid more, relatively speaking.

One tool that I am increasingly using to enhance my cash flow involves the acceptance of payment cards using a device attached to a mobile phone. This device allows me to accept the credit care and debit payments while I am face-to-face with a customer.

If I am out on a jobsite using this device, I know whether or not I am going to get my money within the next 3 days. If the payment is declined, I know about it right then and there, and I can address that with my customer. If authorization goes through, then I know I can put that money back to work within 3 days.

I accept anywhere between $2,500 to $10,000 per month on cards and it would be great if more of my customers paid me this way instead of sending a check. Again, accepting payment cards enables me to get paid typically within a few days.

This is light years faster than the invoice system I otherwise use that typically results in me receiving a payment from a customer by check, which takes as long as 60 to 90 days. Also, with payment cards, small businesses do not need to worry about bounced checks.

Even though I pay a fee to accept card payments, I prefer them as a payment method because I get access to funds almost immediately. That allows me to put the money back to work in my business in near real time. When I receive payment from my customers more quickly, I can put the money to work quickly in my growing business.

If you consider what I pay to accept payment cards as opposed to the cost of me essentially floating a loan to a customer for 60 to 90 days, when I could be putting the cash back to work in my business, it is a no-brainer. I have learned not from a book but from my business and about the time value of money. I want to keep going back to that because knowing time value of money is one of the keys to successfully growing your business.

The situation I just described hits me in two ways. Even if I was not growing business during the 60-to 90-day period, I have to wait to have the invoices paid by check. I have to pay the employees who work for the job out of the other funds. I lose the use of the money and the money that I am owed. I cannot even earn interest on it. As I said, I am basically extending a loan.

When I am growing my business, the impact is even worse. In my view, if laws and regulations make it harder for banks to make payment cards available to my customers or make it harder for companies to develop innovative products like the mobile phone device, that hurts my business.

Of course, like all small businesses, I want to pay less for almost everything that I use in my business. However, if the State of Ohio limited what it could charge to install a wood floor in a government building—I do a lot of work for the State of Ohio—to some percentage of my costs, I guarantee you that I would do best to recover my costs across the rest of my lines of business.

If the limit was too much, I would stop doing that line of business, but no matter what, I would try to grow other areas of my business as opposed to devoting resources to that area of business.

Let me be clear: I do support having some rules of the road as long as I know what those rules are and they make it easier, or I should say better, for both my customers and I to do business. Of course, it would not be fair if the rules were drawn up in favor—and I certainly do not want someone dictating basic choices or business decisions.

I think in many cases, we swing back and forth too far in both directions. I am a small business. I can't always see it coming and I can't always duck.

Not only are extremes bad but there is not—I am sorry, but there is the not knowing that is coming. So I just want to say, if Dodd-Frank or any other legislation like it does not have any things that I have just talked about, I would likely oppose it or whatever parts of it affect or hurt my business.

While I am here, I also want to talk about how my business uses credit cards for purchasing so that I can consider—

Chairman NEUGEBAUER. Mr. Johnson, if you can kind of wrap up there—

Mr. JOHNSON. Oh, sure.

In my experience, any regulation that increases costs to businesses regardless of the industry will ultimately be borne by the business customers and from higher prices. It is difficult for me to characterize exactly how the financial sector law is enacted in Congress because I am not a banker. Other witnesses are better suited to speak to these issues.

What I can say is in the wake of a financial crisis, it is crucial that Congress and regulators not react so strongly that good parts of banking that we rely on—the parts that are not involved in the financial crisis—cease to be viable and healthy. When small business is healthy, the economy is healthy.

And I will be more than happy to answer any questions.

[The prepared statement of Mr. Johnson can be found on page 59 of the appendix.]

Chairman NEUGEBAUER. Thank you, Mr. Johnson.

And now, Mr. Min, you are recognized for 5 minutes.

STATEMENT OF DAVID K. MIN, ASSISTANT PROFESSOR OF LAW, UNIVERSITY OF CALIFORNIA IRVINE SCHOOL OF LAW

Mr. MIN. Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee, my name is David Min and I am an assistant professor at the University of California Irvine School of Law where I teach and research in the area of banking law and financial regulation. I thank you for the opportunity to testify here today on the topic of the impacts of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as I believe this is an issue that has been fraught with confusion.

I would like to make three main points in my testimony today: First, the negative impacts of Dodd-Frank have been greatly exaggerated. The fact is that Dodd-Frank has not had much of an impact to date because most of it has not yet been implemented, thanks in large part to a very successful campaign by Wall Street lobbyists who have spent a record $302 million in 2010 alone to delay and undermine the implementation of this law.

As of July 2, 2012, less than 30 percent of the rules mandated by Dodd-Frank have been issued in their final form, with most of these issued only in the last few months. It is thus difficult to understand the claim that Dodd-Frank has resulted in large regulatory costs, given that it has mostly not yet taken effect.

Second, most of the negative effects being blamed on Dodd-Frank are actually highly speculative and often misplaced. Because of the severe delays in implementing Dodd-Frank, we do not yet have much of a reasonable basis to know what Dodd-Frank will look like, let alone what the impact of those rules might be.

Thus, almost all the claims being made about the regulatory burdens created by Dodd-Frank have been based on unfounded and often wildly incorrect speculation. For example, many critics of Dodd-Frank have claimed that its proposed regulation of derivatives would dramatically increase the compliance cost for end users who currently utilize these derivatives for hedging, such as farmers, energy companies, and airlines, thus increasing the cost of our food, energy, and travel.

This argument has been proven both baseless and wrong. The Commodity Futures Trading Commission, the regulatory agency responsible for promulgating Dodd-Frank's derivatives regulations, did not even release its first set of final rules on this issue until last week, and these rules specifically crafted a broad exemption for this type of end user, rendering this criticism largely moot.

Similarly, while there has been much grumbling about the compliance costs that Dodd-Frank will create for small banks, it is not clear that Dodd-Frank actually will lead to increased compliance costs for these lenders. The primary evidence cited so far that Dodd-Frank will lead to these compliance costs is its length, which some have cited as being 2,300 pages, but which is actually 848 pages long—still a long bill.

In fact, the vast majority of Dodd-Frank has targeted non-bank activities, such as securitization, derivatives trading, prop trading, or the activities of banks with over $50 billion in assets. The fact is that if you are not a megabank, and if you are not running a hedge fund, and you are not dealing in products like derivatives or other exotic products, the overwhelming majority of Dodd-Frank simply doesn't apply to you.

Indeed, Dodd-Frank may actually reduce compliance costs for some small banks since it consolidates a number of regulatory rulemaking responsibilities which previously had been scattered among the Federal Reserve, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, and the Federal Trade Commission, among others, into one central body, the CFPB.

There has also been a great deal of confusion about the negative impacts caused by Dodd-Frank and conflation between the negative impacts caused by the financial crisis. Most of the burdens on small businesses and consumers being blamed on Dodd-Frank, including many of the ones you have heard here today, are actually the result of the financial instability that led to the enactment of Dodd-Frank in the first place.

For example, many have blamed Dodd-Frank for leading to tightened underwriting standards and a lack of credit availability in the marketplace. In fact, the lack of liquidity in credit markets was clearly caused by the financial crisis and predates even the passage of Dodd-Frank let alone the implementation of rules that might have impacted liquidity, such as the Qualified Mortgage (QM) standard, which has not even been implemented yet.

My third point is that in considering the impacts of Dodd-Frank on families, communities, and small businesses, it would be irresponsible for us here today to focus merely on the negative impacts. We must also consider the many positive impacts that this law may have.

Dodd-Frank was passed with the aim of increasing financial stability, improving investor confidence, and enhancing consumer protection, and it has been well-documented that these goals have enormous benefits for families, communities, and small businesses.

Now, many of us have forgotten recent history. I know 4 years is a long time in Congress, but the recent financial crisis in 2008, as Representative Capuano mentioned, caused enormous losses—$19 trillion in lost household wealth. While many critics have focused on the 848-page length of Dodd-Frank, it should be noted that if this law prevents a similar financial crisis from occurring it would actually save American households approximately $22.4 billion per page.

To conclude, the actual impacts of Dodd-Frank have unfortunately been far too minimal so far thanks to a successful lobbying campaign led by Wall Street to delay Dodd-Frank's implementation. The impacts of Dodd-Frank, once it has been fully implemented, are likely to be significant and positive insofar as it will reduce the likelihood of another major financial crisis, restore the shaken confidence of investors who have lost faith in American capital markets, and prohibit predatory lending practices.

I urge the members of this subcommittee to make all efforts to help facilitate the robust and prompt implementation of this law. I thank you again for giving me the opportunity to testify, and I look forward to your questions.

[The prepared statement of Professor Min can be found on page 64 of the appendix.]

Chairman NEUGEBAUER. Thank you.

Ms. Deyanira?

STATEMENT OF DEYANIRA DEL RIO, CHAIR, BOARD OF DIRECTORS, LOWER EAST SIDE PEOPLE'S FEDERAL CREDIT UNION

Ms. DEL RIO. Good morning, Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee, and thank you also for the opportunity to testify today at this hearing. My name is Deyanira Del Rio and I am the board chair of the Lower East Side People's Federal Credit Union in New York City. We are a small, not-for-profit community development financial institution that has $33 million in assets and serves 6,000 members in New York City.

We serve low-income New Yorkers Citywide, but we have a particular focus on two of New York City's poorest neighborhoods, including Central Harlem and parts of the Lower East Side. And I will just say that while we are close to Wall Street geographically, we are very far philosophically and in terms of our members.

I am pleased to comment on the Dodd-Frank Act and the Consumer Financial Protection Bureau from the perspective of our small financial institution and the communities we serve. So I have four main points and I will try to do them speedily.

First, I want to say that from our point of view, the Dodd-Frank Act and the other financial reforms of recent years have not harmed our credit union in any way in terms of our ability to provide low-cost loans and services to our members. If anything, our credit union has improved in performance and profitability in recent years: our lending has increased; we have flexible but responsible underwriting standards that we don't think will be curtailed by any of the regulation; we have 95 percent of our members' deposits in our credit union reinvested back into our neighborhoods in the form of affordable housing, small business, and consumer loans; and we continue to provide free checking accounts to all of our members who maintain at least $25 in our credit union.

We see more and more members coming to us, leaving the banks, which are becoming increasingly unfriendly, particularly to lower-income customers. We also have not experienced any decrease that is noticeable in our revenue as a result of the credit card and overdraft reforms of recent years, although I will say that it is primarily because we didn't engage in the types of deceptive practices that were curbed and addressed in the CARD Act nor did we ever become reliant on these high overdraft fees that a lot of banks and even credit unions turned into their profit centers. We have never offered those kinds of products and have chosen instead to offer traditional overdraft lines of credit and other responsible services to our members.

I will note that also, I think as others have said, that Dodd-Frank does make important accommodations for small institutions like ours. So, for example, as an institution with less than $10 billion in assets, we will be supervised for compliance with consumer financial protection laws by our existing regulator, the National Credit Union Administration. And further, the CFPB is required, as we know, to assess the impact of its rulemaking on financial institutions and small businesses like ours.

My second point is that to the extent our credit union is facing challenges, they overwhelmingly result from the financial crisis and the ongoing economic downturn and not from excessive regulation, and I can't stress this enough. Our credit union, also like many other credit unions, had no part in causing the crisis, but we are certainly feeling the effects and the costs through continued unemployment, the depressed interest rate environment that we are operating in, and the ongoing foreclosure crisis.

These are the threats to our institution over the long term and certainly to our members and our community's well-being. Lack of financial regulation we see as actually causing the stresses that our institution now has to work around.

My third point is that in response to the crisis, strong prudential regulation and consumer protections are needed to prevent future crises and to ensure fairness and opportunity for low-income people and communities. The repercussions of the economic crisis are going to be felt in low-income communities like ours for many years to come.

I will give you one grim statistic, which is that the median net worth of American families fell by almost 40 percent between 2007 and 2009. These are losses that will take families years or possibly generations to recover.

In addition to lost wealth, we are concerned that a growing number of our members and Americans generally are now contending with damaged credit histories as a result of abusive lending practices, the foreclosure crisis, job losses, and just the overall economic downturn, and this is particularly distressing for us because damaged credit histories not only impede people's access to fairly priced loans and credit, but increasingly they are being used outside of the credit sphere and can block people's opportunities for affordable housing, for jobs—increasingly employers are denying people jobs based on having damaged credit—and many other economic opportunities that people will be denied access to because of this damaged credit, often through no fault of their own.

So Congress enacted the Dodd-Frank Act in the wake of undeniable regulatory failure and abusive lending practices. It includes such provisions as a requirement that lenders consider borrowers' ability to repay loans. We think this is a fundamental tenet of responsible lending that was lost in the years leading up to the crash, and we support these and other common-sense regulations which we think all responsible lenders should embrace.

And my last point is that we believe the Consumer Financial Protection Bureau has a vital role to play in regulating and leveling the playing field for both depository and non-bank financial institutions. Our credit union welcomed the creation of the CFPB as the first Federal agency tasked specifically with protecting consumers in the financial services marketplace, something that we certainly could have used in the years leading up to the crash when neighborhoods like ours and across the country were flooded with high-cost, destabilizing forms of credit that ultimately caused havoc for the economy as well as for neighborhoods.

This regulatory failure—the fact that the seven regulatory agencies didn't catch or prevent the crisis—is particularly distressing to us because many of the problems we are facing could have been avoided had regulators paid meaningful attention to the harms that reckless lending was causing on families and communities. And in fact, this overemphasis on what ostensibly is safety and soundness, which is certainly important—and we are examined, like all depository institutions, for safety and soundness—but by focusing on that to the expense of consumer protection, regulators ironically failed to detect the broad systemic risk that was being caused by predatory lending practices which were, after all, lucrative in the short term.

So we think that the agency has a really important role to play in identifying future problems—

Chairman NEUGEBAUER. Ms. Del Rio, I am going to need you to wrap your testimony up.

Ms. DEL RIO. Yes. Okay. So my last point is that I want to say that we at the Lower East Side People's Federal Credit Union and credit union allies of ours have met with CFPB Director Richard Cordray at field hearings and regional meetings and weighed in on comment letters like many others here. We have so far—I want to note, we have been impressed by the approach and the thoughtfulness of the CFPB toward its rulemaking, and rather than coming in and issuing decrees, they have actually been exceptional in the way that they have solicited feedback from small businesses and financial institutions as well as Americans, consumers who are being affected by the practice.

We appreciate that and we think that their efforts to promote transparency and accountability are going to bring benefits to institutions like ours and our communities that are going to far outweigh any marginal or short-term costs of regulatory compliance.

So thank you, and I look forward to answering your questions.

[The prepared statement of Ms. Del Rio can be found on page 50 of the appendix.]

Chairman NEUGEBAUER. Mr. Smith, you are recognized for 5 minutes.

STATEMENT OF GREGORY W. SMITH, CHIEF OPERATING OFFICER AND GENERAL COUNSEL, THE COLORADO PUBLIC EMPLOYEES' RETIREMENT ASSOCIATION (CoPERA)

Mr. GREGORY SMITH. Thank you, Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee. Good morning. I am Greg Smith, the chief operating officer and general counsel of the Colorado Public Employees' Retirement Association (CoPERA). I am pleased to appear before you today on behalf of CoPERA.

With over $39 billion in assets under management, CoPERA is responsible for the retirement security of over 480,000 employees and retirees of State and local government in Colorado. Our members include teachers, snow plow drivers, and prison guards—regular people, hard-working people, people who support small businesses across the State of Colorado and who use local banks throughout the State of Colorado.

Colorado provides over $3.3 billion in annual benefit payments to over 95,000 beneficiaries of the Public Employees' Retirement Association. Ninety percent of these payments are made to beneficiaries living in the State of Colorado. Using commonly recognized economic impact measures, such as output, value-added, and labor income, and employment, these payments in Colorado represent $4.3 billion in output, $1.87 billion in value-add, and $1.1 billion in labor income, and over 23,000 jobs in the State of Colorado.

The annual benefit payments made by Colorado PERA to our beneficiaries represent approximately 3.3 percent of total wage income in the State of Colorado. In the rural counties of Colorado, this percentage is far greater.

In some of our counties, PERA benefits payments represent over 25 percent of total payroll in that county. This infusion of income into the local economies in Colorado creates a critical and stable source of income that fuels Main Streets and businesses throughout the State of Colorado.

As an owner of many of the Nation's large and small public corporations, our fund is strongly aligned with corporate America. We have every interest in its long-term success and in its profitability. As a result, we believe in good corporate governance, and good corporate governance practices are essential to maximize and protect long-term shareowner value and interests.

It is well-established that a key cause of the financial crisis was a failure in corporate governance. Our members have paid a deep price for that failure. Not only did they suffer billions of dollars in investment losses, but many also lost confidence in the integrity of our markets and in the effectiveness of board oversight of corporate management.

In the lead-up to the financial crisis, boards of directors failed to adequately understand, monitor, and oversee enterprise risk and corporate strategy. And far too many boards structured and approved executive compensation programs that motivated excessive risk-taking and yielded outsized rewards for short-term results.

As the costly fallout of such poor board oversight became clear, investors were left with few effective tools to hold directors accountable. Congress responded in the Dodd-Frank Act by providing investors with some of the tools needed to improve market-based oversight of corporate boards.

Those corporate governance reforms, some of which have yet to be fully implemented, have already begun to improve investor oversight of boards. Those key corporate governance provisions of Dodd-Frank, the benefits of which are described in more detail in my testimony, include the following: shareowner advisory vote on compensation; independent compensation committees; clawback of erroneously awarded compensation; enhanced disclosure of incentive-based compensation arrangements; and shareowner proxy access.

To date, only the first of these five important corporate governance reforms, the advisory vote on executive compensation, has been fully implemented as intended. That reform alone has proven highly successful in opening up dialogue between boards and shareowners on executive pay concerns and has also had an impact on eliminating poor pay practices at many companies—practices that were unrelated, and in some cases inconsistent with the company's long-term performance.

The other four corporate governance reforms described in my testimony await rulemaking by the Securities and Exchange Commission and, in some cases, the stock exchanges. These provisions are integral in improving oversight and meaningful accountability of corporate directors. Thus, CoPERA respectfully requests that the subcommittee actively support the prompt and effective implementation of these provisions and support providing the SEC with the resources they need to effectively write and enforce the related rules while at the same time continuing to perform their core responsibilities as the only agency in the Federal Government whose mission includes protecting investors and policing the capital markets.

Thank you, Mr. Chairman, for inviting me to participate at this hearing, and I look forward to your questions.

[The prepared statement of Mr. Smith can be found on page 90 of the appendix.]

Chairman NEUGEBAUER. I thank the gentleman.

I thank the panel for those opening statements, and we will now go to the question-and-answer period. Each Member will be recognized for 5 minutes, and the Chair now recognizes himself for 5 minutes.

Mr. Purcell, one of the things that I hear, and you alluded to in your testimony from small community bankers, particularly who have been used to making what I, when I was in the banking business, would call portfolio mortgage loans. These are loans that sometimes are $25,000, $30,000, $40,000 for houses in the community or outside of town. And a number of those banks have quit making those loans because of some of the requirements of new regulations.

There are two things I want you to elaborate on. First, who is going to make those loans? Because those loans normally aren't securitized and so their only source of funding for those loans in the past has been our community banks. And so how are the citizens, the families in these little small communities, how are they going to buy a house?

Mr. PURCELL. Mr. Chairman, I appreciate the opportunity to speak here, and that is a dilemma in our area. We are a rural area. We have made loans since the inception of the bank 100 years ago throughout the community and we filled a need that was not being met in that no one was interested in making a loan 10 miles from a town of 400 people, we will say, for O'Donnell, Texas, that was only on the small acreage.

We have done 5-year balloon notes. Under the new proposed regulation, the 5-year balloon notes will be high-priced. We don't charge fees.

I have had 14 or 15 community banks in our area—our area is within 200 miles; there are not a lot of people there—that are getting out of the mortgage lending because of the cost. I am not certain where those will go, where they will have to go to family.

But the real problem is that if you can't provide that each one of those customers, they have family, they have friends, and so, "The bank won't take care of me, you know? I have put my money down. I have always paid my obligations as agreed. Where do I go?"

So it is a dilemma. If you want to go to the farm credit system, the Federal Land Bank or some of those, they require 80 acres of land to be there. You can't sell a $25,000 mortgage loan in the secondary market for whatever price you pay.

Chairman NEUGEBAUER. Yes. I think you heard Mr. Min say that all of the claims by small financial institutions that Dodd-Frank is going to have an impact on them are not true. Mr. Purcell, are these community bankers dreaming this stuff up?

Mr. PURCELL. Our customers are not dreaming it up, and they are worried.

I understand that there was a calamity here. Unfortunately, for our part of the world in the 1970s and 1980s, we had a calamity there. I didn't get these bald spots from banking in good times; I got them from bad times.

We did learn some lessons—and I concur that the customer needs to be able to afford it, but if the payments are structured to what they would be paying in rent, they have a chance to build equity in their home. They have a chance to have homeownership.

But at times, we kind of outsmart ourselves, and we try to make people fit in a certain category, and that is one of the unique things about our community is that in our particular bank, a customer goes to whichever officer they want. I have more $500 loans than I do $3 million loans of my customers. It is ones that I started with 25 years ago, and we continue to try to meet their needs.

They have something to lose. If you have skin in the game, your commitment to paying is much, much better. The bank realizes it, and the customer realizes it.

So we are unique, I guess, in the whole scope of things. I don't understand all there is about Wall Street, but we are not driving for Wall Street in Big Spring, Texas.

Chairman NEUGEBAUER. Of course, one of the things that I hear from a lot of the smaller community banks, and maybe even some of the regional banks, is that the scale and the cost of compliance of all of these new regulations obviously impacts their ability to deliver some of those services. And so, we hear people talking about how we are going to see more consolidation in the banking industry, and one of the things that I have heard is that there was a call to break up the big banks because they were too big, but it almost looks like we are forcing a consolidation in the banking industry that basically just kind of going the other direction. Would you agree with that?

Mr. PURCELL. It is amazing that both—

Chairman NEUGEBAUER. Let Mr. Flores—

Mr. PURCELL. Okay.

Chairman NEUGEBAUER. —take that question, thank you.

Mr. PURCELL. I am sorry.

Mr. FLORES. Yes, I would agree with it. I have a colleague who teaches commercial lending in most of the graduate schools of banking around the country, and that is one of the key concerns that they are raising is community bankers, particularly those that are in markets that are low-growth or no-growth, they have had business model issues before this crisis. This has just basically exacerbated that.

And so with the thin margins they were operating under before, with the additional cost and loss of fee income, they are looking to sell. And you are right. Who is going to buy them? It is obviously the bigger banks, and so the default position is that the too-big-to-fail banks will get bigger.

Chairman NEUGEBAUER. I thank the gentleman, and I think my time is up.

Mr. Capuano is now recognized for 5 minutes.

Mr. CAPUANO. Thank you, Mr. Chairman.

Mr. Flores, I can't help myself. You do realize that your company is named after a place where one of the most—not devastating—

broad-based regulations in history came out of. Bretton Woods is a beautiful place but—

Mr. FLORES. It is.

Mr. CAPUANO. —but Bretton Woods resulted in a lot of things that—I was actually hoping Dr. Paul would be here today; that would be interesting.

Mr. Purcell, Ms. Smith, and Ms. Del Rio, I hope that you will take some comfort in a little fact of my life. I have all of my family's personal, business, and campaign funds in small banks. I don't have any—not one penny that I have control over is in a large bank. Not for any reason. I just prefer small banks. I like knowing my bankers and all that other stuff.

So I will just tell you that. Hopefully, you will take some comfort before I go in a different direction.

[laughter].

Mr. Purcell, stop, look, and listen. I totally agree. I actually haven't disagreed with anything I have heard here this morning of significant nature—minor little points, but nothing major. And I agree with everything you said. Stop, look, and listen is 100 percent right.

But Dodd-Frank is now 2 years old. We are stopping, looking, and trying to listen. It doesn't mean we will get it all right, but stop, look, and listen doesn't mean don't cross the street; it means be cautious, be careful, keep an eye on what is going on, and then cross the street. And I would like to think that is what we are trying to do.

Ms. Smith, on the remittance item, to be perfectly honest, today is the first day I have heard about that issue and the 25 per year. It is an interesting issue and I wish it had been brought to my attention.

I am under the impression at the moment that that aspect of this regulation has not been finalized, and I intend to leave this hearing and go look into it. I don't know whether I agree with you or not.

I would just say that is exactly what this stop, look, and listen is all about. It is 2 years later. We still haven't implemented that aspect and, again, I am not informed enough to agree or disagree, but it is an interesting point, a good point, one that is worthy of pursuit. And I assume you know that is not finalized yet.

Ms. LYNETTE SMITH. Thank you very much. I appreciate you looking into that.

That is catastrophic. We do, on average, three international wires a month. If you multiply that times 12, that is 36. I might get to a point where I cannot even offer—

Mr. CAPUANO. No, I understand. I am not arguing with the point at all. I am saying it is a good point worthy of consideration and—

Ms. LYNETTE SMITH. Thank you.

Mr. CAPUANO. —I will look into it, and I wish I had been informed of it as we were going forward.

I guess my bottom line here is that a lot of the concerns I have heard about Dodd-Frank from not just today's panel, but going forward, are fears of what might happen. Some of them are very legitimate and some of them I share—but the way to deal with the fear is not to not do it; the way to deal with the fear is to try to get it right before the mistake is made, or even after the fact.

Things happen after you do something that you did wrong. Everybody on this panel has made a mistake in your life, and when you do, you correct it. You don't just throw the whole thing out; you correct it.

So that is hopefully what we are trying to do. Regulations are not meant for the good players. No regulation is ever meant for the good players. They are only meant to say, "There is the line. Bad players can't cross here."

I use it all the time. One regulation we have is: Don't kill anybody. That is a regulation, guys. It doesn't mean anybody is going to go out and kill somebody; it just means that if you do, there are consequences. All regulations are simply drawing the line saying, here is where we are.

I guess, Mr. Johnson, I just want to ask you a—and I appreciate you being here. I realize you are not a banker; I am not going to ask any technical banking questions. But if—

Mr. JOHNSON. I certainly appreciate that.

Mr. CAPUANO. That is okay. I am only like half a step ahead of you—don't worry—and maybe even less than that.

But if you had a company—and again, you are a member of an association, you are a businessman—I presume you have never misled or deceived any of your customers?

Mr. JOHNSON. I try very hard not to do that.

Mr. CAPUANO. Again, not mistakes, but you have never intentionally—never deceived them into thinking that something you were providing was free, did you?

Mr. JOHNSON. No, I haven't.

Mr. CAPUANO. You have never deceived them into telling them that they were eligible for something for which they are not eligible?

Mr. JOHNSON. No, I haven't.

Mr. CAPUANO. So you would think that any business that engages in intentional misleading of customers is doing something wrong and bad for the economy, bad for America. Would you agree with that statement?

Mr. JOHNSON. I would agree with that statement.

Mr. CAPUANO. Then, you must support what the CFPB did yesterday, which is to enforce Capital One, because that is exactly what they were doing. Now, I don't know whether Capital One is a good, bad, or indifferent company, but they were clearly engaged in misleading customers—2 million customers—and they were slapped for it. Now, that doesn't mean they should be put out of business; it means they were slapped. They are going to have to refund $140 million hopefully to somebody who will need new flooring in your area.

Mr. JOHNSON. And I don't know enough about—

Mr. CAPUANO. I know.

Mr. JOHNSON. —Capital One, but what I can tell you from my vantage point as a business person is that I have seen the effect simply because lines of credit have been snatched away from me and I had to resort to credit cards to keep my business afloat and it was the result of the regulations.

Mr. CAPUANO. But according to your testimony, you are not sure that it is a result of regulation, and Mr. Min has testified—not just about you, obviously, personally—but about most loss of credit in this country was not the result of regulation, it was the result of an economic downturn, that the banks, even when they were infused with capital against the advice of some of my colleagues—they have tons of money, they still refuse to loan it. To my knowledge, there is no way for the Federal Government to force them to loan it.

Mr. Purcell, are you aware of anything that we can do to force you to make a loan?

Mr. PURCELL. No. But I sure wish you would convince our customers of the uncertainty, so they will start borrowing again.

Mr. CAPUANO. I agree with you. I totally agree.

Mr. JOHNSON. So, Mr. Capuano, I can—

Mr. CAPUANO. So, Mr. Johnson, the lack of credit has nothing to do with—

Mr. JOHNSON. But I can tell you that what happened from the collateral standpoint, when the banks would give me financing based on certain pieces of collateral that I had, the regulations took that away and they were unable—

Mr. CAPUANO. Which regulations did that?

Mr. JOHNSON. I don't know. You tell me.

Mr. CAPUANO. That is the problem, Mr. Johnson.

And here is the problem as stated by—oh, I had it here somewhere; who knows where it is—here it is—by the Independent Community Bankers of America president, he said it is more fear than fact. I am interested in facts. I need to know facts. I need to know specific regulations that are either proposed or finalized that don't work. And when that happens, I have done it repeatedly to advocate to stop them or to change them, and I will do it tomorrow. All of us will, on both sides of the aisle.

But to simply say that all regulation has caused me problems is not helpful, especially if you can't point out to me a specific regulation that has done it and—

Mr. JOHNSON. I hope my testimony did not say that, because I really don't believe that. I just believe that you need to take a look at it and say, okay, how can we get cash flow back into the hands of small business people, because it is our lifeblood.

Mr. CAPUANO. There is no disagreement with that. That is exactly what we are trying to do.

All I am trying to do is point out that—I am way over time; I apologize, Mr. Chairman.

All I am trying to do is point out that we are trying to get it right, and that not all regulation is inherently bad. Some regulations are necessary and it is important for all of us to work together to try to get it right.

With that, Mr. Chairman, I appreciate your indulgence.

Chairman NEUGEBAUER. I thank the gentleman.

And now the vice chairman of the subcommittee, Mr. Fitzpatrick, is recognized for 5 minutes.

Mr. FITZPATRICK. I thank the chairman, and I would also like to thank all the members of the panel for your testimony and your participation in the hearing. You are performing a great service for our country and I think that no matter where each of us stand or fall on the issue of the legislation, I think we can agree that what we are doing here today, which is oversight, is incredibly important for the industry, for our customers, and for our constituents. It is appropriate, especially for bills that are new bills that exceed thousands of pages in length, and also in connection with regulations that are yet to be written.

And so, Mr. Purcell, I agree, as Mr. Capuano agrees, stop, look, and listen. We can do that now with regard to regulations and we are interested in hearing from you how these regulations that you know about, as well as the regulations that are threatened or yet to be written, how that impacts your small banks, your institutions, and our constituents.

Mr. Flores, according to your testimony you said Dodd-Frank has increased fees to small businesses and consumers. What effect do these increased fees and reduced services have on consumers? Can you develop that a little bit for us?

Mr. FLORES. It is not a direct relationship because of increased compliance costs. And you are right, a lot of the provisions have not been implemented, but people are preparing and so they are hiring compliance people, or they are re-tasking existing employees to compliance, or they are outsourcing aspects of compliance.

But with the—let's say the Durbin Amendment, with the reduction of interchange fees, that has required—a lot of banks have eliminated free checking. Therefore, with the new checking products that are out there, the cost to have a checking product has gone up, and this primarily impacts low- to moderate-income consumers because if they don't maintain a $1,500 daily balance, they are going to get a service charge.

So it is the indirect impacts—the loss of fee income and the increase of operating expenses that banks are looking for new avenues of revenue production, be it fees or they have very little control on interest margins and so the only thing they can look at are fees. And they are being passed on to consumers and small businesses.

Mr. FITZPATRICK. Mr. Purcell, when you were describing your bank and the type of mortgages you grant and the way that you grant them, it sounds a lot like the small bank back home in Bucks County, Pennsylvania, that my wife and I use for our own family. I think you said for most of the loans, you require 20 percent down, and the bank provides 80 percent; you don't sell the mortgages, you actually keep them and service them. Is that a fair assessment of the way that your bank operates?

Mr. PURCELL. That is correct. We have never sold a mortgage. And I will say that in the times of distress over the last 7 years, there was kind of the end of good times and it has been tough times since then, I might also add we have not foreclosed on any home mortgage. But we do work with the customer.

Mr. FITZPATRICK. So you know what a qualified borrower looks like. You don't need a 1,000-page regulation to describe that for you?

Mr. PURCELL. I don't. The problem on the balloon payment, though, is that—on the 5-year balloon payment, you have to be able to show that customer can continue to make the payments. If you went out to 10 years or 15 years—by the way, we have no deposits committed in our institution for that, and that is what the savings and loans got in trouble for in the 1980s was extending loans further than what their deposits were. That is the reason for the 5-year balloon payment.

Mr. FITZPATRICK. I was intrigued by something that you said in your testimony about the cost of compliance on big banks versus the Main Street, the community banks like yours, that most of us think of when we think about the banking industry. You said, in fact, big banks—the very banks at the center of the problems that spurred the enactment of Dodd-Frank—are among the new law's greatest beneficiaries precisely because they can much more easily shoulder Dodd-Frank's compliance burdens.

Can you describe for us how it is they have benefitted—how the big banks have actually benefitted from the law and how the law has actually negatively impacted your ability to continue to service your customers?

Mr. PURCELL. I know there are Members on both sides of the aisle who want what is best for our country. I want what is best for it. I want what is good for our borrowers, too, and our community.

But when you enact legislation, and you have a large megabank that has a consumer department that is probably 100 times or greater than our total employees are, when you talk with your regulators and you talk about their compliance—how they go, they have two paths. They have a path for the compliance officer who studies—or who handles compliance on the deposit side, and now they have a path for the ones on the lending side.

If it is so complicated that someone who examines compliance issues every day, they have to split it up in two different directions; we are a small bank. And all this time of what everyone has said they wanted, the things that we wanted to avoid—we don't want too-big-to-fail; we want people to have risk and responsibilities for their actions—the large megabanks have continued to increase in size at the expense of small banks.

Mr. FITZPATRICK. Thank you, sir.

Chairman NEUGEBAUER. I thank the gentleman.

And now the ranking member of the full Financial Services Committee, Mr. Frank, is recognized for 5 minutes.

Mr. FRANK. Mr. Johnson, I wanted to pursue something that you said which, like Mr. Capuano, I was surprised to hear. You said one of the problems is that the banks you deal with are now rejecting collateral had previously given them or have somehow changed their attitude. Would you describe that to me?

Mr. JOHNSON. Sure. There were times when banks would turn around and look at your credit rating, they would look at your character and things like that, and they had done business with you historically before. They would take your receivables and other things like that and they would go ahead and loan you money.

Now what is happening is they are sitting there saying, hey, you know what, we can't do that anymore—

Mr. FRANK. Let me say that there is nothing in the statute that compelled them—other than—I assume you are not talking about a residential mortgage?

Mr. JOHNSON. No.

Mr. FRANK. Okay. We do have a problem, and some of us have expressed this frustration that some of the examiners have been overreacting, and I think the problem is it is in the culture. In the history of the world, no examiner was ever reprimanded for a loan that should have been made and wasn't made; they get reprimanded for the loans that were made that shouldn't have been, and that is a constant problem.

But there was nothing in the statute, I am sure, that in any way requires a bank to change its pattern with regard to what you just said.

Now, let me just ask Mr. Sharp, you mentioned two pieces of legislation that this committee has approved. Are there other changes you want to see with regard to derivatives or do you want to make sure that those become law? Is that—

Mr. SHARP. Those are the absolute highest priorities.

Mr. FRANK. All right. Then, we are in agreement there.

With regard to the nonfinancial aspects of it—the non-end-user, the JPMorgan Chase and others, do you have changes you want to see with derivatives in the non-end-user area where we were talking about financial institution or financial institution?

Mr. SHARP. No. Again, the Coalition doesn't have national members or—

Mr. FRANK. I appreciate that. And so, because as I said, and I appreciate—there always are some things that nobody can anticipate on every issue. We did think the regulators were sure—I am hoping that those are unnecessary but I have a principle of legislation: Redundancy is a lot better than uncertainty, particularly for lawyers, because we are the belt-and-suspenders group, so we never mind that.

Mr. Purcell, on the question you mentioned, your lawsuit, and you say you have brought the lawsuit against the CFPB on the grounds that it is an independent agency, not susceptible to checks and balances—that is the CFPB. It doesn't go through the regular appropriations process—the Director is appointed by the President but not otherwise controlled.

Why didn't you sue to get the Comptroller of the Currency thrown out, because everything in your lawsuit of which you complain about the CFPB applies even more strongly to the Comptroller of the Currency? In fact, the CFPB does—Congress can restrict its money.

The Comptroller of the Currency has a totally independent source. He or she is appointed by the President and that is it. What about the CFPB's structure is different in this sense from the Comptroller of the Currency, or you just don't like consumer protection?

Mr. PURCELL. I appreciate you being aware of the lawsuit that we filed. However, I am going to leave that up to the attorneys because—

Mr. FRANK. You mentioned it in your testimony.

Mr. PURCELL. I understand, but it says that I will answer questions about the other part of it. But—

Mr. FRANK. All right. If you don't want to answer, okay. I am sorry, Mr. Purcell. I only have 5 minutes, and if you don't want to answer it, don't answer it.

I have to say—and I would ask people to look at this—the argument aimed at the CFPB, they legally are on all fours, as lawyers say, with the CFPB.

Let me just ask you though, Mr. Purcell, with regard to mortgages—and let me ask—is it Ms. Smith, from the credit union, because some of the criticisms were there: Do you think we should have passed any laws to change the rules regarding the granting of mortgages when we looked at what happened up through 2008?

And if so, for instance, did NAFCU submit to us any proposals for what we should have done with regard to mortgages, Ms. Smith?

Ms. LYNETTE SMITH. Yes, we do. We do support the TILA and RESPA forms. We think that they are—

Mr. FRANK. Okay. I appreciate that. What about the substantive mortgages? That is, should we have changed the law with regard to the ability to do mortgages with 2 years and 28 years interest, and no prepayment allowed, or should we have said, as we do, that there has to be some showing, Mr. Purcell mentioned skin in the game—that you shouldn't give mortgages to people who can't afford it?

Would you in 2009 have recommended to us, or did you, Ms. Smith—obviously it wasn't your job, Mr. Purcell, as an organization—any substantive changes in mortgage law?

Ms. LYNETTE SMITH. I believe there are substantive changes that need to me made and I can give that to you at a later—

Mr. FRANK. Did the NAFCU ever tell us what they were? I don't remember. Do be honest, I think—

Ms. LYNETTE SMITH. No. Honestly, I—

Mr. FRANK. Okay. I am very skeptical of this. People come before us now because they don't like the regulations that are out, then say, "We are not saying there shouldn't be any regulation." Except, many of you did say there shouldn't be any regulation by not saying anything. People who did not tell us in 2009, "Yes, you are right. There were mortgage abuses. Here is the way to correct them," but were perfectly content to let the situation go forward, I am a little skeptical when you now say, okay, yes, there was a need for things, but you should have done it differently.

So if I am wrong that if, in fact, in the prior years you had submitted some things I would be—I will correct myself.

Ms. LYNETTE SMITH. Okay.

Mr. FRANK. Thank you, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from Ohio, Mr. Renacci, is recognized for 5 minutes.

Mr. RENACCI. Thank you, Mr. Chairman.

And I want to thank all the witnesses for being here.

Mr. Min, in your testimony you say—and, of course, this was in regard to the negative aspects of conclusions on Dodd-Frank—"Because of the severe delays in implementing Dodd-Frank it is impossible"—you use the word impossible—to know what the actual impacts of Dodd-Frank will be." Would you also agree that from a positive standpoint, it would be impossible to determine what the impacts of Dodd-Frank would be?

Mr. MIN. I do agree. That is why I don't attempt to quantify what the numbers might be. I think we have some recent evidence, of course, with the financial crisis of 2008, of what the status quo looks like, but whether Dodd-Frank is a perfect answer to that—

Mr. RENACCI. Right. So it is a definitely impossible.

Have you ever operated a small business, or a bank, or a small bank or credit union?

Mr. MIN. No, sir.

Mr. RENACCI. Okay. But you are a professor. If I came to your office before your semester started and I threw 2,300 pages in front of you and said you now had to teach based on those 2,300 pages, that would bring some uncertainty to you, wouldn't it?

Mr. MIN. Actually it depends—it is 848 pages, and if I had to teach it tomorrow, of course that would be a problem; but if you told me that I needed to teach it in the spring, I think that would probably be doable.

Mr. RENACCI. But you would have to get some resources; you would have to understand what is in it; you would have to spend some time and energy to determine—

Mr. MIN. Of course. I would have to read it. The first thing I would do is look at the table of contents and see what provisions I wanted to teach, what seemed applicable to banking law versus, say, securities law or other areas—

Mr. RENACCI. Well, no. What I am talking about on how you teach and how you interact and how you move forward, so it is really how you would move forward, and that is what I am trying to get at. There would be some certainty, you would have to spend some resources.

Mr. MIN. Of course.

Mr. RENACCI. Okay.

Ms. Smith, you talked about regulations and which—give me some idea of which yet-to-be-implemented regulations you anticipate will have the most profound effect on you, your customer base, and the community you serve.

Ms. LYNETTE SMITH. I am really concerned about the interchange price cap. Also, just the overwhelming compliance burdens in the new rules, it is hard for me, running an $87 million credit union, to keep up with all of the compliance, if that answers your question. That is what I have sleepless nights about.

Mr. RENACCI. So you are concerned with the 2,300 pages and what is in it, and—

Ms. LYNETTE SMITH. Yes.

Mr. RENACCI. —compliance, and you have already had to spend some money, I am sure, to prepare for the compliance on it.

Ms. LYNETTE SMITH. Absolutely. I am going to have to hire a full-time compliance officer at this point.

Mr. RENACCI. Do you fear that some of these costs will have to be—that you will have to increase fees for services?

Ms. LYNETTE SMITH. Yes, they could down the road. Credit unions have always been the lender of last resort, and if I could just share with you for a minute, when I have members come into my office and I know they have no other place to go, I can provide them with a loan within an hour. I want to continue to do that. And they walk away and the next day they are bringing me cucumbers from their garden. That is the grassroots that credit unions do. That is what we are in business for.

Mr. RENACCI. Mr. Johnson, welcome. I want to welcome a fellow Ohioan here to Washington. You talked a little bit about credit cards and debit cards and the value to your business and how you were able to get your cash in 3 days versus 90 days.

You also talked about the cost of it, and you compared it to the cost of if you were putting in a wood floor. Can you explain a little bit of what you were trying to get at there?

Mr. JOHNSON. Sure. If I were able to get the money in 3 days, I can take that money and turn it around and do 5 jobs as opposed to having to wait for 60 to 90 days to get that money, so by being able to accept credit cards for payment, I am assured that I am getting the money. I don't have to worry about getting a check, and if the check bounces, I have to take out another loan to pay the bounce fee from the banks.

So it is very, very good for me to be able to get that money and turn it around. If there is a cost to it, I get that, but I can still make a lot more money by getting it and turning it back into the business as opposed to having to wait for 90 days.

Mr. RENACCI. So you weren't really concerned about the cost at the time; you are more concerned about getting the cash in?

Mr. JOHNSON. Absolutely. Cash flow is the lifeblood of my—

Mr. RENACCI. I was a small business owner. I understand wholeheartedly.

Ms. Del Rio, before my time runs out, you heard what Ms. Smith said about some of her concerns. You acted like there were no concerns. You have some compliance costs that you have to prepare for, and you are going to have to pass those costs on to someone.

Ms. DEL RIO. We comply with a wide array of consumer protections and regulations. To us, Dodd-Frank is not going to be something that is going to be a weighty new regulation for us; we are going to incorporate it into our practices.

We don't, at the moment, anticipate having to raise fees for our services. It is something that we are—we do everything we can. We are a low-income credit union and 82 percent of our members are low-income in New York City. So we—

Mr. RENACCI. So even though you are going to have to prepare for 2,300 more pages, you don't see any more costs and no concern about passing that on to—

Ms. DEL RIO. No. Actually, as my colleague said, the majority of those pages don't apply to us.

If you are a responsible lender, the majority of those new checks and balances aren't going to change your practices. There will be some new disclosures, and reporting, and proving that you are in compliance, but that is much different than having to revamp your entire business model.

Mr. RENACCI. Ms. Smith, quickly, I see you just—

Ms. LYNETTE SMITH. Yes. I just wanted to say, the $30 million credit union may not have all the services that an $80-plus million credit union does. We are trying to compete with the big banks. So we are going to—our infrastructure, our array of services are going to be more than a smaller, low-income credit union. And—

Ms. DEL RIO. Can I address that?

Mr. RENACCI. I am running out of time—

Ms. DEL RIO. Okay.

Mr. RENACCI. —so I am going to yield back to the chairman.

Chairman NEUGEBAUER. I thank the gentleman.

And now, Mr. Miller is recognized for 5 minutes.

Mr. MILLER OF NORTH CAROLINA. Thank you, Mr. Chairman.

When I hear of the complaints about compliance costs with consumer protections in financial transactions, it sounds like what is happening is the consumer is walking in and the loan officer or whomever pulls out a legal pad or pulls up their computer screen and says, "Okay, you want to be the party to the first part or you want to be the party to the second part?" and then drafts something from scratch and has to have 2,300 pages of statute or regulations in their head or by their desk that they can consult, and that is pretty seriously different from my own experience in practicing law for 20 years.

There was something called forms, which made life a lot easier. They were published. They were kind of vetted that they were legal. They were often developed by trade associations.

Almost every real estate form, every form used for residential real estate transactions, were forms that had been developed and approved by the Bar Association and by the REALTORS®, and it not only was a lot less work for me—I didn't think I was really cheating—it was a lot less work for me. I think every lawyer used them. They saved a lot of money for the client and you ended up with better forms, with better legal documents that complied with the law.

Ms. Del Rio, how does it work? Do you really generate all of the forms from scratch for your credit unions or does someone develop forms that comply with the law that you can use?

Ms. DEL RIO. It is a variation. It is a mix. We have third-party vendors, for example, that process our credit cards, and they do a lot of the regulation, the compliance work for us. There are times where we have to update a disclosure form to comply with the new regulations.

We welcome these regulations, and we want to be a transparent institution. This is our mission. So for us, that is not a cost.

And I just want to make a small point, which is that we are a full-service institution, so we have checking, savings, business lending, online banking. We have everything that the—all of the consumer financial services and products that a bank and other credit unions do.

We have grown to this. We prioritize where and how we offset our costs, where we raise money to be able to grow and expand our services.

And because we never became dependent on these high fees that a lot of other institutions did, we are not now scrambling to try to figure out where to make it up. I remember just even in the credit union world, there were consultants, regulators, examiners even, encouraging us to find more ways to charge members fees, and we have chosen not to do that and that is why we generate most of our income off of loan interest.

We want to make our income in a way that is responsible, that is actually generating activity in our community. So we did a lot of small business lending, including from businesses that are sent to us by our local banks.

Mr. MILLER OF NORTH CAROLINA. One complaint I did hear from lenders that wanted to do the right thing—honest lenders—was that one of the reasons the disclosures were so unreadable and so big was that their lawyers advised them or they understood that the safest thing to do was to set out disclosures verbatim from the statute. It was safer than trying to summarize them or put them in plain English.

And they specifically cited the example of TILA and RESPA of being similar but not quite the same, and what they would do was set out both statutes verbatim in the disclosures. And so, when the CFPB approved a form that was plain English which included both, it seemed to be a great service to everybody.

Ms. Del Rio, has that been the case at your credit union?

Ms. DEL RIO. As far as I know, the new form is not—

Mr. MILLER OF NORTH CAROLINA. And, Ms. Smith, you said you were okay with that—

Ms. LYNETTE SMITH. Yes. I am okay. I—

Mr. MILLER OF NORTH CAROLINA. You favor that.

Ms. LYNETTE SMITH. Yes. I do favor that. As a matter of fact, I was at the CFPB last year before that form was—

Mr. MILLER OF NORTH CAROLINA. Okay. I do have limited time so—

Ms. LYNETTE SMITH. —generated. So yes.

Mr. MILLER OF NORTH CAROLINA. Mr. Purcell, have you not figured out that you really don't have to write every consumer credit contract at your bank, that there are forms that you can use?

Mr. PURCELL. We do, and every time the law changes, we get to increase our fees for those forms and changes. But yes, we do.

Mr. MILLER OF NORTH CAROLINA. Your national trade associations don't provide you forms that comply with the law? There aren't publishers who will develop forms that comply with the law?

Mr. PURCELL. There are major vendors that do provide that but they do charge maintenance fees and they do charge when you have to have major modifications in it. So—

Mr. MILLER OF NORTH CAROLINA. Okay.

Mr. Min, I know that you are now a professor, so presumably you have no idea what goes on in the real world, but do you have any understanding of how this really works? Are there standard forms?

Mr. MIN. —it should be from the trade association, as I think Ms. Del Rio stated. I would be surprised if the law was as onerous—in practice if it was as onerous as has been claimed.

Mr. MILLER OF NORTH CAROLINA. Okay.

One last—there are 14 titles to Dodd-Frank. Mr. Flores, Ms. Smith, Mr. Sharp—well, not you, Mr. Sharp—but you, Mr. Purcell, how many of those titles apply to your business?

Mr. FLORES. To my business, none, but to my clients' business, several, depending if they are alternative financial services, or community banks, or credit unions, and the size, if they are under $50 billion or over $50 billion in assets.

Mr. MILLER OF NORTH CAROLINA. Mr. Purcell?

Mr. PURCELL. You have your Fair Credit Reporting Act, which is one example. But you also have your different types of lending. You have multiple titles within the Dodd-Frank. You have the CFPB that is wrapping its arms around things that covered us before, but they are changing some of the definitions to include things that weren't, so I could not tell you at this moment exactly which ones do or which ones don't.

Mr. MILLER OF NORTH CAROLINA. Ms. Smith?

Ms. LYNETTE SMITH. Okay. Thank you. There are several, and I can give you that in writing at a later date. Thank you.

Mr. MILLER OF NORTH CAROLINA. All right. Thank you.

Chairman NEUGEBAUER. I thank the gentleman.

And now the gentleman from New Mexico, Mr. Pearce, is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

It is nice to hear each one of you testify. I especially appreciate Mr. Purcell. I can identify with that lingo you speak there; it sounds like where I grew up. If you know where San Jon is, you know where every place in New Mexico is—now that is getting small.

Mr. Johnson, I really appreciate your testimony. We need to be hearing from the people who have built businesses and are out there just trying to make it work. I was a small business man and I appreciate that.

I am going to bypass the desire to ask you what you thought about the President's comment that if you built a small business, you didn't really do that. Again, I built a small business from 2 to around 50 people, and so I have this—we struggled all the way along and I can hear the struggle that you have and ours.

Mr. Smith, I am interested, what assumption of rate of return do you have to make the distributions out of your pension fund?

Mr. GREGORY SMITH. Representative Pearce, our current assumption is 8 percent; our 25-year return is 8.9 percent; our 30-year return is—

Mr. PEARCE. What did you make in the last—what have you made in the last quarter?

Mr. GREGORY SMITH. I don't know; in the last quarter, about 4 percent—

Mr. PEARCE. About 4 percent.

Mr. GREGORY SMITH. In the last 3 years, it—

Mr. PEARCE. How much shorter do your—in other words, your assumptions are at 8 percent. Let me just—

Mr. GREGORY SMITH. We got a 1.9 percent compared to our 8 percent, if that is what you are trying to get to.

Mr. PEARCE. Yes. So yesterday, CalPERS announced that they had a 1 percent rate of return; their assumption is 7.5 percent, and it is looking like maybe they are $800 billion short if they figured at a 3.8 percent, so the calculation for a 1 point rate of return is probably in the trillions—just for California.

So these pension funds that make these assumptions and then pay out very large retirement bonuses or retirements are really putting the long-term future of the pension fund at jeopardy.

I was interested in your comments, Mr. Smith, on executive compensation. Your shareholders would be the pension beneficiaries. Do you allow them to vote on your compensation?

Mr. GREGORY SMITH. Our board of directors is directly elected by our membership and our board of—

Mr. PEARCE. So you allow them to vote like you are asking—

Mr. GREGORY SMITH. —corporation is.

Mr. PEARCE. Do you allow them to vote, Mr. Smith, on your compensation the way that you are requesting in your testimony that corporations would allow?

Mr. GREGORY SMITH. I would challenge whether that is a comparison, sir, but no, they do not vote on my compensation.

Mr. PEARCE. Okay. What do you make? What is your salary?

Mr. GREGORY SMITH. About $300,000 a year.

Mr. PEARCE. And they don't get to vote on that. That is very interesting.

Ms. Del Rio, do you keep track of people who don't make—they are not able to service the loans? Do you all track that? Your customers who can't service the loans?

Ms. DEL RIO. Of course. Sure. You mean people who fall behind on our loans—on their loans—

Mr. PEARCE. And so if someone defaults on a loan, and they come back in for a loan, you have a record of that?

Ms. DEL RIO. Yes. We try to restructure people when they fall behind so that we don't have to get to the point of—

Mr. PEARCE. But you are not just not knowledgeable if they have defaulted on a loan?

Ms. DEL RIO. Oh, no.

Mr. PEARCE. And so, I find your testimony where you are critical of those who do track and do make available credit histories, you are very critical of those who allow credit histories to go about, and yet you all track a credit history. Your testimony—

Ms. DEL RIO. Oh, sorry. Maybe I wasn't clear. So first, in terms of the credit, we do look at credit history of people but we also look at many other things. A lot of our borrowers—

Mr. PEARCE. I understand, but there are people—

Ms. DEL RIO. —have no credit history and so we look at other—

Mr. PEARCE. Thank you.

Ms. DEL RIO. —things.

Mr. PEARCE. Thanks.

Ms. DEL RIO. I am sorry. My critique in my testimony was not about even lenders using credit history, although there are some questions there. It was about employers and others outside of the credit system using that to judge character and whether someone would make a good employee, and—

Mr. PEARCE. Okay.

If I could follow up, Mr. Sharp, do you know on the U.S. Chamber how many employers ask about credit history before they hire? Because in New Mexico, people are dying for employees. They are saying, "Please, send us the employees. All they would have to do is show up for work and pass a drug screen. We need employees badly." And I have never heard one employer in New Mexico ask for a credit history.

Anyway, it is just curiosity.

Mr. Min, have you ever downloaded content off the Web?

Yes, of course, you have. So you might have an opinion about Net neutrality regulations, those who would regulate those who are downloading?

Mr. MIN. I actually don't. I don't think I have enough information about—

Mr. PEARCE. You don't have an opinion about that?

Mr. MIN. I don't actually know enough about the issues, and outside of my issue area, so—

Mr. PEARCE. Okay. There are people who would like to limit your ability to download information, films, whatever.

Mr. MIN. Okay.

Mr. PEARCE. Now, I suspect that they don't have one shred of empirical evidence; they just understand that they are opposed to the government coming out and regulating, so when I see that you talk about regulation being highly speculative, it would be highly speculative that people want to say, "You can't stop me from downloading content. It is a free society. It is free." They won't have one shred of empirical evidence.

Mr. MIN. Sure. I think—

Mr. PEARCE. You would declare that to be highly speculative and I am finding that to be a deep flaw in your testimony.

I yield back, Mr. Chairman. Thank you very much.

Chairman NEUGEBAUER. I thank the gentleman.

Mr. Carney is now recognized for 5 minutes.

Mr. CARNEY. Thank you, Mr. Chairman, and Mr. Ranking Member, for holding this hearing.

And thank you to all the folks who have come to share your experience and expertise with us. I have been sitting—I am usually the lowest man on the totem pole so I get to ask my questions last, and I hear a lot of the back-and-forth and the testimony, and it has been very interesting today.

I liked, Mr. Purcell, your comparison to standing on the corner crossing the railroad tracks and the guidance to stop, look, and listen. My experience—I am new here—in the last year-and-a-half is that we do a lot of stopping and listening and we don't cross many streets. And I think with respect to the Dodd-Frank regulatory reform legislation, the Congress responded to a devastating crisis and crossed the street, and we are here today to explore how crossing that street has affected small businesses and families.

The hearing is entitled, "Who's in Your Wallet? Dodd-Frank's Impact on Families, Communities, and Small Businesses," which suggests to me that somehow the regulations are having an impact on individuals while it is a small business wallet. We forget, I think, the impact on our wallets, our bank accounts, our home equities, our retirement funds, that the financial crisis had on all of us. I think Professor Min said $19 trillion of lost wealth across our country.

We had Fed Chairman Bernanke in yesterday testifying and telling us that the recovery is slowing down, that there are still millions of people out of work. He didn't have to tell me that. I talk to those people every day.

I didn't hear any of you say that financial regulatory reform wasn't necessary, but that it is having some unintended negative consequences on each of you. And I think the purpose of our hearing today is to identify some of those unintended consequences or intended consequences that are having a negative effect on our economy.

It is in all of our interest—Democrats, Republicans—I think it has been said a couple of times that we have a strong economy, that we have a financial system that we have confidence in, that is strong.

So I would like to just ask you, I hear all the time about how it is not so much the regulation—one regulation or another—it is the accumulation of regulations and the duplication.

Could somebody—I see Mr. Purcell shaking his head. Could you address that? And tell us how you think we can change something to address that problem?

Mr. PURCELL. I do not doubt the intent of the Act. I do not disagree that there should not be regulation. The stop, look, and listen is let's think about some of the things that are enacted—and I am speaking in regulation in general, as you spoke of.

It doesn't make a lot of sense to me. We just replaced our ATM about a month ago. Our drive-up ATM didn't have Braille on it. And I don't know which is worse—someone driving in who can't see to use the Braille or not having the Braille on the drive-in. And I am not being critical, I am just saying that is part of trying to make regulations and what we pass effective.

Mr. CARNEY. So is the point that maybe we go too far with small things and it is the accumulation of those small things—

Mr. PURCELL. I believe it is. I think it is. Everyone has a good idea, they have good intentions, but when we start adding it up, and we start with 40 years worth of regulations, and we say we are going to—

Mr. CARNEY. So maybe we need a process to clean out the underbrush, so to speak—

Mr. PURCELL. Yes.

Mr. CARNEY. —and to eliminate some of the things? We have done that a—we have one bill, actually, that is coming through to do that.

Mr. Flores, did you have—it seemed like you had a response there?

Mr. FLORES. I did. It is rationalizing regulations. A lot of my clients would say, "We are being painted with a broad brush"—

Mr. CARNEY. Right.

Mr. FLORES. —when they weren't responsible for the financial meltdown.

As a matter of fact, when you look at re-engineering a process, it is the 80–20 rule. Look at the things that are really creating a bottleneck and it creates an 80 percent efficiency, if you will.

A lot of people who wrote mortgages—the liar loans, the no-docs, the no income verification—they wouldn't have done that if they held them in portfolio. They only did that because they were unable to buy the secondary market buying of primarily Fannie—

Mr. CARNEY. So the legislation addressed that to a certain extent by requiring banks to have some skin in the game, as I heard somebody say earlier, correct?

Mr. FLORES. And I have no problem—if you are selling in the secondary market and if you are servicing a loan because you can know who the customer is and deal with that, then retaining 5 percent to me is not a problem. I know a lot of people disagree with that.

Mr. CARNEY. My time is running out.

But let me just say to all of you, if you have specifics, if you could send them to us so that we could try to address that directly?

I just want to reiterate or revisit the question that Mr. Frank asked with respect to Mr. Sharp on the derivative. So we have passed these two pieces of legislation overwhelmingly in the House addressing some of the concerns that your clients have, but you said there is nothing else. Are there any next steps there, just to reiterate?

Mr. SHARP. I wouldn't say there is nothing else, it is just that these two bills are absolutely the highest priority for this group. They would help the largest number of members of this Coalition, so—

Mr. CARNEY. Great. Thanks very much.

Thank you, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman, and now the gentleman from Texas, Mr. Canseco, is recognized for 5 minutes.

Mr. CANSECO. Thank you, Mr. Chairman.

And thank you all, panel members, for coming here today. I think it has been a good discussion.

I am sometimes very concerned about what happens when we talk about Dodd-Frank, and when we talk about the 2008 economic crash that happened, and the solutions, and the languishing economy, it sort of seems to me that what we are doing is stepping on the brake of an automobile at the same time that we are pressing on the accelerator, not realizing that what we are doing is very counterproductive.

Professor Min, let me—I am sure you are familiar with Sarbanes-Oxley, being an academician in the banking area, and Section 404(b) compliance has resulted in costing 20 times more in reality than the original estimates. You seem to argue in your testimony that we shouldn't worry because we haven't seen the full effects of Dodd-Frank, but doesn't the experience that we have had with Sarbanes-Oxley suggest this is exactly the time to be concerned?

Mr. MIN. So you are asking, essentially, looking back at SOX 404 and the higher costs, I am not sure about the 20-times figure you just cited, whether we should use that as a basis to estimate our—assume that regulation might cost more than evidence gives us belief to do. Is that the question you are asking?

Mr. CANSECO. I am asking you if you are not just projecting wrong and not realizing that sometimes these over-regulations that seem to paint everyone, as Mr. Flores says, with one broad brush are very costly and counterproductive.

But let me go on to this other thing, because I have limited time here.

Mr. Purcell, we hear a lot of talk in Washington about how we need government bureaucrats to protect American citizens from their own judgment. This was a large part of the argument behind the creation of the CFPB.

And I was in community banking for quite a number of years in Texas, just a little bit south of where you are, and—that was before I came to Congress—so I understand that if you are not taking care of your customers, you are going to be put out of business pretty quickly. So can you explain to us from a community banker's perspective why consumer protections, safety and soundness, and doing the right thing all go hand-in-hand and why the creation of the CFPB could disrupt that and actually hurt consumers and families?

Mr. PURCELL. I am not certain that I could answer that in the 2 minutes that is allotted with your time, sir, but I will tell you that many times, we get carried away. The pendulum swings, and times get good and times get bad, and we overreact, generally, in both scenarios.

But we cannot remove the culpability of the person who causes the problem. For instance, overdraft protection; there has been all kinds of news about that.

The question I would have is, who has the checkbook? Who has the deposit slip? And who issues the checks?

And I find it somewhat ironic that the Federal Reserve will charge you $300 for being overdrawn 20 minutes during the daytime, but $25 for someone who is overdrawn 2 weeks. It is unfair. We compare different things, but the person who wrote the check is the one who should be responsible for making that deposit.

For the person who borrowed money at a greater amount—maybe 102 percent of the value of his home—there is a price to pay. For the person who loaned at the 102 percent of that had somewhat of greed in their heart too, they should be the ones who stand the loss. When we let the losses fall around the necks of the ones who create it and we try to let that take place rather than coming up with a regulation to prove that we are going to prevent any future effort—or problem and catastrophe.

Maybe it is skepticism, maybe it is cynicism in my heart, but I am pretty sure that Dodd-Frank will not prevent another catastrophe as long as civilization moves.

Mr. CANSECO. Let me move on to another vein, because I have a couple of seconds left. Recently in a speech, the President remarked that if you own a business, you didn't build that; somebody else made that happen.

I am sure you deal with plenty of small businesses in West Texas. In your experience, who built those businesses?

Mr. PURCELL. The individual did. And if you doubt it, you should come to Texas, and you are from Texas, so you know the independent nature that our business people have.

Mr. CANSECO. Thank you very much.

I yield back the balance of my time.

Chairman NEUGEBAUER. I thank the gentleman.

And now another great gentleman from Texas, Mr. Green, is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. Actually, we have about four Texans in the House currently, and I would like to welcome Mr. Purcell to the committee.

I have met with the small bankers in Texas—a good many of them; not all of them—and small bankers from other places as well, and they all echo the same concerns, and it has been said enough for me to want to find some means by which we can ease some of the consternation.

I am not sure what the solution is, but I would like to, if I may, ask you, do you in your mind, sir, make a distinction between the $10 billion demarcation that we have and a community bank? Because many of the bankers that I meet with are not at the $10 billion mark; they are considerably smaller. Do you make a distinction in your mind?

Mr. PURCELL. I do. I don't know if it is a magic $10 billion; I don't know if it is $2 billion; I don't know if it is $50 billion. But there is definitely a difference for someone who has to—if they make a loan, they get to drive by that business and be proud of it. The bad side of it is is if you made that bad loan, you still have to drive by that property every day and decide that it was not a good deal and remember that.

So it is so foreign. I don't understand all the default swaps and the things that happen on Wall Street. I am even confused by the definition of what a bank is, or how they can come into the FDIC without paying pass premiums, and now they are automatically a bank, because by my definition of a bank it doesn't include a lot of those on Wall Street, sir.

Mr. GREEN. Are you considerably smaller than $10 billion?

Mr. PURCELL. We are less than $300 million.

Mr. GREEN. Less than $300 billion?

Mr. PURCELL. Less than $300 million. That—

Mr. GREEN. $300 million.

Mr. PURCELL. I know zeroes in Washington kind of get confused, sir, but—

Mr. GREEN. It is my hearing.

Mr. PURCELL. —we are a lot less.

Mr. GREEN. It is my hearing. Some things don't function as well as they used to. But, $300 million.

And are most of the community banks that you refer to, are they less than let's say $500 million or—are they less than $1 billion, most of the community banks that you are referring to?

Mr. PURCELL. By my definition, a true community bank would probably be less than $1 billion. There are some successful banks in our area that are $2 billion that really do serve their communities.

Mr. GREEN. And when you are smaller than $1 billion, do you—tell me, how are your departments organized? Do you have many departments or do you have people who multi-task? Now believe me, I have heard the answer, but I want it for the record now.

Mr. PURCELL. It doesn't snow very often in Big Spring, but we multi-task. I sweep the porch off—

Mr. GREEN. How many employees?

Mr. PURCELL. We have about 40 employees, and we have a lending department, and then we have customer service and operations departments. Now, there are some cross-issues there because you have to wear many hats at the same time.

So if a customer comes into the bank and they want to borrow money, they choose who they want to go to. We do not assign them. We don't say, if you are doing consumer credit you need to go to this gentleman, or you need to go to this lady, or you need to fill out an application and we will run your credit check, and we will get back with you in a week. We don't do it that way. We try to answer immediately.

Mr. GREEN. And would you say that most community banks with assets under $1 billion, that they do a lot of what we call multitasking, that they don't have departments set aside for compliance adherence?

Mr. PURCELL. That is correct.

Mr. GREEN. I am asking this because it seems that as I talk to the bankers in Texas—and I talk to a good many—in their minds, they have a distinction between a $10 billion small bank and what they call a community bank. And that is where I am trying to find some means by which we can address some of these concerns.

I don't know that we can go to a third tier. Right now, we have a two-tiered system. But small community banks, they seem to have a different role.

I am picking up that they seem to serve a clientele that is much more intimately known to them. The way that they do business has a lot to do with tradition. And I am trying in my mind to find a way to resolve some of these issues for the small community banks.

Mr. PURCELL. I don't know if I can help you with that, but I do know that if our customer does not do well and survive, our bank does not do well and survive.

Mr. GREEN. If I may, Mr. Chairman, I want to ask one more question. What percentage of your loans do you maintain in-house, maintain on your portfolio?

Mr. PURCELL. One hundred percent of the loans, unless it is too large of credit, and we would participate that out with other community banks in the area that understand the risk involved and know that type of credit. But our customer is serviced there; he does not go anywhere else. If he has a problem, he comes to us. If we have a problem, we go to him too, though.

Mr. GREEN. Thank you, Mr. Chairman.

Chairman NEUGEBAUER. I thank the gentleman.

And now, Mr. Fincher is recognized for 5 minutes.

Mr. FINCHER. Thank you, Mr. Chairman.

And I thank the witnesses for taking the time to be with us today. It is good testimony.

Mr. Purcell, I am from West Tennessee, a lot of farms, agribusiness is big, as in Texas. There is a severe drought right now that we are facing. We have been farmers for 7 generations, with ups and downs many, many times.

I want to just use a hypothetical and some real-time situations as well. Years ago we had some bad times, and I can remember my father going to the bank—our local community bank—and saying, "We have had a bad crop, a bad season, so I want to pay the interest on my notes." We had been doing business at the bank forever and ever. And my father and the banker were able to work out a solution to go forward and work down the road and end up paying the bank off in full.

Today, with what is happening with the drought situation in the country and all the farmers who are going to be short this year, do you still have that same authority and the flexibility to sit down with that customer and work out a solution or are we standing in the way?

Mr. PURCELL. We have the ability to do it, but I don't know that we could sustain it for very long with the regulatory climate, because everything needs to be loss-free. The reason you pay interest, that is the price for taking the risk.

But yes, we would attempt to do that. We would talk about the capacity. If you make a crop next year—the way we would actually structure it is that we would try to set up your carry-over over a 3-to 4-year period but you couldn't stub your toe 3 years in a row and—

Mr. FINCHER. Right.

Mr. PURCELL. —and come out okay.

Mr. FINCHER. Right.

Mr. PURCELL. So yes, we do try to do that.

One of the problems that may be ongoing is the Basel III, which we haven't even discussed, but your mark-to-market accounting on small loans, what is a drought-ridden agriculture loan in West Tennessee worth when he can't pay this year? What is the market value of that and who would buy it?

We can stop credit really fast if we have to go to mark-to-market. It is like, a guy comes in and he wants to borrow some money; he just inherited the land and he is going to use it for collateral, and we tell him to mark-to-market and he is okay. He is 150 percent collateralized.

And next year real estate values go down, and we mark it to market, we say, "We can't loan you the money because your value has gone down." And he says, "But I haven't had a loss."

Mr. FINCHER. Right.

Mr. PURCELL. So it is complicated.

Mr. FINCHER. And again, to Mr. Frank's comments a few minutes ago, the ranking member, about the—some of you not giving suggestions on the rules and what you wanted to see changed and all. The unfortunate part of what I hear when I am out in the district is that most of you were doing it right. You weren't doing things wrong.

So you were cooperating and working in the system as it was, and as you said a few minutes ago, we will—if the—if time goes on and the country exists, and it will, then we will have problems in the future. And us getting in the way most of the time—the unintended consequences usually will mess things up, we won't fix them.

To Ms. Del Rio, you talked about how successful you have been. Five years ago, you would charge the same rate or the same charge for doing business as you charge today? Nothing has changed?

Ms. DEL RIO. You mean in terms of the cost of our services? Yes, more or less. There might be some small modifications here and there, but more or less, we are the same.

Mr. FINCHER. So the charges would be the same?

Ms. DEL RIO. In terms of what we charge our members?

Mr. FINCHER. Right.

Ms. DEL RIO. Interest rates obviously have changed, so those would have been adjusted in accordance with prime rates and so forth, but in terms of fees, we have not raised fees.

Mr. FINCHER. Did your credit union take TARP money?

Ms. DEL RIO. Credit unions didn't take TARP money.

Mr. FINCHER. Any special government funding?

Ms. DEL RIO. Yes. Actually, in my testimony I talk about one of the actual regulatory tools that our credit union—that low-income credit unions that are certified as community development financial institutions by the Treasury Department in 2010 were able to apply for—

Mr. FINCHER. Why did you apply and need money if you were doing things so well?

Ms. DEL RIO. First, let me tell you what we received, if I may. This was actual money that was returned by the banks and was made available to community development financial institutions serving the most distressed neighborhoods.

And what it was was a loan—a secondary capital loan—and it was to strengthen our bottom line, our net worth, so that we could expand lending. So we specifically took that money so that we could increase small business and other lending in our neighborhoods which were the most affected by the economic crisis.

Mr. FINCHER. And you paid the loan back?

Ms. DEL RIO. It is over a length of 8 years, I believe, so we are in the process. We are only in our second year.

Mr. FINCHER. Okay.

And, Mr. Min, to wrap up, in your testimony I heard you say "unclear, uncertain" as we roll out, as we go forward. Dodd-Frank was enacted July 21, 2010—728 days ago. What happens—and I am a freshman Member of Congress, but I am afraid that we may be sitting here 3 years from now saying, what if it is unclear, it is uncertain, we need more stability because it is so big.

And Mr. Frank, again, said, well, a lot of times the regulators, they don't get blamed if they—someone doesn't make a loan, but if they make a bad loan they do, so they are overprotective of what is happening in the private sector. We are not recovering. If you saw the jobs numbers this morning—the jobless claim numbers this morning—this is not getting any better.

And this is just a monster. We are afraid. Absolutely, reforms after 2008, but to this magnitude? It just has to stop somewhere.

So with that, Mr. Chairman, I yield back. I am out of time.

Chairman NEUGEBAUER. I thank the gentleman.

And I thank the panel. I think we have had a great discussion today, and I think we have really been talking about the people that we need to be talking about: the consumers of financial products. Those are actually the people who are most affected by this.

I think we had some good dialogue, and I think one of the things that I feel encouraged about is there seems to be a bipartisan feeling that there are some areas that we need to take a look at. I look forward to working with my colleagues to do that.

I yield to the gentleman.

Mr. CAPUANO. Mr. Chairman, I ask unanimous consent to place 2 news articles in the record: one from The Wall Street Journal entitled, "Financial Crisis Amnesia," by Secretary Geithner; and another one from Forbes Magazine entitled, "What's in Your Wallet?" by Mickey Meece.

Chairman NEUGEBAUER. Without objection, it is so ordered.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for Members to submit written questions to these witnesses and to place their responses in the record.

And with that, this hearing is adjourned.

[Whereupon, at 12:22 p.m., the hearing was adjourned.]

A P P E N D I X

July 19, 2012

Testimony of Deyanira Del Rio
Chair, Board of Directors
Lower East Side People's Federal Credit Union

Before the House Financial Services Committee
Subcommittee on Investigations and Oversight

Hearing: Dodd-Frank's Impact on Communities, Small Businesses and Americans

July 19, 2012

Chairman Neugebauer, Ranking Member Capuano, and Members of the Subcommittee, thank you for inviting me to testify at today's hearing.

I am the Board Chair of the Lower East Side People's Federal Credit Union (LESPFCU), a not-for-profit community development financial institution in New York City. LESPFCU has a 26-year history of promoting savings and asset-building among low income families and stimulating economic development in the neighborhoods we serve. We manage $33.2 million in assets and serve more than 6,000 members. Approximately 82% of our members are low or moderate income; two-thirds are Latino. The majority of our borrowers are female heads of households.

Our credit union offers a full range of financial services, from savings and checking accounts to credit cards, business and real estate loans, and money transfer services. Since the credit union's inception, we have provided $60 million in capital to more than 8,500 families, small businesses, and nonprofit organizations in our target communities.

As a federally-insured depository institution, LESPFCU is subject to extensive consumer protection and safety and soundness regulations. I am pleased to comment on the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 on our financial institution and the communities we serve.

In my testimony, I would like to focus on four main points:

- The Dodd-Frank Act and other financial reforms have not impeded our credit union's ability to provide low-cost loans and services to our members.

- To the extent that our credit union is facing challenges, they result from the financial crisis and ongoing economic downturn – not from excessive regulation.

- Strong prudential regulation and consumer protections are needed to prevent future financial crises, and to ensure fairness and opportunity for low income consumers and communities.

- The Consumer Financial Protection Bureau has a vital role to play in regulating and leveling the playing field for depository and nonbank financial institutions.

1. **The Dodd-Frank Act and other financial reforms have not impeded our credit union's ability to provide low-cost loans and services to our members.**

The Dodd-Frank Act and other reforms enacted since the 2008 financial collapse have not caused our credit union to raise costs or eliminate services for our members. In fact, our credit union's lending has increased in recent years, from $16.9 million in 2007 to $22.4 million as of June 1, 2012. Fully 94.9% of our members' deposits are reinvested back in our communities, in the form of affordable housing, small business, and consumer loans. Approximately 95% of our small business loans are to women and minority owned businesses.

Our credit union is also serving more people than ever before. A record number of new members joined our financial institution last year, in part as a result of widespread mistrust of big banks and growing interest in credit unions. We continue to provide free checking (share draft) accounts to all members who maintain a balance of at least $25 at the credit union.

Our financial institution has not experienced a decrease in revenue as a result of credit card and overdraft reforms – primarily because we did not engage in unfair practices curbed by the CARD Act; nor did we rely on abusive overdraft fees, opting instead to provide traditional overdraft lines of credit and other responsible products to our members.

While our credit union supports the Dodd-Frank Act and the mission of the Consumer Financial Protection Bureau, it is important to note that the new regulatory framework makes accommodations for small financial institutions like ours. For example, as an institution with less than $10 billion in assets, we are supervised for compliance with consumer financial protection laws by our regulator, the National Credit Union Administration. In addition, the CFPB is required to assess the impact of its rulemaking on small financial institutions and small businesses.

2. **To the extent that our credit union is facing challenges, they result from the financial crisis and ongoing economic downturn – not from excessive regulation.**

To be clear, the lack of financial regulation and enforcement leading up to the financial crisis has created enormous burdens for small credit unions like ours – both directly and indirectly. When our financial institution considers challenges that we and our members are likely to face in the coming years, we are primarily concerned about the effects of continued unemployment, a depressed interest rate environment, and the ongoing foreclosure crisis.

These dire economic conditions have harmed our credit union, even though we played no part in causing them. A growing number of our members, for example, have lost jobs and income, which has resulted in higher loan delinquency at our credit union over the past year. In assessing delinquent and charged-off loans, we have identified few underwriting deficiencies, and instead find that they reflect continued economic distress in the neighborhoods we serve, which are among New York City's poorest.

To mitigate these risks, LESPFCU has taken greater advantage of Small Business Administration (SBA) and other loan guarantees; participated in loans with other credit unions; restructured delinquent loans; and raised secondary capital investments from both public and private sources – all of which are important tools permitted by our regulators.

The subprime lending and foreclosure crisis has imposed tremendous costs on the credit union system in another important way. In 2009, the National Credit Union Administration established a Stabilization Fund to stabilize corporate credit unions (institutions that serve as clearinghouses for credit unions like ours) that had invested in what turned out to be toxic mortgage-backed securities. All credit unions must now pay a percentage of their assets into the fund annually. These assessments, which are a direct hit to credit unions' net worth, have harmed many credit unions' ability to lend and grow, and helped lead to the demise of numerous low income credit unions across the country.

In short, effective consumer protection and safety and soundness regulation and oversight would have benefited our credit union, and prevented the hemorrhaging of billions of dollars from the credit union system.

3. **Strong prudential regulation and consumer protections are needed to prevent future crises and to ensure fairness and opportunity for low income consumers and communities.**

In the years leading up to the financial crash, lack of financial regulation permitted abusive lending practices to reach crisis proportions. The economic and social repercussions of the ongoing foreclosure crisis, bank failures, and corrupt financial practices being uncovered on a seemingly weekly basis will be felt by American families and communities for years to come. The Federal Reserve has estimated that the median net worth of American families fell by almost 40% between 2007 and 2009 – losses that will take years, possibly generations, to recover.[1]

In addition to lost wealth, a growing number of families are contending with damaged credit histories as a result of predatory lending and foreclosures, increasingly aggressive debt collection tactics, medical debts, and layoffs. Damaged credit, in turn, blocks many Americans not only from future credit and homeownership opportunities, but also from affordable rental housing, jobs, and other economic opportunities that could help them get back on their financial feet and assist in economic recovery.

Congress enacted the Dodd-Frank Act in 2010, in the wake of undeniable regulatory failure and egregious lending practices that destabilized neighborhoods across the country, and nearly brought down the global economy. Among the Act's provisions is a requirement that lenders consider borrowers' ability to repay loans – a fundamental tenet of responsible lending that was lost during the credit boom. Our credit union supports

[1] *Changes in U.S. Family Finances from 2007 to 2010: Evidence from the Survey of Consumer Finances*, http://www.federalreserve.gov/pubs/bulletin/2012/pdf/scf12.pdf

such common sense regulations, which we believe will go far to preventing similar future crises.

Opponents of financial regulation frequently point out that the Act goes too far – citing its more than 2,000 pages and authorization of up to 400 new rule-makings. In our view, given the size, complexity, importance, and massive failures of our financial sector, we question whether Dodd-Frank will go far enough.

Ultimately, irresponsible and unchecked lending practices undermine our credit union's work to promote savings and asset development, and pose a significantly greater threat to our financial institution's long-term sustainability than the relatively short-term and marginal costs of regulatory compliance.

4. **The Consumer Financial Protection Bureau has a vital role to play in regulating and leveling the playing field for depository and nonbank financial institutions.**

LESPFCU welcomed the creation of the CFPB as the first agency tasked specifically with protecting consumers in the financial services marketplace – a function that was sorely missing in the years leading up to the crash. From hidden overdraft fees and triple digit APR tax refund loans to predatory "No-Doc" and Payment Option ARMs, low income communities across New York and the country were flooded with high-cost, exploitative products that regulators failed to curb. As we all now know, abusive lending practices harmed not only borrowers and their communities, but exposed the financial services system to broad, systemic risk.

This regulatory failure is particularly distressing because many of the problems we are currently facing could have been avoided, had regulators paid meaningful attention to the harms that reckless lending practices wreaked on families and communities. By ostensibly focusing on safety and soundness examinations at the expense of consumer protection, regulators ironically failed to detect the systemic risks caused by predatory lending (which was, after all, lucrative in the short-term).

We are particularly supportive of the CFPB's powers to regulate and supervise nonbank entities in the financial services market. Prepaid debit card companies and money transmitters, for example, have a growing presence in the communities we serve, yet have been insufficiently regulated, particularly with respect to fees and consumer protections. Many of our credit union members have been harmed by aggressive and often illegal debt collection practices by debt buyers, which harass and often file lawsuits against consumers for old and invalid debts. These tactics devastate people's credit reports and scores, and can lead to unwarranted wage garnishment and seizure of bank account funds.

Just this week, the CFPB announced that it will supervise the nation's major credit reporting agencies under its larger participants rule – bringing this industry, which has an outsized impact on people's lives and economic opportunities, under meaningful federal supervision for the first time.

LESPFCU and many of our partner credit unions have engaged directly with CFPB Director Richard Cordray and staff at field hearings and regional meetings, and indirectly in comment letters on various issues and proposed rules. We have been impressed so far by the thoughtfulness of the CFPB's approach to rulemaking, and the many ways in which the bureau has reached out to and solicited feedback from financial institutions, small businesses, and individuals. We believe that the CFPB's efforts to promote transparency and accountability in the financial services marketplace will confer benefits to our members and our financial institution that far outweigh the costs of regulatory compliance.

I look forward to answering your questions and thank you again for this opportunity.

House Committee on Financial Services,
Subcommittee on Oversight and Investigations

Testimony of Michael Flores
CEO, Bretton Woods, Inc.
July 19, 2012

Thank you Chairman Neugebauer, Ranking Member Capuano, and Members of the Committee. I'm Michael Flores, CEO of Bretton Woods, Inc. a management consulting and research firm that specializes in financial institutions, primarily commercial banks and alternative financial service providers. I have more than 30 years' experience in the banking and consulting focusing on strategy and earnings improvement programs. Additionally, I have published several articles and studies on the financial services industry, including overdrafts, short-term credit alternatives and general purpose reloadable and payroll prepaid cards.

Because this hearing is about both the intended and unintended consequences of the Dodd–Frank Wall Street Reform and Consumer Protection Act on communities, small businesses and individuals, I am here to describe both my analysis of the issues as well as relate comments from my clients and others in the industry about their assessment.

In general, while Dodd-Frank was written to address the causes of the financial meltdown of 2008, the end result of the legislation and promulgated regulations are having a disproportionate and negative impact on financial service providers that played no role in the cause of the problems.

Simply stated, Dodd-Frank has and will:

- Substantially increased compliance costs for banks
- Increased fees to small businesses and consumers
- Decreased products and services such as the limited functionality prepaid card offered by banks over $10 billion in assets
- Increased the number of under-banked and the newly coined term, de-banked individuals
- Decreased number of branch offices as in low to moderate income markets as banks attempt to reduce expenses and focus on profitable markets

Contrary to making financial services more available, affordable and consumer friendly, the increased restrictions and compliance costs are reducing services to small businesses and consumers, which have a negative effect on the economic well-being of the communities they serve.

Additionally, the 6,700 community banks (under $1 billion assets) and the 7,000 credit unions are burdened with legacy operating costs and dated technologies that inhibit their ability to profitably serve their constituencies, The 60 million to 70 million low to moderate income consumers and local small businesses are particularly hard hit.

Resources that could be used to update technologies and create more efficient operations are now allocated to regulatory and compliance purposes. Staff dedicated to non-revenue or non-customer service activities is the fastest growing area of most banks and credit unions.

Both transaction accounts (checking) and credit options are impacted. Our own studies indicate that it is unprofitable for most banks and credit unions to individually underwrite loans under $5,000. The traditional options of overdrafts, credit card advances and home equity loans are no longer viable because of the poor economy and regulations. With the reduction of overdraft and interchange fees, many banks have eliminated free checking accounts. The new fee structures are complex making transparency more difficult.

The reduction of interchange fees has actually resulted in a "wealth transfer" from consumers to merchants. The lack of the savings being passed on the consumers is not just large merchants increasing their profit margins; there are also processing issues that do not allow identifying individual cost savings, but also contractual limitations that do not allow any cost reductions (e.g. convenience fees to accept cards as payments).

I contacted several of my clients as well as others in the industry to solicit their feedback on these issues. Because on non-disclosure agreement with my clients, I cannot identify the individuals and organizations, however, they represent community and large banks as well as large card issuers.

The following items highlight their quotes of key concerns:

1. "The basic story is (1) more fees, (2) a reduction in free checking, (3) an increase in the number of de-banked and unbanked households, and (4) a shift from credit cards and bank accounts to traditionally non-mainstream products. The next shoe that is dropping is also a reduction in the number of bank branches."
2. "The unintended consequences (of Dodd-Frank) cannot be fully determined because according to the law firm Davis Polk of the almost 400 rulemakings required by the law, only a quarter have been finalized, while 36% have not even been proposed."
3. "The greatest potential unintended consequence will be the demise of traditional community banks and the impact on access to credit for consumers and small businesses in small communities. Community banks will be forced to consolidate because they cannot afford the compliance costs."
4. "There has been a significant decline of traditional wholesale purchasers of residential mortgages from mortgage bankers/brokers. Some large have left the business which significantly reduces access to mortgage credit particularly for those without an established relationship with a bank. The compliance requirements contained in Dodd Frank are causing many community banks to get out of the mortgage business or only offer variable rate products underwritten to strict credit quality guidelines. Many banks are

reluctant to sell to Fannie and Freddie because of the potential repurchase risk which is also why many of the wholesale purchasers are getting out of that business."

5. "Consumer and mortgage banking will be consolidated in the largest banks which can afford the compliance costs which will reduce access to credit for the under-banked."
6. "The requirement to get new appraisals and update Credit Reports on renewals and existing loans creates extra costs to the customer. This requirement is regardless of the market or strength of the customer."
7. "There is substantial reduction in fee income sources to banks, primarily the result of the Durbin Amendment. To address this, banks are raising fees and charging fees for products previously offered for free which has a disproportionate impact on the under-banked. In essence this is creating a new class of consumers, the de-banked."
8. "The rules implementing Section 1071 of Dodd Frank have not been promulgated but will have a chilling effect on small business lending. To ensure that lenders aren't discriminating against minority groups based on price, this rule will significantly limit lenders' ability to structure loans to meet the specific needs of the customer."
9. "Painting Alternative Financial Service providers with a broad regulatory brush will reduce access to credit and payments services to those who need options most."
10. "Dodd Frank will drive up the cost of credit for consumers and small business borrowers especially as loan demand picks up."
11. "The wild card is the repeal of Regulation Q and the impact on a bank's cost of funds and in turn (increase) the cost of credit as interest rates start to rise."
12. "Dodd Frank will result in the biggest banks getting bigger which is 180 degrees from the original intent."
13. "There is negative impact on the unaffiliated network routing on government benefit programs. Many government programs do <u>not</u> want cash access and therefore are signature only. Adding a PIN network to comply with the network routing provisions opens the programs up to cash back at point-of-sale, which is not what the governments' sponsoring the programs intend or want. Cash access makes it much harder to restrict card-based benefits to designated uses."
14. "Consumers are not benefiting from the reduction of interchange fees. Even if a merchant wanted to pass the savings to the consumer, transaction bundling for processing and contractual agreements for assessing convenience fees precludes the possibility of identifying and passing any savings to the consumer. For example, the IRS has negotiated a flat fee of $3.89 to $3.95. This has not changed since the implementation of Durbin."
15. "From a large prepaid card issuer perspective (i.e. $10B+), there are the unintended consequences that has come as a result of Durbin.
    a. Convenience Checks for payroll. It is anti-consumer that they can only be cashed to the total in the account and only the cardholder can be the

payee. While limited in usage, its usefulness to cardholder is even more limited now.

b. Removal of Pay Anyone Bill Pay - less utility for the cardholder so now they have to find an alternative means to pay bills which will probably cost them a fee
c. Card Access Only to Accounts that eliminated Card to Card and Card to Account Transfers
d. Since overdraft is eliminated, issuers have had to raise the pre authorization at the Automated Fuel Dispenser to $75. If you don't have at least $75, you have to go inside and tell the attendant how much gas you want to pump."

16. Referencing General Purpose Reloadable Prepaid Cards, "...the impact on the rollback of federal preemption for agents, and now program managers that want to offer product and reloads at retail are having to run out and get state money transmitter licenses, which is turning out to be a huge cost and compliance obligation. The remittance rule is going to drive up costs and reduce competition for consumer remittances to foreign countries."

Congressman Frank, in a letter to Chairman Ben Bernanke, dated February 29, 2012, states that "...the Board's decision to condition the reloadable prepaid card exemption from interchange fee restrictions on the card being 'the only means to access underlying funds' associated with the card – might inadvertently result in consumers not having access to useful features or services.".

In conclusion, the causes of the financial crisis have been identified and there was plenty of blame to go around. However, Dodd-Frank with the Durbin Amendment and the CFPB, we have layered significantly more regulation over existing regulation to the point of making the traditional business model for community banks almost unworkable. Historically, it is the community banks that understand the needs of their markets and have been a catalyst to local and regional economic growth.

At the same time, Dodd-Frank is creating roadblocks to innovators such as alternative financial service providers who are working diligently to address the under-banked segment of our society. Without relief, these entrepreneurial innovators will be severely hampered in the development and distribution of the products and services that the low to moderate income consumers require.

Many provisions of Dodd-Frank are threatening the existence of community banks and other financial innovators and do not to address the causes of the 2008 financial crisis. In essence, some provisions of Dodd-Frank are solutions looking for problems – problems that do not exist for the majority of financial institutions in the Unites States.

Thank you and I look forward to answering your questions.

Hearing Entitled "Who's In Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses"

Testimony of Garrick "Gary" Johnson, President, American Flooring Installers, LLC, on behalf of the Ohio Hispanic Chamber of Commerce

Before the House Financial Services Committee's Subcommittee on Oversight and Investigations

July 19, 2012

Good morning, Mr. Chairman, Ranking Member Capuano, and other Members of the Subcommittee. My Name is Gary Johnson, and I am the owner, President and CEO of a small, but fast-growing construction business in Toledo, Ohio, called American Flooring Installers. I am testifying today on behalf of the Ohio Hispanic Chamber of Commerce, where I currently am Chairman. The primary objective of our Chamber is to promote the development and continued growth of the Hispanic business community in Ohio. It is a pleasure to appear before you today.

In my testimony this morning I want to tell you a little bit about my company, and also provide you with a personal account of some of the ways in which I am using financial products and services to run and grow my business. I know that I am here to talk about the effects of regulation, but I hope that if I tell you how my business works, and how I use financial products, it will help when you consider proposals for new regulations. My company currently has 23 full-time employees and we had gross revenues for 2011 of approximately $1.8 million. I am looking to hire additional workers and we are on track to double our revenues this year. One part of meeting that goal is the financial products and services that we and our customers use.

A healthy financial sector is important for businesses of all sizes, especially small businesses like mine. In the business community, many of us are concerned that the new financial sector law enacted by Congress is indirectly hurting small businesses through tighter lending standards and new or increased fees for routine financial services for business and consumer banking customers.

Among the subjects that always seem to come up when I talk with other Chamber members is the challenge with cash flow. Many of us believe that this challenge has been exacerbated by the law enacted by Congress in response to the financial crisis. While less regulation in some areas has contributed to the necessity for government to act, over-regulation has made it extremely hard to obtain the necessary funding needed to grow many small businesses. We are concerned that over-regulation is making it harder for banks to make credit card loans to us and harder for our customers to use payment cards too. These cards are essential for cash flow on both the expense and revenue side of a small business. Other options such as lines of credit either take too long to obtain, or simply are not available.

When I accept payment cards from my customers, I get paid faster, and that time-value of money means I get paid more relatively speaking. One tool that I am increasingly using to enhance my cash flow involves the acceptance of payment cards using a device attached to my mobile phone. The device allows me to accept credit and debit card payments while I am face-to-face with a customer. If I am out on a job, using that device, I know whether or not I am going to get my money within the next three days. If the payment is declined, I know about it right then and there and can address it with my customer. If the authorization goes through, then I know I can put that money back to work within three days.

I accept anywhere from $2,500.00 to $10,000 per month on cards and it would be great if more of my customers paid me this way instead of sending a check. Again, accepting payment cards enables me to get paid typically within a few days. This is light years faster than the invoice system I otherwise use that typically results in me receiving a payment from a customer by check which can take as long as 60 or 90 days. Also, with payment cards, small businesses do not need to worry about bounced checks. Even though I pay a fee to accept card payments, I prefer them as a payment method because I get access to my funds almost immediately. That allows me to put that money back to work in my business on a near real-time basis. When I receive payment from my customers more quickly, I can put that money to work quickly in growing my business.

Also, if you consider what I pay to accept payment cards as opposed to the cost of me essentially floating a loan to a customer for 60 to 90 days when I could be putting that cash back to work in my business, it is a no-brainer. I have learned, not from a book, but from my business, about the time value of money. I want to keep going back to that, because knowing the time value of money is one of the keys to successfully growing your business.

The situation I just described hits me in two ways. Even if I was not growing my business, during the 60 to 90 day period I have to wait to have an invoice paid by check, I have to pay the employees that worked on the job out of other funds. I lose the use of that money and the money I am owed. I cannot even earn interest on it and, as I said, I am basically extending a loan. When I am growing my business, the impact is even worse. In my view, if laws and regulations make it harder for banks to make payment cards available to my customers, or make it harder for companies to develop innovative products like my mobile phone device, that hurts my business.

Of course, like all businesses, I want to pay less for almost everything that I use in my business. However, if the State of Ohio limited what I could charge to install a wood floor in a government building – I do a lot of work for the State of Ohio – to some percentage of my costs, I can guarantee you that I would do my best to recover my costs across the rest of my lines of business. If the limit was too much, would I stop doing that line of business? Probably so. But no matter what, I would try and grow other areas of my business as opposed to devoting resources to that area of business.

Let me be clear that I do support having some "rules of the road," as long as I know what those rules are and they make it easier – or I should say better – for both my customers and I to do business. Of course, it would not be fair if the rules were drawn up in my favor, and I certainly do not want someone dictating basic choices or business decisions. I think in many cases that we swing back and forth too far in both directions. As a small business, I can't always see it coming and I can't always duck. Not only are extremes bad, there is the not knowing what is coming.

So, I just want to say that if Dodd-Frank, or any other legislation like it, does any of the things I have just talked about, then I would most likely oppose it or whatever parts of it had the effects that hurt my business.

While I am here, I also want to talk about how my business uses credit cards for purchasing so that you can consider that when you pass laws. In addition to accepting payment cards, I also use a credit card to pay some of my vendors for supplies and materials. Many small businesses do this. A credit card provides me with an easy way to purchase things I need to keep my business going. It also helps me to continue doing business while enduring the time and process it would take to get a small-business loan. I find that other businesses often prefer when I pay this way because, like me, they want to get paid faster and want to avoid the lag time that occurs with invoicing and check payments. In fact, some of my suppliers and vendors will give me a discount for timely payments I can make with my credit card. This provides me with another way to help cut costs and grow my business. Like many small businesses, we keep a close eye on the credit available to us, and if over-regulation keeps banks from making that credit available, we will suffer for it.

In my experience, any regulation that increases costs to businesses – regardless of the industry – will ultimately be borne by the businesses' customers in the form of higher prices. In the case of banks, that can mean increased costs for small businesses in various ways.

It is difficult for me to characterize exactly how the new financial sector law enacted by Congress has impacted the banks because I am not a banker. Others witnesses are better suited to speak to those issues. What I can say is that in the wake of the financial crisis it is crucial that Congress and regulators not react so strongly that the good parts of banking that we rely on – the parts that were not involved in the financial crisis – cease to be viable and healthy. When small business is healthy, the economy is healthy.

I appreciate the opportunity to testify before you today, and would be happy to answer any questions you may have.

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Written Testimony of

David K. Min
Assistant Professor of Law
University of California Irvine School of Law

Before the House Financial Services Committee
Subcommittee on Oversight and Investigations

"Who's in Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses"

Thursday, July 19, 2012
10:00am
2128 Rayburn House Office Building

Chairman Neugebauer, Ranking Member Capuano, and members of the subcommittee, my name is David Min and I am an Assistant Professor at the University of California Irvine School of Law, where I teach and research in the area of banking law and financial regulation. I previously spent over a decade working in the law and policy of financial regulations, both in private practice and in the federal government, including as a Senior Policy Advisor for the Joint Economic Committee of Congress. I thank you for the opportunity to return here today to testify on the topic of the costs of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as I believe this is an issue that has been fraught with confusion.

Before I get into the issue of the impacts of Dodd-Frank, I would like to note that the entire concept of attempting to quantify the costs and benefits of financial regulations suffers from a number of critical flaws. As the Office of Management and Budget has noted, cost-benefit analysis is "highly speculative" and requires the use of many tenuous and uncertain assumptions.[1] Cost-benefit analysis is also quite costly and time-consuming for resource-constrained regulators. And it tends to be biased against all financial regulations, since the costs of such regulations are easily quantified, whereas the benefits are more difficult to quantitatively assess. What are the quantitative benefits of transparency, financial stability, and promoting investor confidence, which have been the main goals behind financial regulation in the United States since the 1930s? Whatever these benefits

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[1] OFFICE OF MGMT & BUDGET, 2011 REPORT TO CONGRESS ON THE BENEFITS AND COSTS OF FEDERAL REGULATIONS AND UNFUNDED MANDATED ON STATE, LOCAL, AND TRIBAL ENTITIES, at 4 (2011).

are, they are not typically captured by cost-benefit analysis, as they are too diffuse, uncertain, and incalculable.[2]

Because the use of cost-benefit analysis tends to stack the deck against financial regulation, you and your colleagues in Congress expressly chose not to include a cost-benefit analysis requirement in Dodd-Frank when you passed this bill in 2010.

But let's ignore the problems with cost-benefit analysis, and try to answer the question posed by this hearing. What are the impacts of Dodd-Frank for communities, families, and small businesses? I would like to make three main points in my testimony.

First, the negative impacts of Dodd-Frank to date have been greatly exaggerated. The fact is that Dodd-Frank has not had much of an impact to date, because most of it has not yet been implemented, due to a successful campaign by Wall Street lobbyists, who spent a record $302 million in 2010 alone to delay and undermine the implementation of this law.[3] As of July 2, 2012, less than 30% of the rules mandated by Dodd-Frank had been issued in their final form.[4] Most of these have only been issued in the last few months.[5] It is difficult to understand the claim that Dodd-Frank has resulted in large burdens for consumers and small businesses, given that it has mostly not yet taken effect.

Second, most of the burdens attributed to Dodd-Frank by its critics are misplaced or highly speculative in nature. Because of the severe delays in implementing Dodd-Frank, it is

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[2] An upcoming brief by the policy think tank Better Markets provides a robust discussion of cost-benefit analysis and its flaws as a tool for evaluating financial regulations.
[3] *See* Bobby Caina Calvan, *Two Years Later, Dodd-Frank Law is Largely Stalled*, THE BOSTON GLOBE, July 16, 2012, *available at* http://articles.boston.com/2012-07-16/nation/32686074_1_dodd-frank-law-volcker-rule-rule-making-process.
[4] Davis Polk LLP, *Dodd-Frank Progress Report*, July 2012, available at http://www.davispolk.com/files/Publication/8bc2b1c4-c800-45b1-8324-0381454f6ceb/Presentation/PublicationAttachment/b9462d4e-0be9-4eee-9829-0455bca61e9a/July2012_Dodd.Frank.Progress.Report.pdf.
[5] *Ibid*.

impossible to know what the actual impacts of Dodd-Frank will be. Thus, most of the claims about the costs of Dodd-Frank are based on unfounded speculation, and many of these claims are flat-out wrong. For example, as I discuss below in greater detail, many critics of Dodd-Frank have agued that the law's regulation of swaps would result in greatly increased costs for end users who utilize swaps for legitimate hedging purposes. In fact, this argument is baseless, as the Commodity Futures Trading Commission specifically exempted such end users when it released its final rule in this area last week.

Moreover, there has been a high degree of confusion between negative impacts caused by Dodd-Frank and those caused by the financial crisis. Most of the burdens on consumers and small businesses being blamed on Dodd-Frank are actually the result of the financial instability that led to the enactment of this law. For example, many have blamed Dodd-Frank for tightening underwriting standards and reducing the availability of credit for consumers and small businesses. In fact, the lack of liquidity in the credit markets was clearly caused by the financial crisis and predates Dodd-Frank,[6] which has still not finalized its rulemaking on issues that might actually impact underwriting and the cost of consumer credit, such as the "Qualified Mortgage" standard for mortgage lending.

Finally, to state the obvious, in considering the impacts of Dodd-Frank on families, communities, and small businesses, we should consider the many positive impacts that this law may have. The increased financial stability, improved investor confidence, and enhanced consumer protection created by Dodd-Frank should lead to a myriad of benefits, both small and large. As has been well documented, the benefits of financial stability for families, communities and small businesses are enormous. The recent financial crisis

[6] *See, e.g.*, Meta Brown and others, *The Financial Crisis at the Kitchen Table: Trends in Household Debt and Credit*, Federal Reserve Bank of New York Staff Report no. 480, Dec. 2010.

resulted in lost household wealth of approximately $10 trillion.[7] While many critics have focused on the length of Dodd-Frank—2300 pages—if this law prevents a similar financial crisis from occurring, it would save American households approximately $4.3 billion per page.

Dodd-Frank has had minimal impact so far, because it has not yet taken effect

It is important to note that, to date, the actual impacts of Dodd-Frank, either positive or negative, have been de minimis, because this law has mostly not yet taken effect. According to the law firm Davis Polk LLP, which has been tracking Dodd-Frank's implementation, as of July 2, 2012, less than 30% of the rules required by Dodd-Frank had been issued in their final form, with most of these final rules have only been issued in the last few months. More than 35% of the rules required by Dodd-Frank had not yet been proposed in any form.[8]

The extremely slow implementation of Dodd-Frank, which on Saturday will have been signed into law exactly two years ago, is due in large part to a coordinated strategy by Wall Street, which has sent an army of lobbyists to slow down the pace at which these new rules have been implemented.[9]

As a result of its delayed implementation, Dodd-Frank has so far had minimal impact on families, communities, and small businesses.

Most of the negative impacts attributed to Dodd-Frank are unfounded

[7] Anthony J. Crescenzi, "Cyclical Tailwinds, Secular Headwinds and the Market of Bonds," PIMCO (originally published on CNBC.com), Apr. 7, 2010, available at http://www.pimco.com/EN/Insights/Pages/Viewpoints%20Crescenzi%20April%202010.aspx.

[8] Davis Polk LLP, *Dodd-Frank Progress Report.*

[9] Calvan, *Two Years Later.*

One of the problems with the debate over the impacts of Dodd-Frank is that, to date, there has been too much uninformed hyperbole and too little actual data. We do not actually know the impact of Dodd-Frank on families, communities, and small businesses because virtually all of the changes envisioned by Dodd-Frank have not yet or only recently been implemented. As a result, we simply do not have a reasonable basis to know what the impacts of Dodd-Frank will be. Almost all of the claims being made about the negative impacts of Dodd-Frank have been based on unfounded, and frequently wildly incorrect, speculation.

For example, many critics of Dodd-Frank have claimed that its proposed regulation of derivatives would dramatically increase the costs for end users who currently utilize these derivatives for hedging.[10] This argument has been based on pure speculation, as the Commodity Futures Trading Commission, the regulatory agency responsible for promulgating the derivatives regulations envisioned by Dodd-Frank, did not release its first salvo of final rules on this issue until last week. Moreover, this argument has proven baseless, as the CFTC's actual final rules defining the scope of its derivatives regulations crafted a broad exemption for end users seeking to use derivatives for hedging purposes, as well as for small banks with less than $10 billion in assets.[11]

Similarly, while there has been much grumbling about the compliance costs for small depository institutions, such as community banks and credit unions, it is not clear that Dodd-Frank will actually lead to increased compliance costs for these lenders. The primary evidence that Dodd-Frank will lead to greater compliance costs is its 2300 page

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[10] *See, e.g., Think the Dodd-Frank Act's Impact is Felt Only on Wall Street?*, House Financial Services Committee website, *available at* http://financialservices.house.gov.
[11] Commodity Futures Trading Commission, *End User Exception to the Clearing Requirement for* Swaps, Final Rule, 17 C.F.R. Part 39.

length. But Dodd-Frank is primarily targeted at non-bank activities, such as securitization, derivatives trading, and proprietary trading, or the activities of very large bank holding companies with at least $50 billion in assets. Of the 16 titles in the Dodd-Frank Act, only two might potentially lead to in higher compliance costs to small banks—Title X, which creates the Consumer Financial Protection Bureau; and Title XIV, which aims to establish standards for mortgage origination and servicing. Neither Title has yet led to final rules that would substantially affect the vast majority of small banks. Furthermore, it is likely that the final rules implementing these Titles will frequently contain exemptions for small banks.

It is also important to recognize that neither Title X nor Title XIV creates obligations that are inconsistent with the past regulatory obligations owed by banks, which have long been subject to a high degree of regulation in return for the federal deposit insurance they enjoy. Many of the major changes being contemplated by the CFPB are derived from its authority under Regulation Z of the Truth in Lending Act; small banks were already required to adhere to Regulation Z, which imposed limitations on the lending practices and loans that could be originated by banks.[12] Indeed, the limitations on high cost loan features proposed by Dodd-Frank under Titles X and XIV are actually perfectly consistent with the regulations that governed banks during the Quiet Period. For example, the prohibition on balloon payments in mortgages, which has been protested by many as an unprecedented

[12] Federal Reserve, Regulation Z, *available at* https://www.federalregister.gov/articles/2010/09/24/2010-20665/regulation-z-truth-in-lending.

assault on the banking system, was actually a major feature of the regulation of thrifts from the 1940s to the 1980s.[13]

Indeed, it is possible that Dodd-Frank may actually reduce compliance costs for small banks and other small depository institutions, since it consolidates various authorities, which had previously been scattered among the Federal Reserve, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, the Federal Deposit Insurance Corporation, and the Federal Trade Commission, among others, into one central body, the CFPB.

There has also been a considerable amount of conflation between the impacts of the financial crisis and the impacts of Dodd-Frank. Most of the negative impacts being attributed to Dodd-Frank are actually the result of the financial crisis, which Dodd-Frank was intended to address. For example, some have argued that consumer credit and mortgage credit have been constrained because of Dodd-Frank.[14] In fact, the lack of liquidity in these credit markets predates the passage of Dodd-Frank,[15] let alone the implementation of Dodd-Frank's rules impacting consumer and mortgage credit, which has yet to occur. Tighter credit availability runs across all credit categories, including consumer credit, commercial real estate, small business, and home mortgage loans, and is primarily

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[13] *See* Richard Green and Susan Wachter, "The Housing Finance Revolution," Paper Presented at *Housing, Housing Finance and Monetary Policy*, Federal Reserve Bank of Kansas City 31st Economic Policy Symposium (Aug. 30 – Sept. 1, 2007), at 19-20; Robert Van Order and Lynn Fisher, *Economics of the Mortgage and Mortgage Institutions: Differences between Civil Law and Common Law Approaches*, ROSS SCHOOL OF BUS. WORKING PAPER SERIES, No. 1081 10-11 (2006); and John M. Quigley, Federal Credit and Insurance Programs, FED. RES. BANK OF ST. LOUIS REV. 88 (4), 281, 282-88 (2006).

[14] *See Think the Dodd-Frank Act's Impact is Felt Only on Wall Street?*

[15] *See, e.g.*, Meta Brown and others, *The Financial Crisis at the Kitchen Table: Trends in Household Debt and Credit*, Federal Reserve Bank of New York Staff Report no. 480, Dec. 2010.

due to credit losses, both realized and anticipated, that have occurred as a result of the financial crisis.[16]

Claims about Dodd-Frank's impacts on economic growth are similarly contradicted by the facts. The Bureau of Labor Statistics continuously surveys employers to understand why they are laying off workers. In 2010, only 0.2 percent of lost jobs were attributed to government regulation. This compares to 30 percent who were let go because of a drop in consumer demand.[17] This data is consistent with the findings of economists, who have universally found that a drop in aggregate demand, attributable to the effects of the recent financial crisis, is primarily responsible for the anemic economic growth we are currently experiencing.[18]

We should not ignore the many positive impacts of Dodd-Frank

In the rush to point out the negative burdens that Dodd-Frank may create, we have forgotten the plethora of positive impacts that this law is certain to create, which I think can generally be put into three categories. First, Dodd-Frank increases financial stability. Second, it improves investor confidence and promotes market transparency. Third, it provides significant benefits for consumers, which in turn help to promote financial stability. I briefly discuss each of these below.

The positive impacts of increased financial stability

[16] *See* Office of the Comptroller of the Currency, *Survey of Credit Underwriting Practices*, June 2011, *available at* http://www.occ.treas.gov/publications/publications-by-type/survey-credit-underwriting-practices-report/pub-survey-cred-under-2011.pdf.
[17] BUREAU OF LABOR STATISTICS, U.S. DEP'T OF LABOR, REP. 1038, EXTENDED MASS LAYOFFS IN 2010, at Table 6 (Nov. 2011).
[18] *See, e.g.*, Jia Lynn Yang, *Does Government Regulation Really Kill Jobs? Economists Say Overall Effect is Minimal*, WASH. POST, Nov. 13, 2011; Lawrence Mishel, *Regulatory Uncertainty Not to Blame for Our Jobs Problem*, THE ECON. POL'Y INST. BLOG, Sept. 27, 2011, *available at* http://www.epi.org/blog/regulatory-uncertainty-jobs-problem.

The overriding goal of Dodd-Frank was to increase financial stability and prevent another financial crisis of the sort we just experienced. Financial instability is extraordinarily costly, as our recent experience suggests. The recent costs of the financial crisis we just experienced include:

- Over $10 trillion in lost household wealth,[19] approximately 23 percent of the average household's total stored wealth.[20]
- 9.5 million lost jobs.[21]
- An average decline in income of $5,800 per household.[22]
- 10.9 million homes in foreclosure proceedings.[23]
- 33% peak-to-trough decline in home prices.[24]
- The opportunity costs of providing trillions of dollars in TARP and Federal Reserve support to restore and maintain liquidity in the financial markets.

It is important to note that these types of losses were regularly incurred by U.S. households, as major financial crises occurred every five to ten years until your predecessors in Congress decided to stringently regulate banking and other risky financial activities in the 1930s. At the time, much like today, Wall Street and its allies criticized these financial regulations as "unwarranted" attacks that would devastate the country, impede economic growth and inhibit capital markets activities.[25] In fact, what we saw was

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[19] Anthony J. Crescenzi, "Cyclical Tailwinds, Secular Headwinds and the Market of Bonds," PIMCO (originally published on CNBC.com), Apr. 7, 2010, available at http://www.pimco.com/EN/Insights/Pages/Viewpoints%20Crescenzi%20April%202010.aspx.

[20] Jesse Bricker and others, "Surveying the Aftermath of the Storm: Changes in Family Finances from 2007 to 2009," Washington: Federal Reserve Board Finance and Economics Discussion Series, 2011.

[21] Philip J. Swagel, "The Cost of the Financial Crisis: The Impact of the September 2008 Economic Collapse," Briefing Paper No. 18, Pew Financial Reform Group, 2010, p. 11, available at http://www.pewtrusts.org/uploadedFiles/wwwpewtrustsorg/Reports/Economic_Mobility/Cost-of-the-Crisis-final.pdf?n=6727.

[22] Ibid, at 9.

[23] "The Impact of Dodd-Frank's Home Mortgage Reforms: Consumer Market Perspectives," *Hearing Before the H.R. Comm. on Fin. Services Subcomm. on Fin. Inst. and Consumer Credit,* 112th Congress (2011) (statement of Eric Stein, Center for Responsible Lending), available at http://www.responsiblelending.org/mortgage-lending/policy-legislation/congress/Stein-Testimony-for-House-Financial-Institutions-Subcommittee-Hearing.pdf.

[24] *See* S&P/Case-Shiller 10-City Composite Home Price Index.

[25] *See* Marcus Baram, *The Bankers Who Cried Wolf: Wall Street's History of Hyperbole About Regulation*, THE WATCHDOG, HUFFINGTON POST, June 21, 2011, *available at* http://www.huffingtonpost.com/2011/06/21/wall-street-history-hyperbole-regulation_n_881775.html.

the exact opposite, as we experienced an unprecedented period of financial stability and market transparency that led to the greatest period of prosperity and efficient capital formation in the history of the world.[26] The benefits of increased financial stability, in other words, are enormous.

Dodd-Frank aims to increase financial stability in a number of important ways, including: expanding prudential regulation to non-bank activities and entities that pose systemic risk, such as derivatives trading or hedge funds; heightening regulation for systemically important, or "too big to fail," financial institutions; and removing other sources of systemic risk. Most of these are relatively uncontroversial propositions outside of Wall Street. For example, imposing heightened capital requirements on large, systemically important financial institutions will certainly lead to greater costs for these firms, but it is also basically undisputed that the value added by reducing the leverage of these firms and thus reducing the risk of another financial meltdown is much greater than these costs.

The positive impacts of improved investor confidence and greater transparency

Dodd-Frank also seeks to restore investor confidence and introduce greater transparency in the U.S. financial markets. The 2008 financial crisis exposed a number of critical flaws in the U.S. financial system, including how asset-backed securities (and derivatives based on these securities) were created, rated, and sold. As a result, since the crisis, investors have stayed away from so-called private-label securities—those not backed by the federal government. Since the fall of 2008, there have been only two new

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[26] *Ibid. See also* Nicholas Economides et al., *The Political Economy of Branching Restrictions and Deposit Insurance: A Model of Monopolistic Competition Among Small and Large Banks*, 39 J.L. & ECON. 697, 698 (1996) (quoting Francis H. Sisson, the president of the American Bankers Association at the time of the passage of Glass Steagall, who predicted that bank deposit insurance and heavy regulation would ruin the banking system).

issuances of mortgage-backed securities, both from the same firm, accounting for less than $600 million. By way of comparison, there were approximately $1.2 trillion in private-label MBS issued in 2005, at the height of the market.

Dodd-Frank proposes a number of important changes meant to fix the problems illustrated by the crisis, and thus bring back investors into the marketplace. Among these are increased regulation of credit rating agencies and a risk retention requirement meant to align the interests of MBS sponsors and investors. These will undoubtedly result in some increased regulatory burdens for affected parties, but they should also create large positive effects as well, particularly if they restore investor confidence in U.S. capital markets.

Dodd-Frank's attempt to increase transparency in the derivatives market, by requiring that certain classes of heavily traded swaps be centrally cleared and exchange traded, should also lead to outsized benefits. These financial instruments currently trade in opaque over-the-counter markets controlled by the largest Wall Street firms. Adding a degree of transparency to these products should not only improve financial stability, but it should also lead to lower costs, as open, transparent, and competitive markets have almost always resulted in better pricing than opaque, closed, and uncompetitive markets.

To the extent that they promote increased investor confidence and greater transparency, the changes contemplated by Dodd-Frank in this area will likely engender large positive impacts for all of us.

The positive impacts of greater consumer protection

Perhaps the most controversial changes contemplated by Dodd-Frank are those intended to protect consumers, as it has been claimed that these will lead to greatly increased compliance costs that will end up hitting small banks, small businesses, and households. It is curious that in this regard, we only hear about the regulatory burdens involved (which I would again emphasize have to date been mostly unfounded speculation and largely overstated). Lest we have forgotten, the financial crisis was driven in large part by credit losses associated with bad loans that were frequently provided to consumers with misleading or hard-to-understand terms. The losses resulting from defaults on predatory, high cost loans are exponentially higher than even the most exaggerated estimates of increased compliance costs.

By improving the disclosures that consumers receive, and limiting the ability of lenders to engage in predatory lending practices or offer high cost products, Dodd-Frank should help to prevent another subprime lending boom of the sort we just saw, and the resulting collateral damage it caused. Moreover, these changes should also help level the playing field for small banks in particular, which were forced into a race to the bottom with unscrupulous non-bank lenders during the housing bubble of the 2000s. The benefits of enhanced consumer protection must be weighed against any regulatory burdens that are considered.

Conclusion

The actual impacts of Dodd-Frank have unfortunately been minimal so far, because the implementation of Dodd-Frank has been held up by an unprecedented and successful Wall Street lobbying campaign. The impacts of Dodd-Frank, once it has been fully implemented, are likely to be significant and positive, insofar as it will reduce the likelihood of another major financial crisis, improve the transparency of our financial markets, restore the shaken confidence of investors, and empower consumers so as to avoid a reprise of the subprime lending boom, that proved so devastating.

I urge the members of this Subcommittee to make all efforts to help facilitate the full and prompt implementation of Dodd-Frank. Once Dodd-Frank is fully implemented, we will have a better idea of where and how it might be improved, to accentuate its positive impacts and pare down its regulatory burdens where appropriate. I thank you for giving me the opportunity to testify, and I look forward to your questions.

TESTIMONY OF JIM R. PURCELL,
CHAIRMAN AND C.E.O. OF
THE STATE NATIONAL BANK OF BIG SPRING

Before the U.S. House of Representatives,
Committee on Financial Services,
Subcommittee on Oversight and Investigations

"THE ADVERSE CONSEQUENCES OF THE DODD-FRANK ACT ON COMMUNITY BANK CUSTOMERS AND BORROWERS"

July 19, 2012

Chairman Neugebauer, Ranking Member Capuano, and members of the Subcommittee: My name is Jim Purcell, and I am Chairman and C.E.O. of the State National Bank of Big Spring. We operate in rural West Texas—our headquarters is in Big Spring, a town of fewer than 30,000 people, and we have offices in O'Donnell and Lamesa. And we are separated from Wall Street by more than just distance: we are a community bank, with less than $275 million in deposits.

For over a century, we have served our local communities. In fact, it's written into our charter. We exist to serve the community, and we strive to offer the full spectrum of financial services that our local community needs: savings accounts, checking accounts, loans and mortgages, wire transfers, and other services.

In terms of mortgages, we traditionally loaned money to customers to purchase rural properties. We would offer mortgages even for properties that lacked a ready resale market in the event of the borrower's default. And we would structure those loans to meet the needs of the borrowers, often by setting the monthly payment amounts to match what the borrowers would have otherwise paid in rent. Unfortunately, Dodd-Frank's regulatory uncertainty and compliance burdens forced us to stop making those loans.

Our bank—like hundreds of other federal- and state-chartered banks in Texas—did not originate toxic mortgages, we did not securitize those mortgages, and we did not engage in the sale of derivatives like credit default swaps. Nevertheless, Dodd-Frank imposes heavy burdens on our bank and on the communities that it serves.

Much of this is discussed in the complaint that the bank filed last month in federal district court in Washington, D.C.[1] In that case, we challenge the constitutionality of Dodd-Frank's Titles I and X—which created the Financial Stability Oversight Council and the Consumer Financial Protection Bureau ("CFPB"). As the complaint explains, those sections of Dodd-Frank violate the Constitution's separation of powers by creating independent agencies that are unaccountable because they are not susceptible to constitutional checks and balances.

But my purpose in testifying today is not to focus on those issues, which are already described in our complaint and will be fully examined by the Court in the upcoming litigation. I'll leave all that to the lawyers. Instead, I would like to use my limited time before this subcommittee to discuss the costs that Dodd-Frank provisions not at issue in the litigation, such as Dodd-Frank's Title XIV, impose on small, rural banks like ours, and the communities that depend on them. I appreciate the opportunity you have offered me to share our perspective on this problem.

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1 *State Nat'l Bank of Big Spring v. Geithner*, No. 1:12-cv-01032-ESH (D.D.C. filed June 21, 2012). The complaint is available online, at http://cei.org/sites/default/files/SNB%20v%20Geithner%20-%20Complaint.PDF.

Take, for example, Title XIV's treatment of "high-cost" mortgages, the subject of the CFPB's latest proposed regulations. Title XIV and the CFPB's rules impose many restrictions on the sorts of arrangements that a bank and borrower can agree upon in such a mortgage: there are limits on "balloon payments" and late fees, and requirements for mandatory loan counseling. Simply put, Dodd-Frank seeks to severely limit the availability of high-cost loans, even though high-cost loans are an appropriate and critically important service for many borrowers. Our bank's customers are the perfect example: because our borrowers often seek relatively small mortgages (that is, relative to the bank's assets) for their properties, the loan's costs and fees are spread across a smaller principal balance, and those mortgages are therefore more likely to qualify as "high-cost." By making these types of loans prohibitively difficult for banks to offer Dodd-Frank ensures that many rural borrowers are unable to get the loans that they need, loans that banks such as State National Bank of Big Spring long have offered for the good of the community.

Also, Title XIV encourages regulators to define and promote "Qualified Mortgages." Under Dodd-Frank, banks offering "Qualified Mortgages" might be saved from the prospect of certain legal liabilities, while those offering other mortgages are exposed to the full risk of subsequent legal liability throughout the life of the loan. The full definition of "Qualified Mortgage" remains to be seen; Dodd-Frank defines it in part by reference to eventual Federal Reserve regulations defining maximum debt-to-income ratios for borrowers. In any event, if the Federal Reserve defines it too narrowly, then community banks may be unable to satisfy those requirements, and instead rural borrowers will have to turn exclusively to big banks not rooted in local communities.

In fact, big banks—the very banks at the center of the problems that spurred the enactment of Dodd-Frank—are among the new law's great *beneficiaries*, precisely because they can much more easily shoulder Dodd-Frank's compliance burdens. Big banks have armies of lobbyists, lawyers, consultants, and compliance staffers, without denting the banks' profitability. Community banks, by contrast, lack those resources, and every extra dollar of compliance costs is one less dollar to spend on customer service, one more dollar of cost that ultimately must be passed through to customers.

Look no further than the rules that the CFPB proposed last week, to implement Title XIV. The proposed rules are intended to "simplify" mortgages—yet the rules are *one thousand ninety-eight pages long*.[2] Maybe a thousand pages qualify as "simplification" in Washington, or on Wall Street. But not in Big Spring or other small communities. And last week's rulemaking is just one example; the CFPB, Federal Reserve, and other agencies have promulgated many other Dodd-Frank rules, and even more rules will follow.

Finally, each time the CFPB prohibits or burdens a given financial service, its actual effect on community banks will reach far beyond that single service. Our customers want a bank that can offer them the full range of financial services that they need now or may need in the future—savings and checking accounts, of course, but also loans and other services. When the law forces community banks to reduce or eliminate any single service, customers will be all the more likely to take *all* of their business to full-service banks—that is, to big banks that can shoulder the new compliance costs.

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[2] The proposal is available on CFPB's web site, at http://files.consumerfinance.gov/f/201207_cfpb_proposed-rule_integrated-mortgage-disclosures.pdf.

Take, for example, international "remittance transfers"—that is, wire transfers—which were the subject of a recent CFPB rulemaking. It is a service we've offered in the past. For example, we wired money to Europe to a stranded foreign exchange student, or a retiree whose purse was stolen. We didn't know the exchange rate in Spain or France; we didn't know the fees being charged upon receipt. What we *did* know was that our customers needed help and we provided help.

Unfortunately, the CFPB's rules make it effectively impossible for a small, local bank to offer this service, because they require the bank to disclose information that the bank simply cannot know, such as the fees and exchange rate that international banks will charge for their participation in the transfer. Our bank decided shortly after the CFPB's final rule was published that it had to completely get out of the business of doing international remittance transfers, a service we had previously been able to provide our customers, particularly when they found themselves in some tough scrapes. Now, if someone in West Texas needs to send money to friends or family abroad, he may well take all of his banking business to Wells Fargo or Citibank—which will continue to offer international remittance transfers because their integrated international operations make it much easier comply with the new rules—instead of State National Bank of Big Spring. Even if remittances make up a relatively small part of our business, our inability to offer remittance services costs us a lot more of the customers' business.

In the end, the best way to protect consumers is not to create new federal bureaucracies that impose huge regulatory burdens on banks. The best protection for consumers is to promote a banking system rooted in the relationship between a community and the community's banks—where the bank knows its customers, and the customers know their bank. Dodd-Frank's supporters may well have believed that the new law would protect consumers, but in fact it accomplishes the opposite: by punishing community banks and promoting big banks, Dodd-Frank hurts the people that it is supposed to protect.

Mr. Chairman, thank you for the opportunity to testify before the Subcommittee.

Statement of the U.S. Chamber of Commerce

ON: Who's In Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses.

TO: U.S. House Subcommittee on Oversight and Investigations

DATE: July 19, 2012

The Chamber's mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance – is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 115 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Good Morning, Chairman Neugebauer, Ranking Member Capuano, Members of the Subcommittee, it is a pleasure to appear before you this morning. My name is Jess Sharp and I am Managing Director of the Center for Capital Markets Competitiveness at the U.S. Chamber of Commerce.

I am here today in my capacity with the Chamber; but, I am also here representing the Coalition for Derivatives End-Users, in which more than 300 end-user companies and dozens of trade associations have been active. We represent companies across the economy, both financial and non-financial, in the manufacturing, agricultural, energy, and other sectors, all united in one respect; they use derivatives to manage risk, not create it. Throughout the legislative and regulatory processes of the Dodd-Frank Act, the Coalition has advocated for strong regulation that brings transparency to the derivatives market and imposes thoughtful, new regulatory standards that enhance financial stability while avoiding needless costs on end users.

The diversity of the Coalition demonstrates the widespread use of derivatives by Main Street businesses, and helps drive home the real economic consequences of getting derivatives regulation wrong. Many U.S. companies maintain successful operations due in large part to a variety of risk management tools available through the use of derivatives. End-users currently use exchange trading, clearinghouses and over-the-counter (OTC) derivatives to help manage these risks.

For example, many auto manufacturers use derivatives to manage market risks such as foreign exchange, commodity, and interest rate risks resulting from the design, manufacture, sale and financing of vehicles. In manufacturing operations, derivatives are used to hedge currencies and commodities to lock in some near-term certainty for both revenues and costs from global vehicle production. For example, cars that are manufactured in Chicago, Illinois, are not only shipped to various states within the U.S., but are also exported to Canada, Mexico, and many other countries. Currency exposure that arises from production costs being in U.S. Dollars, and revenues in Canadian Dollars and Mexican Pesos, is hedged using foreign exchange swaps, forwards, and option contracts. OTC derivatives are also used to hedge commodities used in production such as aluminum and copper, while opting for long-term supply arrangements for some commodities that do not have a deep and liquid financial market. Many product and sourcing decisions are made years in advance of delivery.

Auto and other manufacturers also have large pension obligations to retired and deferred participants in the U.S. who depend on company pension funds for their retirement. These pension funds use derivatives to manage risk and mitigate funded status volatility that would be harmful to participants in the pension plans and to the company. For example, one of the biggest risks faced by pension funds is interest rate risk. A one percentage point drop in interest rates can cause pension liabilities to increase by billions of dollars.

For other members of the Coalition, use of derivatives is driven by the desire to reduce commercial risk associated with their business. In the case of a bottle and can manufacturer, for example, the business involves buying billions of dollars of aluminum coils per year, converting those coils into cans and selling them to large beverage and food companies. As aluminum is an actively traded commodity, they are able to use OTC swaps to exactly match the prices and timing of when they buy coils of aluminum to when they sell the completed cans. This risk management technique allows companies to prudently manage their costs and reduce volatility of price changes during the manufacturing process as well as over the life of multi-year contracts.

For commercial businesses that rely on customer financing to sell their products, derivatives also play a large role in their day-to-day operations. Companies that sell large construction or agriculture equipment, for example, provide financing for their customers on a significant percentage of sales in both good and bad economic times that may involve both fixed and variable rate financing to meet the various long and short-term financing needs of customers. These companies issue debt in the commercial paper, medium term note, and asset-backed securitization markets to fund their loan and lease portfolios. Institutional debt investors purchase the majority of the debt securities, and the demand for these securities varies as economic conditions change. Derivatives enable these companies to match the interest rate characteristics of the funding available in the capital markets with the financing needs of their customers.

Energy company members of the Coalition also rely on derivatives because of the nature of the business of energy production and transmission. For example, in the case of electricity, it must be produced and consumed simultaneously, cannot be stored, and has exposure to volatile fuel markets in coal, natural gas, and uranium. Furthermore, electricity gets delivered to thousands of points along the grid at a moment's notice. Physical energy markets are volatile and unpredictable, but hedging with derivatives allows energy companies to manage these risks and provide thousands of customers with electricity and natural gas at a low fixed price.

These are just a few examples of how thousands of U.S. companies use derivatives in their businesses to provide products at low and fixed prices to millions of customers across the country. All Americans, including businesses as well as consumers, benefit from the availability of derivatives as a way to manage commercial risk.

I'd like to take a moment to thank the Committee for its hard work in passing legislation in the House to address some of the unintended consequences of the Dodd-Frank Act and overreaching regulations put in place by regulators that threaten the ability of U.S. companies to use derivatives to manage their risk.

End-users are primarily concerned about proposed margin requirements, regulation of inter-affiliate trades, and the effectiveness of the clearing exception. In each of these three areas, we have seen strong bipartisan support for measures that would shield Main Street businesses from regulatory overreach.

H.R. 2682, which this committee approved unanimously, and the full House approved 370-24, creates a narrow, partial exemption from margin requirements for non-financial businesses that use derivatives in their commercial operations. Imposing unnecessary margin requirements on these end-users would divert working capital away from productive business use. Despite clear evidence that Congress did not intend for regulators to impose margin requirements on end-users, prudential banking regulators have proposed to do so, which would drain capital from the economy and eliminate jobs.

A survey by the Coalition found that imposing a 3% initial margin requirement on over-the-counter derivatives could cause the loss of 100,000 to 120,000 jobs and reduce capital spending by $5.1 to $6.7 billion within with the S&P 500 companies alone. The passage of H.R. 2682, in particular, helps protect Main Street from these huge cash calls that could become reality under proposed regulations.

H.R. 2779, which this committee also approved unanimously and the full House approved 357-36, prevents internal, inter-affiliate trades from being subject to regulatory burdens that were designed to be applied only to market-facing swaps and ensures that companies are not forced to abandon hedging through central risk-mitigation centers. These centers generate economic savings by allowing U.S. companies to manage commercial risk more effectively and secure better pricing for their derivatives trades—savings that companies can pass on to consumers or use to grow their business and create jobs. Without H.R. 2779, companies could be pushed towards using hedging methods that are riskier and less efficient

The overwhelmingly bi-partisan and collegial process that led to passage of H.R. 2682 and H.R. 2779 in the House demonstrates that the two bills provide noncontroversial approaches to helping grow business and improving the economy.

With regulatory compliance deadlines expected to begin in early fall for several CFTC regulations, the Coalition's concerns in these areas are more pressing than ever and have not been adequately addressed by regulation.

Ensuring that Congressional intent is followed by the CFTC and other regulators is critically important to the entire end-user community. We had hoped after passage of the Dodd-Frank Act that future legislation would not be required to address the concerns I have outlined here today. However, if legislation is not passed to clarify the statute's intent, end-users risk losing the ability to use derivatives to manage risk with the same cost-effective methods that they use today. It is important to remember that end-users rely on derivatives to reduce risk; bring certainty and stability to their businesses; and, ultimately to benefit their customers.

Thank you and I am happy to address any questions that you may have.

COLORADO PERA

Testimony of

Gregory W. Smith

Chief Operating Officer/General Counsel

Colorado Public Employees' Retirement Association

before the

United States House of Representatives

Committee on Financial Services

Subcommittee on Oversight and Investigations

July 19, 2012

Who's In Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Business

Chairman Neugebauer, Ranking Member Capuano, and Members of the Subcommittee:

Good morning. I am Greg Smith, Chief Operating Officer and General Counsel of the Colorado Public Employees' Retirement Association ("CoPERA"). I am pleased to appear before you today on behalf of CoPERA.

My testimony includes a brief overview of CoPERA and its investment approach followed by a discussion of our views on those key provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank")[1] that we believe have improved, and when fully implemented and effectively enforced, will further improve, corporate governance practices and, thereby, benefit long-term investors like COPERA and the hundreds of thousands of retirees and employees that are the beneficiaries of our fund.

CoPERA

With over $39 billion under management, CoPERA is responsible for investing and safeguarding assets used to fund retirement benefits for over 480,000 current and former employees of Colorado state government, public schools, universities and colleges, and many cities and local government districts.

Colorado PERA provides over $3.3 billion in annual benefit payments to over 95,000 beneficiaries. Ninety percent of these payments are made to beneficiaries living in Colorado. Using commonly recognized economic impact measures such as output, value-added, and labor income and employment, these payments in Colorado represent $4.31 billion in output (all goods and service transactions), $1.87 billion in value-added (State gross domestic product), $1.01 billion in labor income, and over 23,000 jobs.[2]

The annual benefit payments made by Colorado PERA to our beneficiaries represent approximately 3.3 percent of Colorado statewide payroll. In the rural counties in Colorado, this percentage is far greater. In some counties, PERA benefit payments represent over 25 percent of payroll. This infusion of income into the local economies in Colorado creates a chain of economic activities whose total impact on "main street" is greater than the initial benefit payment. This "multiplier effect" plays an important role in supporting main street businesses in Colorado.

Due to the fund's far investment horizon and heavy commitment to passive investment strategies, CoPERA is naturally a long-term, patient investor. Because CoPERA's passive strategies restrict our fund from exercising the "Wall Street walk" and fully eliminating our holdings when we are dissatisfied, corporate governance issues are of great interest to our fund and members. CoPERA believes good corporate governance

[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (July 21, 2010), http://www.gpo.gov/fdsys/pkg/PLAW-111publ203/pdf/PLAW-111publ203.pdf.
[2] Highlights of the Economic and Fiscal Impacts of Colorado PERA 1(Nov. 2011), http://www.copera.org/pdf/Impact/State%20of%20Colorado.pdf.

practices are essential to maximize and protect long-term shareowner value and interests.

CoPERA primarily participates in corporate governance decisions by voting its proxies. We firmly believe that the right to vote our shares of stock is, in itself, an asset of the fund, and therefore our responsibility as fiduciaries to manage our members' assets includes proxy voting. Accordingly we have developed and actively maintain a written proxy voting policy covering a variety of corporate governance issues. All proxy issues are reviewed by CoPERA staff on a case-by-case basis and then voted according to the policy's guidelines. CoPERA also participates in corporate governance decisions and company engagement as an active member of the Council of Institutional Investors.

With over 50 percent of our portfolio invested in domestic stocks and bonds, CoPERA is deeply committed to U.S. capital markets. As an owner of many of the Nation's public corporations, our fund is strongly aligned with corporate America—we have every interest in its long-term success and profitability. CoPERA believes that market discipline and accountability are hallmarks of a vibrant and healthy capitalist system. These values must begin in the boardroom with strong corporate governance.

Corporate Governance and the Financial Crisis

It is well established that a key cause of the global financial crisis was a failure in corporate governance.[3] As the Financial Crisis Inquiry Commission concluded:

> [D]ramatic failures of corporate governance at many . . . institutions were a key cause of this crisis.
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> . . .
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> Compensation systems—designed in an environment of cheap money, intense competition, and light regulation—too often rewarded the quick deal, the short-term gain—without proper consideration of long-term consequences. Often, those systems encouraged the big bet—where the payoff on the upside could be huge and the downside limited.[4]

CoPERA's members have paid a steep price for those failures. Not only did they suffer billions of dollars in investment losses, many lost confidence in the integrity of our markets and in the effectiveness of board oversight of corporate management.

Some corporate boards failed to include directors with the necessary blend of independence, competencies and experiences to adequately oversee risk management and corporate strategy. And, as the Financial Crisis Inquiry Commission noted, far too

[3] *See* Financial Crisis Inquiry Commission, The Financial Crisis Inquiry Report *xviii-xix* (Jan. 2011); Grant Kirkpatrick, The Corporate Governance Lessons from the Financial Crisis 2 (Feb. 2009), http://www.oecd.org/dataoecd/32/1/42229620.pdf.

[4] Financial Crisis Inquiry Commission at *xviii-xix*.

many boards structured and approved executive compensation programs that motivated excessive risk taking and yielded outsized rewards—with little to no downside risk—for short-term results.

As the costly fallout of such poor board oversight became clear investors were left with few effective tools to hold directors accountable. As the July 2009 report of the Investors Working Group explained:

> [S]hareowners currently have few ways to hold directors' feet to the fire. The primary role of shareowners is to elect and remove directors, but major roadblocks bar the way. Federal proxy rules prohibit shareowners from placing the names of their own director candidates on proxy cards. Shareowners who want to run their own candidates for board seats must mount costly full-blown election contests. Another wrinkle in the proxy voting system is that relatively few U.S. companies have adopted majority voting for directors. Most elect directors using the plurality standard, by which shareowners may vote for, but not against, a nominee. If they oppose a particular nominee, they may only withhold their votes. As a consequence, a nominee only needs one "for" vote to be elected and unseating a director is virtually impossible.[5]

The lack of meaningful, investor-driven market discipline over boards only served to encourage board mismanagement and complacency.

Dodd-Frank Corporate Governance Reforms

While Dodd-Frank did not provide investors with all of the tools that they need to improve market based oversight of corporate boards,[6] Congress did respond to the corporate governance failures identified during the financial crisis by including in Subtitles E and G of Title IX of Dodd-Frank several measures that address some of the corporate governance problems that contributed to the financial crisis. Those measures, rather than facilitating investors seeking short-term gains, are consistent with enhancing long-term shareowner value.

<u>Proxy Access</u>

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[5] Investors' Working Group, U.S. Financial Regulatory Reform: The Investors' Perspective 22 (July 2009), http://www.cii.org/UserFiles/file/resource%20center/investment%20issues/Investors'%20Working%20Group%20Report%20(July%202009).pdf.

[6] A provision that would have required "the SEC to direct the national securities exchanges and national securities associations to prohibit the listing of any security of an issuer who has on their board members that did not receive a majority vote in uncontested board elections" was unfortunately dropped from the Dodd-Frank Wall Street Reform and Consumer Protection Act during the House-Senate conference committee despite broad support for the provision from institutional investors. Comm. on Banking, Hous., & Urban Affairs, Rep. on The Restoring American Financial Stability Act 118 (Mar. 22, 2010), http://banking.senate.gov/public/_files/RAFSAPostedCommitteeReport.pdf.

Nearly 70 years have passed since the Securities and Exchange Commission ("SEC") first considered whether shareowners should be able to include director candidates on management's proxy card, commonly known as "proxy access." This reform, which has been studied and considered on and off for decades, is long overdue. Its adoption would be one of the most significant and important investor reforms by any regulatory or legislative body in decades.

CoPERA believes reasonable access to company proxy cards for long-term shareowners would address some of the various problems with director elections. We believe such access would substantially contribute to the health of the U.S. corporate governance model and U.S. corporations by making boards more responsive to shareowners, more thoughtful about whom they nominate to serve as directors and more vigilant about their oversight responsibilities.

We strongly supported Section 971 of Dodd-Frank affirming the SEC's authority to issue a mandatory proxy access rule giving long-term shareowners greater influence over the director nomination process. We agreed with the conclusion of Congress as indicated in the legislative history to this provision that "it is proper for shareholders, as the owners of the corporation, to have the right to nominate candidates for the Board using the issuer's proxy under limited circumstances."[7]

In August 2010, under the authority granted by Section 971, the SEC promulgated a comprehensive proxy access rule that would have applied to all U.S. public companies. But on October 4, 2010, the SEC delayed the implementation of the rule in response to a legal challenge from the Business Roundtable.

On July 22, 2011, the D.C. Circuit Court of Appeals agreed with the Business Roundtable's arguments and struck down the provisions of the rule that would have established a uniform proxy access rule. The SEC, however, implemented the unchallenged provisions of the rule that facilitates shareowner proposals for proxy access on a company-by-company basis. In response, over 20 proxy access shareowner proposals were submitted during the 2012 proxy season.

The most noteworthy of the proxy access proposals to-date may have been at Hewlett-Packard where the shareowner proxy access proposal was voluntarily withdrawn after the company negotiated with shareowners and agreed to put a proxy access bylaw up for a shareowner vote at its 2013 annual meeting.

Of the 9 proxy access shareowner proposals that have made it to a vote during the 2012 proxy season, the average vote in support of the proposals is 35%, and at 2 of the 9 companies the proposal has been approved:

- On June 5th, 56 percent of the shareowners at Nabors Industries voted to give shareowners—who own at least 3 percent of the company's shares for three

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[7] *Id.* at 119.

years—the right to nominate directors on the company's proxy ballot, for up to 25 percent of the board, and

- On June 8th, 60 percent of the shareowners at Chesapeake voted for proxy access on terms consistent with those at Nabors Industries.

While CoPERA supports these company-by-company developments, we and many other institutional investors continue to believe that the SEC should give priority to the reissuance of a proxy access rule that sets uniform standards and requirements for access at all public companies.[8]

Executive Compensation Reforms

As long-term investors with a significant stake in the U.S. capital markets, CoPERA has a vested interest in ensuring that U.S. companies attract, retain and motivate the highest-performing employees and executives. We are supportive of paying top executives well for superior performance.

However, the financial crisis has offered yet more examples of how investors are harmed when poorly structured executive pay packages waste shareowners' money, excessively dilute their ownership in portfolio companies and create inappropriate incentives that reward poor performance or even damage a company's long-term performance. Inappropriate pay packages may also suggest a failure in the boardroom, since it is the job of the board of directors and the compensation committee to ensure that executive compensation programs are effective, reasonable and rational with respect to critical factors such as company performance and industry considerations.

CoPERA believes executive compensation issues are best addressed by ensuring that corporate boards can be held accountable for their executive pay decisions through majority voting and access mechanisms, by giving shareowners meaningful oversight of executive pay via non-binding votes on compensation, by requiring disgorgement of ill-gotten gains pocketed by executives, by requiring independent compensation consultants, and by requiring companies to provide full, plain English disclosure of key quantitative and qualitative elements of executive pay.

CoPERA, therefore, strongly supported, and continues to support the following four Dodd-Frank provisions that provide long term investors like CoPERA with some of the tools that we need to hold directors more accountable with respect to the critical corporate governance issue of executive compensation.

1. Advisory Vote on Compensation

Section 951 of Dodd-Frank provides shareowners an advisory vote on executive compensation. The legislative history in support of this provision indicates that Congress believed that the "economic crisis revealed instances in which corporate

[8] Press Release, Council of Institutional Investors, Council Statement on Shareowner Proposals Addressing Proxy Access (Nov. 23, 2011), http://www.cii.org/UserFiles/file/11-28-11%20release%20on%20Council%20statement%20on%20access%20proposals.pdf.

executives received very high compensation despite the very poor performance of their firms."[9]

CoPERA believes that the Section 951 requirement, which first became effective for the 2011 proxy season, efficiently and effectively provides boards with useful information about whether the investors' view the company's compensation practices to be in shareowners' best interests.[10] We note that during the 2012 proxy season shareowners have rejected 55 executive compensation resolutions compared to 44 failures in 2011. While the failure rate is only about 3 percent of all say-on-pay votes, the numbers underplay the importance of this requirement.

Many experts agree that in the two years since Section 951 has been in effect, it has had a significant and positive impact on the design and magnitude of pay packages.[11] As a direct result of the requirement, compensation committees of boards are concerned about how investors will react to executive pay packages so they are actively reaching out to shareowners ahead of the vote and voluntarily reducing pay that is not tied to performance. As recently reported in Businessweek:

> Almost all of the companies that faced "no" votes last year have done away with practices that irked their investors. Hewlett-Packard (HPQ) no longer uses the formula that allowed CEO Leo Apotheker to pocket $30 million for an 11-month run during which the stock fell by almost half. Successor Meg Whitman has a salary of $1, with the bulk of her $16.5 million package tied to the company's share performance. Nabors Industries' (NBR) former chief agreed in February to waive his $100 million termination payment in the face of last year's no vote.[12]

The bottom line is that Section 951 is working as intended, inducing compensation committees to reach out to investors and engage with them in a dialogue about how executive pay programs can be better aligned with company performance and better serve the interests of long-term investors like CoPERA.

2. *Stronger Clawback Provisions*

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[9] Rep. on The Restoring American Financial Stability Act at 109.

[10] *See* Katherine Reynolds Lewis, The 5 Best and 5 Worst Regulations in Dodd-Frank, Fiscal Times 2 (July 19, 2011), http://www.thefiscaltimes.com/Articles/2011/07/19/The-5-Best-and-5-Worst-Regulations-in-Dodd-Frank.aspx#page1 (Describing "Investor protections" generally and the "provisions giv[ing] shareholders more say in matters such as executive compensation" as one of the five best regulations in Dodd-Frank.).

[11] *See* Diane Brady, Say on Pay: Boards Listen When Shareholders Speak, Businessweek, June 7, 2012, http://www.businessweek.com/articles/2012-06-07/say-on-pay-boards-listen-when-shareholders-speak.; Robin Ferracone et al., Say on Pay, Identifying Investor Concerns 21 (Sept. 2011) http://www.cii.org/UserFiles/file/resource%20center/publications/Say%20On%20Pay%20-%20Identifying%20Investor%20Concerns.pdf ("Compensation committees and boards have become much more thoughtful about their executive pay programs and pay decisions.").

[12] Diane Brady at 1.

Section 954 of Dodd-Frank imposes on executive compensation a "clawback" requirement on public companies. Under a listing standard to be mandated by SEC rule, public companies must set policies to recover incentive based compensation that was paid out based on inaccurate financial statements that do not comply with accounting standards. The legislative history in support of this provision indicates that Congress concluded that "it is unfair to shareholders for corporations to allow executives to retain compensation that they were awarded erroneously."[13]

Like many investors, CoPERA believes a tough clawback policy is an essential element of a meaningful "pay for performance" philosophy.[14] If executives are rewarded for "hitting their numbers" – and it turns out that they failed to do so – they should not profit. While Section 304 of the Sarbanes-Oxley Act of 2002 ("SOX") gave additional authority to the SEC to recoup bonuses or other incentive-based compensation in certain circumstances, CoPERA shares the view of Congress that the SOX clawback language was too narrow. Importantly, unlike the Section 304 clawback, the clawback under Section 954 is not conditioned on an adjudication of misconduct in connection with the problematic accounting that required the restatement.

While the SEC has yet to propose a rule to implement Section 954, public support for a strong clawback requirement continues to grow. That support was reflected in JPMorgan's recent decision to go beyond the clawback requirements of Section 954 and voluntarily clawback pay from senior executives linked to the nearly $6 billion dollars in trading losses incurred at its Chief Investment Office.[15] Commenting on JPMorgan's action, Kenneth Feinberg, the former Special Master for Executive Compensation for the Troubled Asset Relief Program stated:

> 'I think the fact that that JPMorgan is publicly announcing an implementation of its clawback policy is a major step in the right direction.'[16]

We agree with Mr. Feinberg and look forward to commenting on the SEC's proposed rule implementing Section 954.

3. Independent Compensation Consultants

Section 952 of Dodd-Frank mandates that members of board compensation committees and any compensation counsel or adviser be independent. It also requires the SEC to adopt rules requiring the national securities exchanges and associations to prohibit the listing of any equity security of an issuer that does not comply with Dodd-Frank's

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[13] Rep. on The Restoring American Financial Stability Act at 111.
[14] Paul Hodgson et al., Wall Street Pay, Size, Structure and Significance for Shareowners 2 (Nov. 2010), http://online.wsj.com/public/resources/documents/CIIWhitePaperWallStreetPayFINAL11302010.pdf (Paper commissioned by Council of Institutional Investors concluding that strong clawbacks are an important step to improving compensation practices.).
[15] Mary Thompson, JPMorgan Breaks New Ground on 'Clawback' Front, CNBC, July 13, 2012, http://www.cnbc.com/id/48175180/JPMorgan_Breaks_New_Ground_on_Clawback_Front.
[16] *Id.*

compensation committee independent requirements. Those rules were issued by the SEC on June 30th and are expected to be put in place by the exchanges later this year.

CoPERA believes that compensation consultants and advisors play a key role in the pay-setting process. The advice provided by these consultants may be biased as a result of conflicts of interest. Most firms that provide compensation consulting services also provide other kinds of services, such as benefits administration, human resources consulting and actuarial services. Conflicts of interest contribute to a ratcheting up effect for executive pay and thus should be minimized and disclosed.

We agree with SEC Chair Shapiro that the recently issued SEC rule in response to Section 952, if properly implemented by the exchanges and aggressively enforced, will:

> Help to enhance the board's decision-making process on executive compensation matters, particularly the selection, engagement and oversight of compensation advisers, and will provide more transparency with respect to conflicts of interest of consultants engaged by boards.[17]

4. Enhanced Disclosures

Section 953 of Dodd-Frank includes a "pay v. performance" disclosure requirement for proxy statements. Specifically, the SEC must require companies to disclose in their annual proxy statement a clear description of any compensation required to be disclosed under Regulation S-K Item 402, including information that shows the relationship between executive compensation actually paid and the company's financial performance, taking into account the change in the value of shares, dividends and distributions. The legislative history in support of this provision indicates that Congress concluded that these disclosures "will add to corporate responsibility as firms will have to more clearly disclose and explain executive pay."[18]

As U.S. Supreme Court Justice Louis Brandeis noted, "sunlight is the best disinfectant." Transparency of executive pay enables shareowners to evaluate the performance of the compensation committee and board in setting executive pay, to assess pay-for-performance links and to optimize their role of overseeing executive compensation through such means as proxy voting.

CoPERA is accordingly very supportive of the requirement of Section 953 to enhance the disclosure of executive compensation. A clearer description of the relationship between executive compensation and company performance would eliminate a major impediment to the market's and investor's ability to analyze and understand executive compensation programs and to appropriately respond.

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[17] Press Release, U.S. Securities and Exchange Commission, SEC Adopts Rule Requiring Listing Standards for Compensation Committees and Compensation Advisers 1 (June 20, 2012), http://www.sec.gov/news/press/2012/2012-115.htm.

[18] Rep. on The Restoring American Financial Stability Act at 110.

We look forward to commenting on the SEC's proposed rule to implement the requirements of Section 953.

SEC Funding

Finally, as you are aware, the SEC is responsible for implementing and enforcing many of the requirements of Dodd-Frank, including the critically important corporate governance provisions discussed in this testimony. Those responsibilities are in addition to its day-to-day responsibilities as the only federal agency responsible for protecting investors and policing the capital markets.

CoPERA agrees with the conclusion of the Investors Working Group and many others that "starving" the SEC of needed resources while at the same time increasing its responsibilities is a strategy that is unlikely to benefit investors and the capital markets, or lessen the odds of another financial crisis.[19] In that regard, we believe the SEC's FY2013 funding request appears to be quite reasonable and appropriate particularly given the scope of the SEC's core responsibilities, as well as the many new responsibilities required by Dodd-Frank.[20] We, therefore, respectfully request that the Subcommittee and its individual members consider actively supporting the SEC's funding request.

Thank you, Mr. Chairman for inviting me to participate at this hearing. I look forward to the opportunity to respond to any questions.

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[19] Investors' Working Group at 1.
[20] *See* Erick Wasson, Bill Limiting SEC Funds to Enact Dodd-Frank Headed to House Floor, Hill, June 20, 2012, http://thehill.com/blogs/on-the-money/banking-financial-institutions/233871-bill-limiting-sec-heads-to-house-floor.

NAFCU

Testimony of

Lynette Smith

President/CEO of Washington Gas Light Federal Credit Union

On behalf of

The National Association of Federal Credit Unions

"Who's in Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses"

Before the

House Financial Services Committee Subcommittee on

Oversight and Investigations

July 19, 2012

Introduction

Good morning, Chairman Neugebauer, Ranking Member Capuano, and Members of the Subcommittee. My name is Lynette Smith and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). I serve as the President and CEO of Washington Gas Light Federal Credit Union in Springfield, Virginia. Washington Gas Light FCU has more than 4,600 members with assets totaling $86.9 million.

At Washington Gas Light our mission is to "Bring our Members Financial Dreams to Light." We often times find ourselves as a lender of last resort for members with challenging credit histories. We pride ourselves in educating our members by offering a series of seminars providing financial literacy education tools that empower them to manage their personal goals from buying a home to retirement planning. We also help them take advantage of the free automated services we provide such as bill pay and home banking.

NAFCU is the only national organization exclusively representing the interests of the nation's federally chartered credit unions. Representing over 800 credit unions, NAFCU members collectively account for approximately 66 percent of the assets of all federally chartered credit unions.

On behalf of NAFCU and the entire credit union community I would like to thank you for holding this important hearing. We appreciate having the opportunity to share with the Subcommittee the impact that the *Dodd-Frank Wall Street Reform and Consumer Protection Act* [P.L. 111-203] is having, and will continue to have, on credit unions and their 94 million member-owners. As community-based financial service providers, credit unions are in the forefront serving Main Street America by helping small businesses grow as they recover from the financial crisis.

Background on Credit Unions

Historically, credit unions have served a unique function in the delivery of necessary financial services to Americans. Established by an act of Congress in 1934, the federal credit union system was created, and has been recognized, as a way to promote thrift and to make financial services available to all Americans, many of whom would otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to meet a precise public need—a niche credit unions fill today for Americans from all walks of life. Every credit union is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes." (12 § USC 1752(1)).

While over 75 years have passed since the Federal Credit Union Act (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

• credit unions remain totally committed to providing their members with efficient, low-cost, personal financial service; and,

• credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

The nation's approximately 7,000 federally insured credit unions serve a different purpose and have a fundamentally different structure than banks. Credit unions exist solely for the purpose of providing financial services to their members, while banks aim to make a profit for a limited number of shareholders. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union—"one member, one vote"—regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors— something unheard of among for-profit, stock-owned banks. Unlike their counterparts at banks and thrifts, federal credit union directors generally serve without remuneration—a fact epitomizing the true "volunteer spirit" permeating the credit union community.

As consolidation of the commercial banking sector has progressed, with the resulting depersonalization in the delivery of financial services by banks, the emphasis in consumer's minds has begun to shift not only to services provided, but also—more importantly—to quality and cost of those services. Credit unions are second-to-none in providing their members with quality personal financial services at the lowest possible cost.

The Dodd-Frank Act and Credit Unions

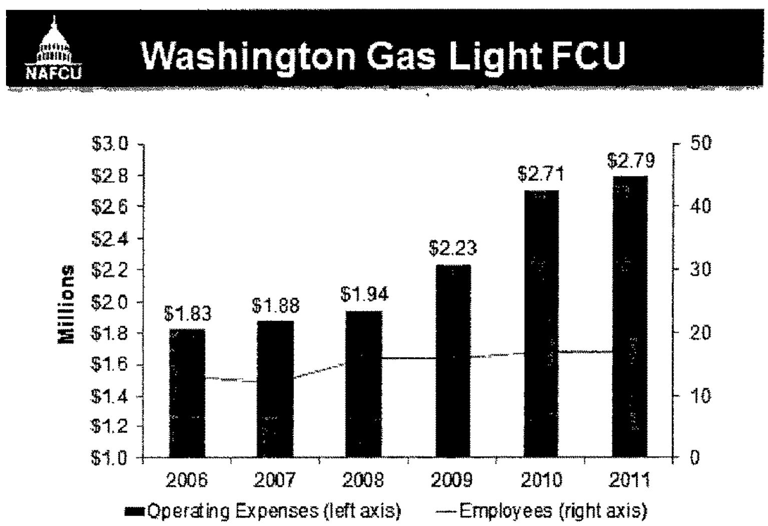
As widely recognized by members of Congress on both sides of the aisle, credit unions and other community based financial institutions were not the root cause of the housing or financial crises. Historically, credit unions have been among the most highly regulated of all financial institutions, facing restrictions on who they can serve and their ability to raise capital. Still, despite the fact that not one Congressional hearing was held on the issue of whether or not credit unions should be subject to any aspect of the new Consumer Financial Protection Bureau (CFPB)—and despite strong opposition from NAFCU—all credit unions are subject to the rule making authority of the CFPB. While there are credible arguments to be made for the existence of the CFPB, its primary focus should be on regulating the unregulated, not adding new regulatory burdens to entities that already fall under a functional regulator. In short, we are very concerned that efforts at the CFPB to rein in bad actors and greed on Wall Street will inevitably have a negative impact on community based financial institutions like credit unions, especially when it comes to regulatory and compliance burdens. Early evidence shows those concerns to be well placed. For example, credit unions will need to be in compliance with the nearly 2,000 pages of the CFPB's first two major rule proposals.

One of the biggest impacts Dodd-Frank has had on credit unions comes from the debit interchange price cap added on the Senate floor without benefit of a hearing in either the Senate or House. While this hastily crafted provision was supposed to exempt credit unions under $10 billion from its impact, market forces have already seen some credit unions begin to have higher debit card costs and declining interchange revenue. Some early evidence is starting to show that the worst concerns of credit unions may come true, and that market forces will eventually push everyone toward to the artificial capped rate.

Furthermore, with no end in sight, the steady stream of regulations pouring out of Dodd-Frank only adds to the existing compliance burden our nation's credit unions already face. While many of them are well-intentioned to correct the abuses of others, for credit unions they are often a solution in search of a problem. I cannot overemphasize how burdensome and expensive unnecessary Dodd-Frank Act related compliance costs will be for credit unions. We can only hope Congress will urge regulators to do more robust cost-benefit analysis of potential regulations and follow-up once the regulations are in place and make changes if the costs are too high.

Washington Gas Light has a staff of just 17. My employees and I already spend countless hours updating disclosure booklets and web sites while constantly reviewing documents to comply with the never ending changes to laws and regulations. Just in the last few years there have been extensive changes made from new credit card legislation to new disclosure requirements. Layered on top of this will be a number of rules from the CFPB that will directly impact credit unions. This will compound existing challenges and uncertainty.

Every dollar we spend at my credit union to keep up with various regulations and reporting requirements is one less dollar we can use towards credit availability for our members. My credit union is healthy, growing and has good loan demand. Still, rather than looking to hire a new loan officer, the growing compliance burden means I must look to hire a compliance officer. While we still try to make the loans our member's need, the staff time dedicated to compliance means that many often have to wait longer to get their loan. As depicted in the chart below, operating expenses at my credit union have steadily risen in large part due to increased compliance burden, while the number of employees at Washington Gas Light has remained nearly constant in that same timeframe.



Financial Stability Oversight Council Positioned to Facilitate Robust Regulatory Coordination

With households still recovering from the greatest financial crisis since the Great Depression, it has never been more important for regulators to institute commonsense regulations that strike a balance between protecting consumers and giving credit unions the flexibility they need to best serve their members.

Under the Dodd-Frank Act, the Financial Stability Oversight Council [FSOC] has a duty to facilitate regulatory coordination. We hope that they take this duty seriously. This duty includes facilitating information sharing and coordination among the member agencies of domestic financial services policy development, rulemaking, examinations, reporting requirements and enforcement actions. Essentially, the FSOC is charged with identifying weakness within the regulatory structure and promoting a safer, more stable system.

With respect to this goal, NAFCU would like to emphasize how important it is to credit unions for our industry's copious regulators to coordinate with each other to help mitigate regulatory burden. As NAFCU member credit unions have testified on numerous occasions, it is not any single regulation, but an accumulation of regulations from numerous regulators operating independently of each other with little to no coordination that magnifies the undue regulatory burden credit unions face today.

Included at the end of my written statement is a letter from NAFCU to Treasury Secretary Geithner in his capacity as Chairman of the FSOC expanding on the importance of increased regulatory coordination and how this can help keep credit union's focused on serving their members. NAFCU urges the Subcommittee to use its oversight authorities with the FSOC and to keep the FSOC's role in mind moving forward as the full impact of Dodd-Frank unfolds at our nation's credit unions.

Dodd-Frank Rule Making Underway

As widely publicized, the CFPB estimated that its first rule on international remittance transfers would require 7.7 million total employee hours of work for the industry to implement and comply with. This mindboggling headline strikes at the very core of what credit unions fear most – Dodd-Frank mandated regulation will be finalized so quickly, and so often, that community-based financial institutions simply won't be able to keep up.

It is worth noting that revisions that led to the CFPB's final rule on international remittance transfers were originally proposed by the Federal Reserve, but as mandated in Dodd-Frank, finalized by the CFPB. On the same day the rule was finalized, the CFPB simultaneously issued a proposed rule and request for comment that sought feedback on the disclosure process for recurring remittance transfers. The proposed rule also sought comment on whether it should allow an exception for institutions that infrequently provide such services. NAFCU appreciates the Bureau's decision to seek more input regarding the unique problems that arise with preauthorized or reoccurring electronic fund transfers. We hope that this is an openness that will continue in both word and deed.

Under the proposed rule, an exception for remittance transfer providers, presumably made to accommodate small financial institutions, falls far short of offering any tangible relief to credit unions who operate in this space. Those providers making less than 25 international remittance transfers a year would be exempt and therefore free of the extensive disclosure requirements that are mandated for those providers above that threshold. This arbitrary and exceptionally low number will not provide relief for credit unions. A NAFCU survey of our member credit unions found that nearly 84% of those credit unions that provide remittance services, make more than 25 a year. The same survey found that nearly 58% of those that had a remittance program make less than $1,000 per year on the program or operate it at a loss. The new compliance costs of this rule may force many of those to make changes to their programs or eliminate those services outright.

Furthermore, a vast majority of credit unions who provide remittance transfer services rely on open network systems. By the CFPB's own admission, under the rule already finalized, it will be exceedingly difficult for open network systems, as currently configured, to comply. This leaves credit unions with two plausible choices – stop doing international remittance transfers, a service that many members utilize and value, or pay for a massive reconfiguration of the payment networks needed to comply. It should be noted that Congress only recently gave credit unions the ability to do remittances for all consumers in their field of membership, in an effort to reach the under-or un-banked. Without changes, the new rule from the CFPB will likely lead some credit unions to stop remittance services and undo the intent of Congress by discouraging under- and un-banker populations from using credit unions for these services. This is the first of what has the potential to be many financial products credit unions will no longer be able to offer their members as a result of the undue regulatory burden being thrust upon them.

While the international remittance transfer rule was the first and only rule related to Dodd-Frank to be finalized by the CFPB thus far, there are an overwhelming number of upcoming Dodd-Frank mandates that will directly impact credit unions. The CFPB's mandates are particularly daunting as related to Regulation Z, the implementing regulations for the Truth in Lending Act (TILA). Nearly every aspect of current compliance requirements with respect to operating a mortgage portfolio has the potential to change.

By January 2013, the CFPB is expected to expand the scope of coverage under the Home Ownership and Equity Protection Act, address mortgage origination and mortgage servicing standards, amend rules associated with the Truth in Lending Act and Financial Institutions Reform, Recovery, and Enforcement Act, change requirements for escrow accounts and issue rules under Dodd-Frank relative to what constitutes a qualified mortgage (QM).

As subcommittee members are aware, the CFPB request for comment on QMs just closed on July 9, 2012. The request for comment was a follow-up on the Federal Reserve Board's proposed rule regarding a consumer's ability to repay mortgage loans. While NAFCU supports efforts to ensure that consumers cannot enter into mortgages they cannot afford, we are very concerned that the proposal will create more regulatory burden on credit unions. We believe: (1)

credit unions that make qualified mortgages should have a clear safe harbor; (2) disclosure of compensation arrangements are counterproductive to providing consumers with meaningful information; and (3) the 2011 proposal is overly complex. The proposal would require some credit unions, with narrowly tailored programs that require limited verification of income, to significantly overhaul these programs, thus incurring significant cost, even though there will be little benefit to their members. Additionally, many credit union members, including those in the immigrant community and those which operate cash based businesses, may no longer be able to obtain credit due to the inflexible income verification requirements, such as not counting spousal income.

NAFCU appreciates the focus that the House Financial Services Committee has placed on reviewing the QM request for comment from the CFPB. NAFCU strongly supports a clear safe harbor for lenders who have met qualified mortgage requirements.

Additionally on July 9, the CFPB released a much anticipated proposal combining and streamlining the Truth in Lending Act (TILA) and Real Estate Settlement Procedures Act (RESPA) mortgage loan forms. NAFCU has been actively participating in the processes the CFPB has used to gather information leading up to the proposal of this rule, including partaking in the recent Small Business Regulatory Enforcement Fairness Act review panel on this topic. NAFCU is hopeful that these panels will be held in the future, and input given will translate into commonsense rulemaking that doesn't create additional and unnecessary compliance burdens for credit unions. Still, NAFCU needs these efforts to have real impact on the rulemaking. In the proposed rule, the CFPB details discussion and gives a thorough cost benefit discussion of the rule for small entities, highlights the massive impact of the proposed rule, but makes no changes in the proposal for small entities.

As noted early, this proposal is just shy of 1100 pages. The proposal changes two separate regulations, changes dozens of substantive processes for financial institutions, including the way the annual percentage rate is calculated, changes what disclosures go on loan estimate and loan closing forms, will require hundreds of hours of staff training, and will require the reconfiguring systems and how loans get delivered. That does not even take into account changes that will need to be made with relationships with settlement agents and the like. And this is just one rule. It is not in any way an exaggeration to say that this will have a big impact on our ability to deliver credit.

In addition, while many of the details are yet to emerge about the various mortgage proposals, the sheer pace at which these new rules are scheduled to be implemented should cause serious pause. Even if they are well-intentioned and ultimately bring about positive changes, there is a significant burden on small institutions in just keeping up.

The CFPB recently released its 2012 Semi-Annual Regulatory Agenda which outlines 27 different areas where potential rulemaking may occur in the near future. As the CFPB's final rule on remittances and their mortgage-related proposed rules demonstrate, it will be very challenging for my limited staff of only 17, I am not sure how I can keep up and continue to serve our members' needs.

Review of Existing Regulations

In January of last year, President Obama announced a government review of existing regulations. We hope that this ongoing review by the Administration and the efforts by Congress can recognize what credit unions like mine know all too well – the problem is not necessarily one single bill or regulation, but the cumulative effect of new regulations piled on top of each other, without studying these effects on small financial institutions that don't have an army of lawyers with which to comply. These burdens do not just come from one or two regulators, but from a host of federal agencies and laws that can impact our business. The Dodd-Frank Act just made this worse. For small financial institutions, this is almost a death by a thousand cuts.

As part of this review, National Credit Union Administration (NCUA) Chairman Debbie Matz informed the Obama Administration that, since NCUA began to review their regulations every three years, they have been successful in reducing regulatory burdens. However, I can say from a credit union perspective that burdens on credit unions remain. It is unclear to credit unions whether there is a true process for NCUA to eliminate regulations, or if they have set or met any particular benchmarks in reducing compliance burdens.

In the past two years, NCUA has made changes to its Regulatory Flexibility (RegFlex) program. Under the RegFlex regime certain well-run credit unions were exempt from a number of regulatory requirements. Recently, NCUA expanded the RegFlex program to include all credit unions, but it also eliminated two very beneficial RegFlex provisions relative to fixed assets and personal guarantees. NAFCU feels that NCUA can and should do much more to eliminate outdated regulation. Even small tweaks to NCUA's rules can have a major impact on operations.

Furthermore, NCUA should actively embrace and take into consideration technology advancements when promulgating regulations – that would be one way to ease some burden.

As the CFPB ramps up, NAFCU has actively participated in the Bureau's request for comment on an array of issues including regulatory streamlining. To truly understand how the onslaught of regulation scheduled to be finalized through Dodd-Frank will impact credit unions, one must look at the regulatory environment that already exists. NAFCU is hopeful that the CFPB will ultimately use its authority not only to identify, but also to streamline and simplify regulation where possible. If the CFPB and other regulators will not do this in a timely and effective manner, Congress must step in and do so. As discussed earlier in my testimony, the members of the Financial Stability Oversight Council also have a unique role and distinct responsibility in terms of surveying the current regulatory environment, information sharing, and coordinating with respect to regulation.

Amending or eliminating outdated regulation must be a priority as unnecessary day-to-day compliance costs at credit unions represent resources that could otherwise be used to help members purchase a new car or start a new small business. A prime example of an outdated compliance burden is the redundant and unnecessary requirement in the Electronic Funds Transfer Act and its implementing rule (Regulation E – 12 CFR 1005.16) requiring automated teller machine (ATM) operators to provide two separate notices to consumers regarding the imposition of a fee for use of the ATM. NAFCU appreciates swift action in the Financial Services Committee and on the House floor in passing H.R. 4367. This bipartisan legislation introduced by Representatives Luetkemeyer (R-MO) and Scott (D-GA) will eliminate the physical placard disclosure requirement while retaining the on-screen notice with option for the consumer to decline the transaction. I look forward to Senate passage of this important bill as many credit unions are forced to constantly police ATM machines in an effort to fend-off the threat of frivolous lawsuits, spending time and resources that could be better used to help their members.

Another increased burden for credit unions comes from recent changes in the exam process. Part of the response to the economic crisis was to create new layers of regulation and institute more aggressive enforcement of existing law. Three credit unions, despite no contributions to the crisis, are already subject to new examinations of the CFPB. Many more will ultimately fall into the grasp of CFPB examinations as Congress did nothing to index the thresholds of the Dodd-Frank Act, including the CFPB examination threshold of $10 billion. This means the "supposed" $10 billion exemption is really a disintegrating one that will allow the CFPB to capture more and more institutions under its full power over time. One way for Congress to rectify this would be to pass legislation indexing all thresholds in the Dodd-Frank Act.

Regulators have increasingly tightened examination standards in order to aggressively enforce new and old regulations and to avoid a repeat of the crisis. Exam cycles are shorter, adding an element of burden to credit unions as staff time and resources are dedicated to prepare and respond to the exam. It is with this in mind that we also urge the committee to move forward and vote on the Financial Institutions Examination Fairness and Reform Act (H.R. 3461) introduced by Representatives Capito and Maloney.

I cannot overstate how critical it is for the CFPB to review and simplify the complex regulatory framework credit unions already face. Such an effort could help mitigate layering regulation upon regulation to the detriment of credit unions and their member-owners.

Attached for the Subcommittee's review, please find NAFCU's detailed response to the CFPB's request for comment on regulatory streamlining (Docket No. CFPB-2011-0039). Again, NAFCU and its member credit unions remain hopeful that steps are taken to update and streamline existing regulation before new regulation is simply pushed through and layered on top of it.

Cost-Benefit Analysis

One thing that is unfortunately missing from far too many regulations and laws is a robust cost-benefit analysis for the changes that are sought. This is particularly important for not-for-profit credit unions. Simply put: Are the benefits to the consumer greater than the cost of compliance?

Federal agencies are required to conduct cost-benefit analysis before they issue certain proposed or final rules. These requirements have been added incrementally by various statutes and executive orders over the past 50 years. The elements of analysis usually include some or a combination of the following: quantitative and qualitative estimates of costs and benefits, effects on the national economy, consideration of a range of alternatives, selection of the alternative that is least costly, most cost-effective, or least burdensome, or an explanation of why that alternative was not selected.

Many of the current requirements have substantial exclusions and exceptions, giving federal agencies considerable discretion to decide whether an analysis is required. For example, some requirements do not apply to rules that are issued without a prior notice of a proposed rulemaking, and agencies can avoid regulatory flexibility analyses if they certify that their rules do not have a significant economic impact on a substantial number of small entities. At NCUA, only credit unions under $10 million in assets are currently considered small entities. NCUA should consider raising the small entities benchmark. For example, the CFPB uses $175 million for the Small Business Regulatory Enforcement Fairness Act review panels.

The number of economically significant regulations, those costing the regulated community more than $100 million or having a significant adverse impact on competition, employment or productivity has increased substantially.

Conclusion

While credit unions were not the problem, the Dodd-Frank Act impacts credit unions in many ways. While the interchange provision has some of the biggest impact, the greatest impact will likely come from the ever increasing burden of new regulations emerging as a result of the Dodd-Frank Act, whether from the CFPB or functional regulators. Congress must continue vigorous oversight and look for ways to act on regulatory relief.

Regulators must also accept responsibility in this regard, and the newly created FSOC should make regulatory coordination part of its focus.

This is critical because every dollar spent on compliance, whether stemming from a new law or outdated regulation, is a dollar that could have been used to reduce cost or provide additional services or loans to members. This has a real impact on the small businesses in our local communities we are counting on to create jobs and economic growth. NAFCU continues to urge

Congress to move forward with legislation that will provide regulatory relief from outdated laws and regulations for credit unions.

We thank you for your time and the opportunity to testify before you here today on these important issues to credit unions and ultimately our nation's economy. I welcome any questions you may have.

Attached:

6.27.2012 letter from NAFCU President and CEO Fred Becker to Treasury Secretary Geithner re: FSOC's Role to Reduce Regulatory Compliance Buren at Credit Unions

3.2.2012 letter from NAFCU President and CEO Fred Becker to Monica Jackson/ CFPB re: Docket No. CFPB – 2011-0039/ Streamlining Regulations

NAFCU

National Association of Federal Credit Unions
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Fred R. Becker, Jr.
President and CEO

June 27, 2012

The Honorable Timothy F. Geithner
Secretary of the Treasury
United States Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: FSOC's Role to Reduce Regulatory Compliance Burden on Credit Unions

Dear Secretary ~~Geithner:~~ Secretary Geithner

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents the interests of our nation's Federal credit unions (FCUs), I am writing to you in your capacity as Chairman of the Financial Stability Oversight Council (FSOC).

As you know, under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Act), the FSOC has a duty to facilitate regulatory coordination. This duty includes facilitating information sharing and coordination among the member agencies of domestic financial services policy development, rulemaking, examinations, reporting requirements and enforcement actions. Through this role, the FSOC is effectively charged with ameliorating weaknesses within the regulatory structure, promoting a safer and a more stable system.

In regards to this goal, NAFCU would like to emphasize how important it is to credit unions for our industry's copious regulators to coordinate with each other to help mitigate regulatory burden. As highlighted in the testimony of NAFCU Board Member Ed Templeton before the House Financial Services Committee on May 9, 2012, it is not any single regulation, but the panoply of the regulatory regime of numerous regulators, each operating "within their own lanes" and with minimal, if any, interagency coordination, that not only helps create, but significantly magnifies, today's undue regulatory burden on credit unions and other small financial institutions.

In his testimony, Mr. Templeton, CEO of a small credit union that serves a large number of underserved Americans, emphasized the difficulties facing credit unions to

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plan ahead and keep pace with the rapid rate of regulatory changes under the Act. As Mr. Templeton testified, 96.4% of credit unions in a NAFCU survey last spring reported that they were devoting more staff time to regulatory compliance than they did in 2008. Consequently, credit unions have not been able to use their resources efficiently as they are devoting far too much time and money on regulatory compliance and related functions; they should be empowered, instead, to expend such time and resources to serving their members.

The array of regulations that are making operating a credit union more and more difficult are being fired simultaneously from multiple directions and by a host of agencies. For example, the Consumer Financial Protection Bureau (CFPB) has issued several rules and is soon expected to propose numerous major rules that would greatly impact credit unions' products and services, including savings, mortgage lending, and credit and debit card services. Concomitantly, the credit union's principle regulator, the National Credit Union Administration (NCUA), is issuing regulations on issues such as concentration and interest rate risk, loan participations, credit union service organizations and appraisal management. At the same time, the Department of Justice is issuing regulations on physical assess to ATMs, while the Department of Labor is issuing regulations on employee rights and the Financial Crimes Enforcement Network (FinCEN) is issuing regulations on currency transaction reports and suspicious activity reports.

As we have approached each agency regarding the ever-increasing regulatory burden, they quickly respond that the rules being issued by other agencies are outside of their purview. NAFCU believes the FSOC is well-positioned to rectify this lack of coordination. In that regard, we ask that you establish within the FSOC robust inter-agency coordination on the issuance of rules impacting financial institutions.

NAFCU also urges the FSOC to establish policy requiring member agencies to conduct and publish a thorough cost-benefit analysis prior to issuing regulations as well as a separate cost-benefit analysis a year after each regulation the agency prescribes and every other year thereafter. Also, a cost-benefit analysis should be conducted every two years on each regulation that an agency has on its books, with the agency required to justify the regulations' continued existence. These cost analyses should be reviewed by the FSOC to assess the total impact on the financial services industry. We strongly believe that conducting such exercises would better instruct regulators of the high cost of compliance, and equip them with the information necessary to assess whether a particular regulation is effective and justifiable.

America's credit unions have long been reliable sources of financial advancement for millions of people. We believe that the FSOC, with your leadership, is in a position to help credit unions and other small financial institutions continue to achieve their mission of serving their members.

Secretary Geithner
U.S. Department of the Treasury
June 27, 2012
Page 3 of 3

NAFCU appreciates your attention to our concerns. Should you have any questions or concerns, please feel free to contact me or Carrie Hunt, NAFCU's General Counsel and Vice President of Regulatory Affairs, at 703-842-2234.

Sincerely,

Fred R. Becker, Jr.
President/CEO

cc: Members of the Senate Banking Committee
Members of the House Financial Services Committee
The Honorable Ben Bernanke, chairman of the Federal Reserve Board
Martin J. Gruenberg, acting chairman of the Federal Deposit Insurance Corporation
The Honorable Richard Cordray, director of the Consumer Financial Protection Bureau
Edward DeMarco, acting director of the Federal Housing Finance Agency
The Honorable Debbie Matz, chairman of the National Credit Union Administration
The Honorable Karen Mills, administrator of the Small Business Administration
The Honorable Hilda Solis, secretary of the Department of Labor
The Honorable Shaun Donovan, secretary the Department of Housing and Urban Development
James H. Freis, Jr., director, Financial Crimes Enforcement Network
The Honorable Julius Genachowski, chairman of the Federal Communications Commission
The Honorable Jon Leibowitz, chairman of the Federal Trade Commission

NAFCU

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NAFCU | Your Direct Connection to Education, Advocacy & Advancement

March 2, 2012

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1801 L Street, NW
Washington, D.C. 20036

RE: Docket No. CFPB–2011–0039

Dear Ms. Jackson:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents federal credit unions, I am writing to you regarding the Consumer Financial Protection Bureau's (CFPB) request for comment on regulatory streamlining. NAFCU very much appreciates the CFPB's early identification of the critical importance of streamlining regulations.

Over the last several years, there has been an ever-increasing regulatory burden for credit unions, particularly in the area of lending. In general, credit unions are smaller institutions, with lesser economies of scale; consequently, these constant changes have a more significant impact on their ability to serve their member-owners. Further, given that every dollar a credit union must pay starts with a member at a teller window, the changes have a very direct impact on credit union member-owners. There are a number of steps the CFPB can take to streamline and simplify the complex regulatory framework for credit unions. Following is a detailed explanation of several regulatory issues that NAFCU urges the CFPB to simplify.

<u>Regulation Z</u>

There are several small issues with Regulation Z, primarily relating to mortgages and credit cards, which could be improved with relatively modest changes.

<u>Mortgages</u>

<u>Lender Cost of Funds</u>

The CFPB should use its authority to eliminate the "lender cost of funds" disclosure that the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the Dodd-Frank Act) requires on mortgage disclosures. This is one of NAFCU's top priorities for the streamlining process as the disclosure does not provide any useful information and, in some cases, may be misleading. The implication of the disclosure is that the lender is making a profit spread between the cost of funds and the rate the borrower is paying. Important components that make up the ultimate price, such as interest rate risk and credit risk are ignored by the disclosures and consequently will be ignored by borrowers. The purpose of the Know Before You Owe project is to simplify and clarify disclosures for consumers. Instead, this disclosure provides consumers additional information that they likely will not understand and that has only a tangential bearing on the cost of the mortgage.

Further, in the context of mortgage loans sold into the secondary market, the disclosure is also potentially misleading. The mortgage lender likely does not know the cost of funds for the investor at the time these disclosures are made. Consequently, the best that could be accomplished in this context is for the Bureau or some other entity to publish an average rate on a daily, weekly or monthly basis that could be used to make the disclosure. Providing borrowers an average rate that may be days or weeks old, we believe, detracts from the purpose of the disclosures.

NAFCU recommends the CFPB consider using its authority under section 104 of the Truth In Lending Act (TILA), which enables the Board to exempt disclosures that "are not necessary to carry out the purposes" of the Act. Alternatively, the Bureau could use its exemption under section 105, which permits the Board to exempt statutorily required disclosures based on a five factor balancing test. Either exemption would apply to this proposed disclosure, which provides little if any value and only confuses a process which the agency's Know Before You Owe project is designed to clarify.

Waiting Period after Re-disclosure

The agency should also make changes to the rules implementing the Mortgage Disclosure Improvement Act (MDIA). Lenders are currently required to provide early disclosures three days after a mortgage application is received. Lenders must also provide updated or final disclosures at settlement. If the annual percentage rate (APR) changes beyond a certain threshold or if certain fees exceed a threshold, new disclosures must be provided. Further, section 1026.19(1)(2)(ii) requires that at least three days pass between re-disclosure and closing. Truth in Lending (Regulation Z), 76 Fed. Reg. 79,801 (proposed Dec. 22, 2011) (to be codified at 12 C.F.R. pt. 1026). NAFCU recommends the CFPB modify the three day waiting period. While well intentioned, the three day minimum is potentially harmful and, at the very least, bothersome to borrowers who understand the changes and want to move forward with closing the loan. The regulation only allows for a waiver of the waiting period if waiting will create a bona fide personal financial emergency for the borrower; however, the only example the regulation provides that would qualify is if the borrower will lose his home to foreclosure if funds are not released. Id. at 79,986. There are a number of other potential scenarios that may create such a hardship but lenders are wary of moving forward without more guidance. Further, there are dozens of other legitimate reasons for a borrower to wish to move forward with the loan that certainly fall short of a "bona fide personal financial emergency."

NAFCU recommends the agency consider three different options. First, if the agency insists on keeping a non-negotiable, minimum wait time, it should allow borrowers to move forward after one business day. One business day would still provide borrowers sufficient time to examine the changes. Further, the rule could still allow borrowers to have up to three business days after re-disclosure to examine the documents if they so choose. Permitting a minimum one day wait would minimize the hardships for people who have compelling reasons to move forward but who fail to qualify for the bona fide personal hardship exception. Additionally, a one day minimum period would still ensure that borrowers would have time to consider the changes on their own and would protect against borrowers being pressured into the change at closing. Second, the CFPB should consider relaxing the waiver requirement and allowing borrowers to waive the three day period at their discretion. Third, the agency should, at the least, provide more guidance as to what constitutes a bona fide personal financial emergency.

Credit Cards

Ability to Repay and Non-working Spouses

The CFPB should modify one aspect of the existing rule regarding the ability to repay a credit card account. Currently Regulation Z does not permit a credit card issuer to consider household income when determining whether a consumer has the ability to repay a credit card account. 12 C.F.R. § 1016.51. Requiring that issuers determine the ability to repay based solely on personal income, even in cases where there is sufficient household income to make payments is shortsighted and disproportionately impacts now-working spouses. This rule serves little practical purpose in terms of ensuring the debt will be repaid. In cases where there is a steady household income, creditors should be permitted to consider that income, rather than only the applicant's personal income. The applicant presumably has access to the household income to pay the credit card bill and the inquiry should end there. The rule forces non-working applicants to seek the spouse's approval for any extension of credit.

The rule is also incongruent. The rule only permit lenders to consider personal income, while at the same time requiring consideration of all household liabilities when making the determination of whether the debt is likely to be repaid. In addition to this aspect of the proposal being inconsistent, it, again, will only exacerbate the negative impact on non-working spouses. Issuers should be permitted to take into consideration household income on which the applicant states he or she can rely. The current rule negatively impacts all non-working spouses and greatly reduces the availability of credit for all non-working spouses.

Reevaluation of Rate Increases

The CFPB should consider modifying 12 C.F.R. § 1026.59, which requires credit card issuers to reevaluate rate increases. If a card issuer increases the APR on the account for virtually any reason, it is then required to reevaluate the APR at least every six months for an indefinite period of time. NAFCU understands the purpose behind the requirement, however, to require reevaluations every six months indefinitely for *all* APR increases is unduly burdensome. Under the current rule, a cardholder's credit score could drop by 50 percent (or more) and the credit card issuer would still be required to reevaluate the APR every six months as long as the account is active. This requirement is problematic for two reasons. First, it is a waste of resources as the issuer is required to reevaluate an account every six months when there is very little possibility that the APR will be reduced in the near future. Second, the requirement creates a perverse incentive as it drives up the cost on already risky accounts, which encourages lenders to close the account rather than work with the borrower. Accordingly, the CFPB should terminate the obligation in instances where the cardholder's credit score has dropped dramatically. This change is all the more reasonable given that most issuers will review a consumer's account upon request.

If a cardholder suffers a decrease in credit score of 5 percent, for example, it will take him a considerable amount of time to repair his credit to the point that he is eligible for the initial APR he received prior to his score decreasing. There is no benefit to consumers in requiring card issuers to reevaluate accounts every six months given the length of time it will likely require to repair the credit score. There are, however, considerable costs involved for the institution in reevaluating each account every six months. Terminating the obligation in instances where the cardholder's credit score has dropped dramatically is a reasonable way in which to balance the institution's costs against the consumer protection concerns advanced in the *Credit Card Accountability, Responsibility and Disclosure Act* (CARD Act). Further, the credit card market is highly competitive and it will likely ensure that consumers who are able to quickly repair their credit will be able to take advantage of better rates. Consumers who suffered a credit problem and have since repaired that problem will undoubtedly receive solicitations at a better rate if their current card issuer refuses to lower the APR. Indeed the credit card market is one area in which there are virtually no barriers to a consumer moving from one company to another if a better price is offered. NAFCU understands the need for consumer protection and government oversight. However, the CFPB should set some limits on the reevaluation requirement in cases where a borrower has suffered a serious decline in creditworthiness.

NAFCU urges the CFPB to alter the rules regarding household income and to simplify the reevaluation requirement in cases where a cardholder's credit score has dropped significantly.

Annual Statement of Billing Rights

The CFPB should eliminate the requirement that lenders provide borrowers an annual statement regarding their billing rights, as required by 12 C.F.R. § 1026.9. Institutions are already required to disclose all relevant information regarding the consumer's billing rights during the application and account opening process. Institutions should only be required to send an updated statement if the policy has changed. Further, these statements can be made available online and in branches and would eliminate this costly and generally useless burden.

The Annual statement of billing rights is one of three annual disclosures (privacy policies and error resolution policies are discussed below) that institutions must regularly provide. Eliminating all three of these annual disclosures is a top priority for NAFCU. The CFPB indicted it will look at five primary factors in determining whether to adopt a proposed change. Those factors are:

- The potential benefits and costs of the proposed change for consumers and regulated entities;
- The likelihood that the Bureau would be able to achieve benefits consistent with the underlying statute;
- The speed with which the public would realize the benefits;
- The governmental and private resources it would take to realize the benefits; and
- The state of the evidence with which to judge the previous four factors.

In the case of all of the annual disclosures, the benefit to regulated entities is significant as they would save considerable amounts of time and money printing and sending the annual disclosures. The change could be made consistent with the underlying statute. Further, the CFPB has considerable authority to implement TILA as it sees fit, if certain disclosures or requirements are redundant or unnecessary. The benefits would be realized immediately for financial institutions and would not require any governmental resources beyond changing the regulation. While the change may seem modest, it would save institutions a significant amount of money printing and sending the disclosures. Additionally, the change would free up valuable time for employees who would otherwise need to carry out the process. On balance, the factors heavily weigh in favor of eliminating the requirement.

General Concerns with Regulation Z

The CFPB specifically asked if the transaction threshold for coverage under Regulation Z should be increased. Currently, lenders that make twenty-five or fewer non-home secured loans a year are not covered by Regulation Z. Similarly, lenders that make five or fewer home secured mortgages per year are not covered by the rule. NAFCU recommends increasing the threshold exemption to 50 loans per year for all loan types.

Additionally, for the special rules for private student loans, NAFCU recommends a similar exemption. Specifically, a lender should not be required to comply with the existing rules for private education loans included in 12 C.F.R. §§ 1026.46-50 unless it makes at least fifty private student loans per year. The disclosures required for private student loans are lengthy and complicated. Further, the rule is so broad that virtually any loan that a borrower intends to use for education purposes is subject to the rule. Consequently, some lenders have chosen not to extend credit if the loan might be construed as a private education loan as the costs of compliance outweigh the income that can be derived from extending a small number of covered loans. Accordingly, NAFCU recommends an exemption from the requirements if a lender makes fewer than fifty private student loans per year.

Regulation E

ATM Fee Disclosure

NAFCU's top priority is eliminating the redundant and unnecessary requirement that automated teller machine (ATM) operators place a fee disclosure notice *on* the ATM, as required by 12 C.F.R. § 1025.16(c)(1). The requirement is outdated, unnecessary and has spawned a number of frivolous lawsuits. Plaintiffs have filed suit claiming the disclosures are not large enough, despite the fact that the statute and regulation do not contain size requirements and only state that the disclosure must be conspicuous. Further, it is impossible for ATM operators to ensure compliance as the sign on the ATM can simply be removed or obscured.

All ATMs include a fee disclosure on the screen during the transaction and provide consumers an opportunity to terminate the transaction without paying any fee. The on-screen disclosure should be sufficient to notify consumers. The utility of the physical sign disclosure is all the more questionable since that disclosure must only state that there may be a fee, but not the actual amount of the fee.

Accordingly, NAFCU has two recommendations. First, NAFCU encourages the CFPB to eliminate the disclosure requirement included in 12 C.F.R. 1025.16(c)(1). While this disclosure is required by statute under 15 U.S.C. § 1693b(d)(3)(A)(i), the statute also provides the CFPB authority to prescribe regulations that "contain such classifications, differentiations, or other provisions" that "provide for such adjustments and exceptions for any class of electronic fund transfers...as in the judgment of the [agency] are necessary or proper to effectuate the purposes of this subchapter, to prevent circumvention or evasion thereof, or to facilitate compliance therewith." Id. at § 1693b(c). The broad authority accorded the CFPB is sufficient to allow an exception for signs located on ATMs. The requirement is duplicative at best as more detailed on-screen disclosures are provided on every ATM. Consequently, an exception would not undercut the consumer protections provided by the statute. Alternatively, if the CFPB refuses to eliminate the requirement, it should consider adding an additional provision to the regulation that holds harmless an ATM operator that can show it did affix a sign to an

ATM. While this option is not as helpful, it would be useful in cases where a vandal or prospective litigant removes the disclosure from an otherwise compliant ATM.

The factors the CFPB will use in determining what proposal to adopt all weigh in favor of eliminating this requirement. The potential costs and benefits for consumers and regulated entities weigh heavily in favor of eliminating the provision. Not only does the disclosure provide little, if any, benefit, it has grown increasingly costly for ATM operators as a result of litigation. In the case of not-for-profit, member owned credit unions; these costs are passed on directly to the member-owners. As discussed above, the statute provides the CFPB considerable authority to make adjustments as it sees fit to effectuate the act. The benefits would be realized immediately as ATM operators would not need to contend, going forward, with frivolous lawsuits spurred by an out of date consumer protection requirement that provides consumers little in the way of actual protection. There would be virtually no governmental or private resources required to realize the benefits. Accordingly, the CFPB should eliminate this requirement.

Account Truncation

NAFCU recommends the CFPB allow financial institutions to truncate account numbers in some cases. Regulation E requires a periodic statement for accounts from which electronic fund transfers may be made. 12 C.F.R. § 1005.9(b). Practically speaking, any checking and savings account falls under the regulation's coverage. Further, § 1005.9(b)(2) requires the periodic statement to include the account number. NAFCU recommends permitting truncation of the account number on the periodic statement. Truncating the account number is a useful way to help combat fraud and identity theft. Indeed, § 1005.9(a) specifically allows for truncation to as few as four digits for receipts at ATMs or other electronic terminals. Understandably, there is a heightened concern that ATM receipts will be quickly discarded in a public place. Periodic statements are, perhaps, less likely to be discarded in a public place, nonetheless, allowing for truncation would help protect consumers by minimizing fraud risks. There is little, if any, reason not to allow truncation in this instance.

Annual Statement Regarding Error Resolution

Regulation E currently requires an annual notice concerning error resolution. The CFPB should eliminate this requirement. Institutions are already required to provide the notice at account opening. Institutions should only be required to send an updated error resolution notice if the institution's policy has changed. Error resolution policies are generally available at branches and online and the CFPB could require the document be made available online in place of the current requirement. Requiring institutions to mail the same policy year after year serves little benefit. Indeed many consumers likely assume the disclosure means there has been some change to the policy. NAFCU recommends the agency eliminate the requirement to send error resolution policies every year if the policy has not changed. For all the same reasons discussed above in the section regarding the annual statement of billing rights, NAFCU believes the CFPB's factors for consideration weigh in favor of making this change.

Regulation P

The agency should also eliminate the requirement that financial institutions send customers annual privacy notices. This requirement is included in 12 C.F.R. § 1016.5. Again, institutions are already required to provide the privacy notice at account opening. The CFPB should eliminate the annual requirement and instead only require a notice after account opening if the institution's privacy policy has changed. Privacy policies are also generally available at branches and online. Requiring institutions to mail the same privacy policy year after year serves little benefit. NAFCU recommends the agency eliminate the requirement for annual privacy policy disclosures in cases where the policy has not changed. For all the same reasons discussed above in the section regarding the annual statement of billing rights, NAFCU believes the CFPB's factors for consideration weigh in favor of making this change.

Regulation C

Under Regulation C, institutions that refinance a single loan in a calendar year must file a Home Mortgage Disclosure Act (HMDA) report. NAFCU recommends instituting a minimum threshold of at least fifty refinance transactions before an institution is subject to the rule. A threshold of fifty would make the rule consistent with Regulation Z, without undercutting the policy rationale of HMDA. Institutions that refinance fewer than fifty transactions per year are arguably not even offering refinancings in the normal course of business. An institution that extends fifty or fewer such transactions is likely only doing so as an accommodation to existing customers. Granted, a threshold exemption will result in a small number of loans going unreported. However, Regulation C will still capture the vast majority of all mortgage loans and refinancing transactions. Further, the very small cost of slightly fewer reporting entities is outweighed by the fact that these entities are likely more willing to extend credit for a refinancing on a case-by-case basis if they can do so without automatically becoming subject to the HMDA reporting requirements.

The agency should also alter the requirement for lenders to guess an applicant's race or natural origin. Currently, if an applicant declines to answer the question, the loan officer is required to provide his or her best guess based on observation or the applicant's surname. Given the breadth and depth of data gathered under HMDA, it does not seem necessary to require lending officers to report their educated guesses. Further, many applicants may find such a guess offensive. Simply put, there is sufficient data to further the goals of HMDA without forcing lending officers to guess the race or national origin of applicants.

Regulation V

Regulation V, which implements the *Fair Credit Reporting Act* (FCRA) requires lenders making firm offers of credit to include certain opt-out disclosures. Specifically, 12 C.F.R. § 1022.54(c)(1) requires a "short notice" regarding opt-out rights. Additionally, 12 C.F.R. § 1022.54(c)(2) requires a "long notice" that includes some of the same information included in the short notice and some additional information. NAFCU recommends streamlining the notices and permitting institutions to provide a single disclosure.

It would also be helpful if the CFPB streamlined and simplified the adverse action notices required under Regulation B and the very similar risk-based pricing notices required under Regulation V. The FCRA and the *Equal Credit Opportunity Act* (ECOA) have virtually identical adverse action notice requirements. In addition, the FCRA has a very similar, but different, risk-based pricing notice requirement. Further complicating the issue, the FCRA's adverse action notice requirements have no implementing regulation. In order to comply with the FCRA's adverse action notice, creditors may use the model forms included in the Board's Regulation B, which implements the ECOA. The rest of the FCRA, however, is implemented through Regulation V.

What's more, the adverse action notice required by Regulation B and the risk-based pricing notice required by Regulation V are virtually identical and are given under similar – but not the same – circumstances. An "adverse action" notice is given if the consumer was denied credit or there was a change in terms of an existing credit arrangement. A risk-based pricing notice is provided to a consumer that receives credit, based in whole or in part on his credit score, on terms that are materially less favorable than the most favorable terms available to a substantial proportion of consumers.

The policy underlying the risk-based pricing notice is identical to the policy underlying adverse action notices (to inform consumers that lenders – or others – are examining their credit history). The content of the two different disclosures is virtually identical. The circumstances under which the disclosures must be made are very similar. Yet, lenders must look to two different regulations to determine how to comply. Further complicating the matter is that the Federal Reserve Board chose to implement most of the FCRA through Regulation V but chose to implement one discrete section (the adverse action notice requirement) through Regulation B.

This is a case where two closely linked issues that had the potential to be confusing have, indeed, grown incredibly complex as a result of the way in which the regulations were implemented. Understandably, some of the issues are a result of the way in which the underlying statutes were written. This is, however, an issue where the CFPB could simplify matters for financial institutions without any substantive change to the protections afforded consumers. NAFCU is not seeking fewer notices or less detailed disclosures. Rather, we only ask that the CFPB reconsider the way in which these closely related statutes are implemented and re-write the regulations in a way that is simple and straightforward.

Conclusion

NAFCU appreciates the opportunity to provide input regarding regulations that can be modified or streamlined, and we very much appreciate the CFPB's decision to make this one of the first items on its regulatory agenda. Credit unions have been forced to contend with a significant number of regulatory changes over the last several years, particularly in regards to TILA and Regulation Z. We are hopeful that the CFPB will move forward and eliminate some of the less useful, redundant or unnecessary provisions in the regulations that it oversees. Should you have any questions or concerns, please feel free to contact me or Carrie Hunt, NAFCU's General Counsel and Vice President of Regulatory Affairs at 703-842-2234.

Sincerely,

Fred R. Becker, Jr.
President/CEO

Forbes

Mickey Meece, Contributor
I write about consumer issues.

RETAIL | 7/18/2012 @ 1:14PM | 1,209 views

What's In Your Wallet? If It's a Capital One Card, You May Be Due a Refund

Capital One (Photo credit: Wikipedia)

Capital One Financial announced settlements with two bank regulators on Wednesday over deceptive marketing practices related to add-on products sold to credit card customers.

As part of a joint settlement, Capital One said it would set aside $150 million to refund two million customers later this year.

In addition, Capital One said it would pay a $25 million civil penalty to the Consumer Financial Protection Bureau and a $35 million penalty to the Office of the Comptroller of the Currency.

In its first public enforcement action, the CFPB found that third-party call-center vendors of Capital One Bank pressured or misled customers into paying for payment protection and credit monitoring products when they activated their credit cards, according to a press release.

Customers with low credit scores or low credit limits were given the hard sell, the CFPB said. For example, some were led to believe the products would improve their credit scores. Some thought the products were not optional, the bureau said, or that the products were free. Some customers were enrolled without their consent, it added.

"We are putting companies on notice that these deceptive practices are against the law and will not be tolerated," said CFPB Director Richard Cordray.

Capital One, in its own release, acknowledged the settlement with CFPB and with the Comptroller of the Currency.

"We are accountable for the actions that vendors take on our behalf," Ryan Schneider, President of Capital One's Card business said in a statement. "These marketing calls were inconsistent with the explicit instructions we provided to agents for how these products should be sold. We apologize to those customers who were impacted and we are committed to making it right."

Between August 2010 and January 2012, as described in both agreements, Capital One said its third-party vendors did not "always adhere to company sales scripts and sales policies for Payment Protection and Credit Monitoring products."

What's more, the agreements stipulate, the bank did not adequately monitor their activities.

The agreement with the OCC also addresses certain billing practices relating to Credit Monitoring products administered by third-party vendors, Capital One said.

Capital One said it learned of the sales practices and lack of monitoring in late 2011. The company said it immediately stopped phone sales of the products and began efforts to identify impacted customers to provide full refunds.

As part of the agreements with regulators, Capital One said it would set aside $150 million to provide the refunds, almost all of which it said would go to customers impacted by the vendor sales practices from 2010-2012.

Under the OCC agreement, about $7 million of the $150 million will go to customers impacted by the billing practices related to Credit Monitoring products administered by third-party vendors between 2002 and 2011, Capital One said.

Separately, Capital One (COF) announced it would release second-quarter earnings a day early after the market closed.

In conjunction with the enforcement action, the Consumer Financial Protection Bureau released two Consumer Advisories. One advisory is intended to make Capital One customers aware of the action and the other serves as a general warning to consumers who may encounter such deceptive practices.

THE WALL STREET JOURNAL.
WSJ.com

Financial Crisis Amnesia
My wife looks up from the newspaper with bewilderment at another story about people in the financial world or their lobbyists complaining about Wall Street reform.
By TIM GEITHNER
March 1, 2012

Four years ago, on an evening in March 2008, I received a call from the CEO of Bear Stearns informing me that they planned to file for bankruptcy in the morning.

Bear Stearns was the smallest of the major Wall Street institutions, but it was deeply entwined in financial markets and had the perfect mix of vulnerabilities. It took on too much risk. It relied on billions of dollars of risky short-term financing. And it held thousands of derivative contracts with thousands of companies.

These weaknesses made Bear Stearns the most important initial casualty in what would become the worst financial crisis since the Great Depression. But as we saw in the summer and fall of 2008, these weaknesses were not unique to that firm.

In the spring of 2008, more Americans were starting to face higher mortgage payments as teaser interest rates reset and they could no longer refinance out of them because the value of their homes stopped rising—the leading edge of a wave of foreclosures and a terrible fall in house prices. By the time Bear Stearns failed, the recession was then already several months old, but it would of course get much worse in coming months.

These problems were partly the result of amnesia. There was no memory of extreme crisis, no memory of what can happen when a nation allows huge amounts of risk to build up outside of the safeguards all economies require.

When the CEO of Bear Stearns called that night, it was not because I was his firm's supervisor or regulator, but because I was then the head of the Federal Reserve Bank of New York, which serves as the fire department for the financial system.

The financial safeguards in the law at that moment were tragically antiquated and weak. Neither the Fed, nor any other federal agency, had the necessary comprehensive authority over investment firms like Bear Stearns, insurance companies like AIG, or the government-sponsored mortgage giants Fannie Mae and Freddie Mac.

Regulators did not have the authority they needed to oversee and impose prudent limits on overall risk and leverage on large nonbank financial institutions. And they had no authority to put these firms, or bank holding companies, through a managed bankruptcy that wound them down in an orderly way or to otherwise adequately contain the damage caused by their failure. The safeguards on banks were much tougher than those applied to any other part of the financial system, but even those provisions were not conservative enough.

A large shadow banking system had developed without meaningful regulation, using trillions of dollars in short-term debt to fund inherently risky financial activity. The derivatives markets grew to more than $600 trillion, with little transparency or oversight. Household debt rose to an alarming 130% of income, with a huge portion of those loans originated with little to no supervision and poor consumer protections.

The failure to modernize the financial oversight system sooner is the most important reason why this crisis was more severe than any since the Great Depression, and why it was so hard to put out the fires of the crisis. The failure to reform sooner is why the crisis caused gross domestic product to fall at an annual rate of 9% in the last quarter of 2008; why millions of Americans lost their jobs, homes, businesses and savings; why the housing market is still so far from recovery; and why our national debt has grown so significantly.

For all these reasons, President Obama asked Congress to pass tough reforms quickly, before the memory of the crisis faded. The Dodd-Frank Wall Street Reform and Consumer Protection Act, signed into law by the president on July 21, 2010, put in place safer and more modern rules of the road for the financial industry. Yet only four years after the financial crisis began to unfold, some people seem to be suffering from amnesia about how close America came to complete financial collapse under the outdated regulatory system we had before Wall Street reform.

Remember the crisis when you hear complaints about financial reform—complaints about limits on risk-taking or requirements for transparency and disclosure. Remember the crisis when you read about the hundreds of millions of dollars now being spent on lobbyists trying to weaken or repeal financial reform. Remember the crisis when you recall the dozens of editorials and columns against reform published on the opinion pages of this newspaper over the past three years.

Are the costs of reform too high? Certainly not relative to the costs of another financial crisis. Credit is relatively inexpensive and growing across most of the U.S. financial system, although it is still tight for some borrowers. If the costs of reform were a material drag on credit growth, then loans to businesses would not have grown faster than the overall economy since the law passed and its implementation began.

Are these reforms complex? No more complex than the problems they are designed to solve. And, it should be noted, most of the length and complexity in the rules is the result of the care required to target safeguards where they are needed, not where they would have a damaging effect.

Is there some risk that these reforms will go too far with unintended consequences? That depends on the quality of judgment of regulators in the coming months as they flesh out the remaining reforms. But our system provides considerable protection against that risk, with the rules subject to long periods of public comment and analysis and with room in the law to get the balance right. The greater error would be for Congress or the regulators, under tremendous pressure from lobbyists, to once again exempt large swaths of the financial industry from rules against abuse.

These reforms are not perfect, and they will not prevent all future financial crises. But if these reforms had been in place a decade ago, then the rise in debt and leverage would have been less dangerous, consumers would not have been nearly as vulnerable to predation and abuse, and the government would have been able to limit the damage that a financial crisis could have on the broader economy. President Obama, along with Sen. Chris Dodd and Rep. Barney Frank, deserves enormous credit for pushing for tough reforms quickly.

My wife occasionally looks up from the newspaper with bewilderment while reading another story about people in the financial world or their lobbyists complaining about Wall Street reform or claiming they didn't need the Troubled Asset Relief Program. She reminds me of the panicked calls she answered for me at home late at night or early in the morning in 2008 from the then-giants of our financial system.

We cannot afford to forget the lessons of the crisis and the damage it caused to millions of Americans. Amnesia is what causes financial crises. These reforms are worth fighting to preserve.

Mr. Geithner is secretary of the U.S. Treasury.

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July 19, 2012

The Honorable Randy Neugebauer
Chairman
Subcommittee on Oversight and Investigations
Committee on Financial Services
United States House of Representatives
Washington, D.C. 20515

Dear Chairman Neugebauer:

On behalf of the Credit Union National Association (CUNA), I am writing about your Subcommittee's upcoming hearing on "Who's In Your Wallet? Dodd-Frank's Impact on Families, Communities and Small Businesses." CUNA is the largest credit union advocacy organization in the United States, representing nearly 90% of America's 7,200 state and federally chartered credit unions and their 95 million members. We appreciate the opportunity to provide comments for this hearing.

As rules are proposed and finalized emanating from the Dodd-Frank Act, compliance burdens will continue to mount against smaller financial institutions such as credit unions. My comments will focus on several key areas related to the Dodd-Frank Act: exemption authority of the Consumer Financial Protection Bureau (CFPB), the remittances rule, qualified mortgage definition, and some general observations about the implementation of the Dodd-Frank Act.

CFPB Exemption Authority

When the CFPB was created, credit unions were assured it would level the playing field by subjecting unregulated entities engaging in abusive practices to the same regulation as credit unions and other highly regulated financial institutions. Congress should continue to remind the CFPB that it was these unregulated companies that were the bad actors in the marketplace and therefore should receive the most scrutiny.

Credit unions were not the cause of the financial and mortgage crisis that prompted Congress to enact legislative remedies to prevent such a calamity from happening again. However, the rules to fix the mortgage market and protect consumers do not solely impact the bad actors – they affect those that acted responsibly as well, such as credit unions. The repeated changes in rulemaking and final rules have a real dollar impact on consumers, especially at credit unions. A dollar spent on regulatory compliance is a dollar diverted from lending. So, in fact, some mortgage reforms in the Dodd-Frank Act do negatively impact access to mortgage credit for consumers.

CUNA believes that the CFPB has the authority to exempt certain entities under Section 1022(b)(3) of the Dodd-Frank Act from a number of regulations the agency is developing. Under this section, the Bureau, "by rule, may conditionally or unconditionally exempt any class of covered persons, service providers, or consumer financial products or services, from any provision of this title, or from any rule issued under this title as necessary or appropriate to carry out the purposes and objectives of this title." CUNA has urged the CFPB to include an analysis of its exemption authority with every proposal and final rule so that every time the agency considers a

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new regulation, it will also consider whether institutions such as credit unions that are already heavily regulated should be exempted.

We are very concerned that the Bureau seems to be picking and choosing when to use statutory flexibility Congress provided to the CFPB in the Dodd-Frank Act. We believe the agency has more authority than it has been exercising, to extend relief to credit unions and others from certain compliance responsibilities. It is important that Congress aggressively urge the CFPB to utilize the exemption clause so that the weight of compounding regulations that are intended for abusers and the largest of financial institutions do not overburden credit unions and other smaller financial institutions.

Remittance Rule

Required by Section 1073 of the Dodd-Frank Act and effective in February 2013, this regulation imposes a series of new requirements on those entities making international remittance transfers. Basically, the regulation requires a "remittance transfer provider" that sends international wire or ACH transfers in the "normal course of business" for consumers to a recipient in a foreign country to comply with very detailed rules. Until now, few credit unions would have ever considered themselves to be "remittance transfer providers," believing this term would cover companies such as Western Union or MoneyGram.

Under the final regulation, any credit union that provides this service to members will have to comply. At the same time the Bureau issued the final regulation (which was 116 pages of text and explanation in the Federal Register), it issued a proposal to define a key term, "normal course of business." The agency proposed a definition that would say any credit union that makes 25 or fewer international remittances a year would not be considered a "remittance transfer provider." Credit unions were surprised at the very low number proposed, which would only help a very, very small number of institutions.

If the Bureau adopts the meaningless 25 annual transfer level, many credit unions have said they will simply stop providing this service to their members because of the burden of complying with this new remittance regulation. Surely this is not what Congress intended.

CUNA originally urged a 2,400 annual transfer threshold for coverage, which was rejected as inconsistent with the statute. We are now asking that a credit union may make at least 1,000 transfers a year before being subject to this burdensome regulation, which we believe is reasonable.

We believe the rule should treat differently those remittance service providers that are in the business for the sole or primary purpose of providing remittance transfers as opposed to credit unions that provide these services as an accommodation to their members who trust them. A credit union can be very small and serve, for instance, an immigrant population who will want such a service. Time and again, the CFPB and members of Congress have acknowledged that credit unions do a good job providing services to their members, and it is a shame when a regulation imposes such a burden that a credit union has to either raise the fee for providing the service or discontinue the service altogether.

The Honorable Randy Neugebauer
July 19, 2012
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Qualified Mortgage (QM) definition

The CFPB has decided to delay until after the November elections the issuance of the Qualified Mortgage rule that will determine proper underwriting standards for borrowers. We wholeheartedly support this delay. CUNA generally supports the proposed definition of "qualified mortgage" and offers the following comments regarding specific provisions of the proposal.

"Safe Harbor" Alternative
CUNA strongly supports the proposed "safe harbor" alternative ("Alternative 1") which would treat "qualified mortgages as a legal safe harbor because the safe harbor approach would provide greater legal protection for credit unions than "Alternative 2" (a "presumption of compliance") with respect to the borrower's "defense to foreclosure" under TILA section 130(k), 15 U.S.C. §1640(k), against creditors that do not preform sufficient "ability to repay" analyses.

Additionally, CUNA believes that adoption of the safe harbor approach, by limiting the legal liability and exposure for prudent mortgage lenders such as credit unions, will limit the costs to consumers and provide greater choice in the marketplace for consumers.

Credit unions have historically engaged in safe and sound mortgage underwriting that includes a robust ability to repay analysis. Credit unions are concerned that, without a safe harbor, they could be faced with significant amounts of frivolous foreclosure defense litigation with respect to future foreclosures. A credit union making a qualified mortgage should be entitled to significant legal protections because it will have gone well beyond its statutory obligations under TILA to do an "ability-to-repay" analysis.

For these reasons, CUNA encourages the subcommittee to urge the CFPB to issue a final rule that structures QM as a strong legal safe harbor, not a rebuttable presumption.

Prepayment Penalties
CUNA does not support the proposal to include within the definition of "prepayment penalties" waived closing costs that can be recouped in the event of prepayment or certain amortized interest because it would discourage the very member-friendly practice of sometimes waiving some of the costs. In addition, the courts and agencies such as the National Credit Union Administration (NCUA) do not consider these items to be "prepayment penalties".

CUNA opposes including within the prepayment penalty definition fees, such as closing costs, that are waived unless the consumer prepays the loan because NCUA has determined that such arrangements are not "prepayment penalties."[1] Federal credit unions are currently not permitted to charge prepayment penalties pursuant to 12 U.S.C. § 1757(5)(A)(viii). Conflicting regulatory

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[1] See, for example, "Prepayment Penalties – Loan Incentives," Letter of Richard S. Schulman, Associate General Counsel, NCUA, to David A. Jones, VP, Hartford Telephone FCU (June 13, 1996) ""When the FCU waives the closing costs, it confers a benefit on the borrower. If the borrower repays his loan within two years and must reimburse the FCU for closing costs, the borrower has simply lost the benefit.") available at http://www.ncua.gov/Legal/OpinionLetters/OL1996-0522.pdf.

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definitions of "prepayment penalty" will lead to increased confusion by credit unions and consumers, and will increase credit union's regulatory burden.

CUNA also opposes the proposed treatment as a "prepayment penalty" of amortized interest occurring after prepayment (such as if a mortgage amortizes monthly on the first of the month and the borrower prepays in full on the 5th of the month, but the creditor continues to charge interest as though the loan were still outstanding until the end of the monthly amortization period). The courts have held that such computation methods are not "prepayment penalties"[2] and requiring credit unions that use this type of periodic amortization calculation to treat this method as a "prepayment penalty" for disclosure purposes would be confusing to consumers and would impose significant regulatory burdens on credit unions while providing limited benefits to consumers.

Lower Documentation "Qualified Mortgages"
Some credit unions serve significant numbers of self-employed people and/or immigrant populations who may not have documents such as W-2 forms, pay stubs, and so forth. In order to ensure continued access to mortgage credit for these groups, CUNA has requested the CFPB clarify that "qualified mortgages" can be underwritten based primarily or exclusively on financial institution records so long as those records show ability to repay.

"Balloon Payment Qualified Mortgages" for Lenders in Rural and Underserved Areas:

CUNA supports the proposal to allow balloon payment mortgages to be considered "qualified mortgages" if made by lenders under $2 billion in assets that operate predominantly in "underserved" and "rural" areas. This is necessary for maintaining consumer access to mortgage credit in these areas because it allows smaller institutions to control interest rate risk.

CUNA supports the proposed $2 billion asset limitation and believes that no additional limitations regarding the creditor's total annual number of mortgages made or total dollar annual value of mortgage transactions are needed given the asset size limitation and the other proposed limitations in the rule.

CUNA does not support, however, the Bureau's proposed definitions of "underserved" and "rural" because these proposed definitions are far too narrow to be meaningful in practice. We believe that the proposed definitions of "underserved" (i.e. counties where only one creditor makes five or more mortgages a year) and "rural" (i.e. only counties that are not within or adjacent to a metropolitan statistical area or a micropolitan statistical area) are far too restrictive and should be expanded to include areas determined to be "underserved" or "rural" by other federal agencies such as the National Credit Union Administration (NCUA) Board.

In our view, limiting the definitions of "underserved" and "rural" to only the most underserved and the most rural counties will have the effect of limiting access to mortgage credit in other

[2] In *Goldman v. First Federal Sav. & Loan Ass'n,* 518 F.2d 1247 (7th Cir. 1975), Judge (and later Supreme Court Justice) John Paul Stevens' majority opinion specifically held that prepaid unearned interest retained by a federal thrift after the borrowers prepaid their loan was not a "prepayment penalty" within the meaning of the Federal Home loan Bank Board regulations. See id. At 1249-54.

objectively underserved and rural areas in a manner inconsistent with Congressional intent. Some counties are objectively underserved even when two or more financial institutions each originate 5 or more mortgages a year and many rural areas are in counties adjacent to or included within a micropolitan statistical area or a metropolitan statistical area.

Delayed Compliance Date

CUNA has urged the Bureau to set a compliance date that recognizes creditors' need for additional time to implement these requirements. Credit unions and other creditors are faced with myriad new regulatory compliance requirements they are trying to meet that also will affect their compliance efforts with this rule. Additional time will be especially important for credit unions and others that rely on third parties, such as software vendors. These third parties will need time to incorporate the necessary updates, complete the necessary testing, and then include this change into their regularly scheduled releases.

General Comments

Credit unions are not-for-profit financial cooperatives, owned solely by its members, who receive the benefit of ownership through reduced fees, lower interest rates on lending products, and higher dividends on savings products. Because of this structure, the cost of a credit union's compliance with unnecessary and unduly burdensome regulations impacts its members directly. Every dollar that a credit union spends complying with an unnecessary or overly burdensome regulation is a dollar that cannot be used for the benefit of its member-owners.

Credit unions are among the most highly regulated financial institutions in the United States, and their regulatory burdens continue to multiply with little or no apparent regard for the costs of each requirement or, more important, the cumulative impact on the institutions that must comply. These concerns are compounded by the range of upcoming regulations credit unions will face under the Dodd-Frank Act. Combined with existing regulatory burdens, the increasing regulatory requirements pursuant to the Dodd-Frank Act and other government initiatives are among the major drivers of credit union consolidation.

Some have called this a "crisis of creeping complexity" because it is not any one particular regulation which makes the ability of smaller credit unions to serve their members difficult, instead it is the steady accumulation of regulatory requirements that can strain a credit union to its breaking point. Credit unions are concerned that these creeping regulatory burdens not only take up an increasing share of credit union employee and volunteer time—often necessitating mergers with larger credit unions—but also stifle innovation in credit union financial services.

Congress should continue its prudent oversight of regulatory agencies as they continue to propose and finalize rules coming out of the Dodd-Frank Act and keep a keen eye on the cost of compliance and growing regulatory burden for smaller financial institutions, such as credit unions, that were not a party to the financial crisis. We served our members through the financial crisis and continue to do so in its aftermath.

The Honorable Randy Neugebauer
July 19, 2012
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Thank you for holding this hearing and receiving our view on this important topic.

Best regards,

Bill Cheney
President & CEO