Testimony of

Salvatore Marranca
Director, President, and CEO
Cattaraugus County Bank

On behalf of the
Independent Community Bankers of America

Before the

United States House of Representatives
Subcommittee on Capital Markets and Government Sponsored Enterprises
Subcommittee on Financial Institutions and Consumer Credit

Joint Hearing on

"H.R. 1697, The Communities First Act"

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Washington, D.C.

Opening

Chairman Capito, Chairman Garrett, Ranking Member Maloney, Ranking Member Waters and members of the subcommittees, I am Sal Marranca, Director, President, and CEO of Cattaraugus County Bank, a $180 million asset bank in Little Valley, New York. I am pleased to be here today to represent the nearly 5,000 members of the Independent Community Bankers of America. Thank you for convening this hearing on the Communities First Act (H.R. 1697). This legislation is a top priority for ICBA and community banks nationwide. We are grateful to Rep. Luetkemeyer for introducing this legislation and to the more than 50 Members from both parties who have cosponsored it.

ICBA strongly supports the Communities First Act because, put simply, it will help community banks better serve their communities by providing carefully crafted regulatory relief without jeopardizing consumer protection or safety and soundness. It will also provide needed tax reforms and encourage individual savings. Rather than a top-down program crafted by academics, the CFA was crafted from the bottom up with input from community bankers who know what will work on Main Street.

Community Banks and Local Economies

Community banks will play an integral role in any broad-based economic recovery. We serve the small towns and rural areas not served by the larger institutions, and we are responsible for 60 percent of all small business loans under $1 million. As the economy recovers, small businesses will lead the way in job creation with the help of community bank credit.

Most community banks are closely-held institutions whose viability is directly tied to the economic life of the communities they serve. My bank has nine offices serving the small communities of rural Western New York. Community bank deposits are reinvested in the community to support local businesses and residents, not transferred out of state. Community banks focus on traditional banking products and have a distinct business model from larger banks and Wall St. firms. Our businesses are built on long term relationships with customers who are also neighbors, parents of our children's friends, and people we see in the community every day. We often deliver customized products that large banks with their mass marketing and volume-based business models cannot or will not offer. We make loans passed over by the mega-banks because we have first-hand knowledge of local conditions and of the character of the borrower that cannot be captured by statistical modeling done in another region of the country. We thrive when the community thrives.

Community Banks are Low Risk Institutions

Early in my career, I was a Senior Bank Examiner with the FDIC for over a decade, and the commitment I made then to safety and soundness I still carry with me today as President of my bank and as Chairman of ICBA. The longevity of my bank – like many

community banks we've been in business for over a century and survived the Great Depression and many intervening recessions – is a testament to our conservative risk management. Our commitment to treating customers fairly is equally strong because our business will thrive or fail based on our reputation in the small communities we serve. These twin commitments to safety and soundness and fair treatment of customers are broadly shared by community banks. Because we are low risk institutions, the manner in which we are regulated should be distinct from that of large banks and Wall Street firms. Regulation calibrated to large bank risks and business models can suffocate smaller banks. This is why the Communities First Act is needed to provide appropriate tiering of regulation and relief for smaller, low risk institutions so that they can better serve their communities.

Growing Regulatory Burden

The steady accretion of regulation over many decades – always added but too seldom modernized or removed – has become a growing threat to community banks. Some of these regulations are sensible and necessary. But, as President Obama recognized in his January Executive Order requiring a government-wide review of existing regulations, others are outmoded, conflicting, overly prescriptive, redundant and overly burdensome. To community banks like mine, regulation is a disproportionate expense, burden, and distraction. We simply don't have the scale of larger banks to amortize the expense of compliance. Cattaraugus County Bank has 65 employees. A compliance staff of five to six employees manages the multiplicity of rules covering every aspect of our business. This is out of proportion to our primary business of lending and deposit taking. My compliance staff is half as large as my lending staff, the 11 loan officers who serve customers directly. Every new regulation is a strain on my staff and the thin margins on which we operate. Every new regulation brings new liability exposure in case we fail to interpret it properly, despite our best efforts. Every hour that I spend on compliance is one hour less to spend with customers or prospective customers who can help our local economy grow.

Regulations are particularly burdensome when they are insufficiently flexible to fit the community bank business model. As I've stated, our competitive advantage with regard to the large banks is offering customized products and services to meet our local customers' needs. Regulations that privilege plain vanilla products, for example, or prohibit certain product features would put our customers at a disadvantage.

Of course, many regulations serve a legitimate purpose. But what's most troubling is the cumulative effect. One of my ICBA colleagues describes it this way: It's like snowflakes falling on a roof. Falling steadily over the course of hours – without any sweeping away – they accumulate enough weight to strain even a well-constructed roof, but you can't identify the one snowflake that was responsible. The problem is the cumulative impact, and a cumulative problem warrants a broad response. That's why the Communities First Act contains 26 provisions. No one of them is a silver bullet. Some of the provisions, while important, are narrow and technical. Others will have a broader impact. All of them are carefully chosen, balanced and fully consistent with the President's Executive

Order. Cumulatively, they will have a real impact for community banks and their customers.

Provisions of the Communities First Act

Of the 26 provisions of the CFA, 18 are within the jurisdiction of this committee. I would like to highlight some of the more important provisions.

Short Form Call Report for Qualifying Banks

The report of condition, or "call report," is an essential tool for bank regulators, providing important information. Insured depository institutions are required to file call reports on a quarterly basis. The call report runs to over 70 pages with schedules covering every aspect of our business. This is useful information, but when a bank has assets of less than $10 billion and is highly-rated and well-capitalized, we believe that it would make sense for regulators to focus their limited resources on undercapitalized institutions. H.R. 1697 would not dispense with the call report for qualified banks. Rather, it would require bank regulators to develop a short form call report that is "significantly and materially less burdensome" to prepare and "provides sufficient material information for the appropriate Federal bank agency to assure the maintenance of the safe and sound condition of the depository institution and safe and sound practices." A qualifying bank would be allowed to file the short form call report in two non-consecutive quarters each year. This change would reduce the burden on qualified community banks without compromising safety and soundness.

Exemption from Escrow Requirement for Mortgages Held in Portfolio

Current law requires creditors to establish escrow accounts for the collection of taxes and insurance in connection with higher-priced mortgage loans. The Dodd-Frank Act lengthened the period during which such accounts must be maintained. While escrow accounts make good sense in many cases in order to protect collateral value, they are simply impractical for many low volume lenders who don't have resources to perform this function in house and for whom outsourcing would be prohibitively expensive. Community banks often lend to uniquely situated borrowers with properties that are atypical due to the location or the acreage. Because the collateral is atypical, the loans are frequently "high priced," as defined by Federal Reserve Regulation Z. This is especially true in the current interest rate environment in which a loan with an annual percentage rate below 6.5 could be considered high priced and therefore subject to the escrow requirement. Given the low profit margins of mortgage lending, an escrow requirement could tip a community bank's decision against remaining in this line of business and lead to further consolidation in the mortgage industry. Rural borrowers in particular would be harmed by industry consolidation because large banks don't comprehensively serve rural areas. When a community bank holds a mortgage in portfolio, they have more than enough "skin in the game" and every incentive to protect their collateral. CFA would exempt lenders with less than $10 billion in assets who hold loans in portfolio from the escrow requirement. This provision would help keep

community banks in the mortgage lending business at a time when it is becoming increasingly hard to compete with large lenders.

Eliminate Annual Privacy Notices When No Change in Policy Has Occurred

Under the Gramm-Leach-Bliley Act, financial institutions are required to provide annual privacy notices to customers even when their policies have not changed. The Communities First Act would eliminate the annual privacy notice when no change in policy has occurred and require annual notices only when a change in policy has occurred or to give a customer the opportunity to opt-out of information sharing, except as provided under an established exception. Annual notices when no change in policy has occurred do not provide useful information to customers and represent an unproductive expense for financial institutions.

Reimbursement for Mandatory Production of Records

A number of Federal agencies have authority to require banks to produce records for investigative and law enforcement purposes under the Right to Financial Privacy Act. However, banks may only claim reimbursement for the expense of producing records when they have been requested by a Federal banking agency. They may not do so when the request comes from the SEC, IRS, or other agencies.

CFA would amend the Right to Financial Privacy Act to require any Federal government agency to reimburse any financial institution with assets of $10 billion or less for the cost of producing records for any Federal law enforcement or investigative purpose. In one case, an ICBA member bank incurred significant expenses in complying with a records request from the SEC. Such cases are not frequent, but the underlying principle is important. Reimbursement of reasonable expenses is only fair and would relieve some community banks of a significant cost burden.

Additional Provisions

There are several additional provisions of CFA that warrant mention. One would raise the exemption for qualifying small bank holding companies from the Federal Reserve's capital adequacy guidelines. This exemption is known as the Federal Reserve Small Bank Holding Company Policy Statement. Another CFA provision would exempt banks with assets of less than $1 billion from the internal control attestation requirement of Sarbanes-Oxley Section 404(b). This exemption threshold is warranted because community bank internal control systems are closely and continuously monitored by bank examiners. Two provisions of CFA address accounting principles. The first would require the SEC to ensure that the reports and other disclosures it requires take into account the business model of the preparer. Specifically, the SEC should differentiate between traders in assets and liabilities and community banks that hold assets and liabilities for the long term and should not be required to revalue them frequently. The other accounting provision would require the SEC to conduct a cost-benefit analysis of GAAP standards. Another provision of CFA, championed by Mr. Perlmutter, would

allow banks with less than $10 billion in assets to amortize losses on commercial real estate loans over 10 years, but only for regulatory capital purposes. This provision, which would be temporary, would encourage workouts and reduce foreclosures. It is modeled on temporary extended amortization approved by Congress in the 1980s to help agricultural lenders. A related provision would address the impact of sudden and temporary drops in real estate values by measuring losses using a rolling five-year average appraisal value instead of a single appraisal. This change, which would apply only for regulatory capital purposes, would provide more useful real estate values by smoothing out potentially wide fluctuations.

Additional provisions which lie outside of the jurisdiction of this committee would reform Subchapter S of the tax code to facilitate capital formation among Subchapter S firms. Some 2,300 community banks are organized under Subchapter S. Bank examiners are constantly telling community banks to raise additional capital. Without access to the broader capital markets, these banks turn to their communities for additional capital. Amending the Subchapter S rules will help them to raise capital in their communities and meet the demands of their examiners. Other provisions would encourage individual savings, extend the 5-year carry back period for net operating losses to 2010 and 2011, create a limited tax credit for community banks to offset the competitive advantage enjoyed by tax-exempt credit unions, and support rural lending.

Finally, I'd like to thank the committee for passing H.R. 1965 which raises the threshold number of bank shareholders that triggers SEC registration from 500 to 2,000. Registration is a significant expanse and an update to the threshold trigger is long overdue. We're grateful to representatives Himes and Womack for introducing this legislation, and we were very pleased to see it pass this committee and the House with nearly-unanimous support. A similar provision is included in CFA, and similar ICBA-backed legislation is now advancing in the Senate.

Closing

This is not a comprehensive description of the Communities First Act, which is beyond the scope of this testimony, but it does fairly represent the range of provisions and the overarching intent and potential impact of the bill. Each provision is carefully selected with input from community bankers nationwide and crafted to preserve and strengthen consumer protections and safety and soundness. There are some 7,000 community banks in this country with different charter types, ownership, tax statuses, and lending specializations, from agriculture to small business to residential mortgage. The Communities First Act is a broad and diverse solution to the regulatory challenges facing a diverse industry. I would also note that credit unions, which are represented at today's hearing and play a significant role in our diverse financial system, would benefit from several provisions of the CFA, including reforms to the Financial Stability Oversight Council review of CFPB rules, reimbursement for mandatory production of records, and the limited restoration of credit ratings for small institutions that do not have internal resources to perform credit analysis.

Left unaddressed, the increasing burden of regulation will discourage the chartering of new community banks and lead to further industry consolidation. Consolidation will lead to higher interest rates for borrowers, lower rates paid on deposits, and fewer product choices – especially in the rural areas and small towns currently served by community banks. A more concentrated industry, dominated by a small number of too-big-to-fail banks, will jeopardize the safety and soundness of the financial system and expose taxpayers to the risk of additional costly bailouts. That's why it's so important to enact the sensible regulatory reforms embodied in the Communities First Act. These reforms will help preserve the community banking model and the rich, diverse financial system that supports our nation's diverse economy.

We encourage you to reach out to the community bankers in your district. Ask them about the current regulatory environment and whether the reforms of the CFA would help them to better serve their customers and the communities of your district. We're confident that they will agree with us. Please consider becoming a cosponsor of CFA. And to the leaders of these subcommittees, we encourage you to act on the CFA soon in response to the struggling economy.

Thank you again for the opportunity to testify today and offer ICBA's perspective on the important reforms of the Communities First Act.

United States House of Representatives
Committee on Financial Services

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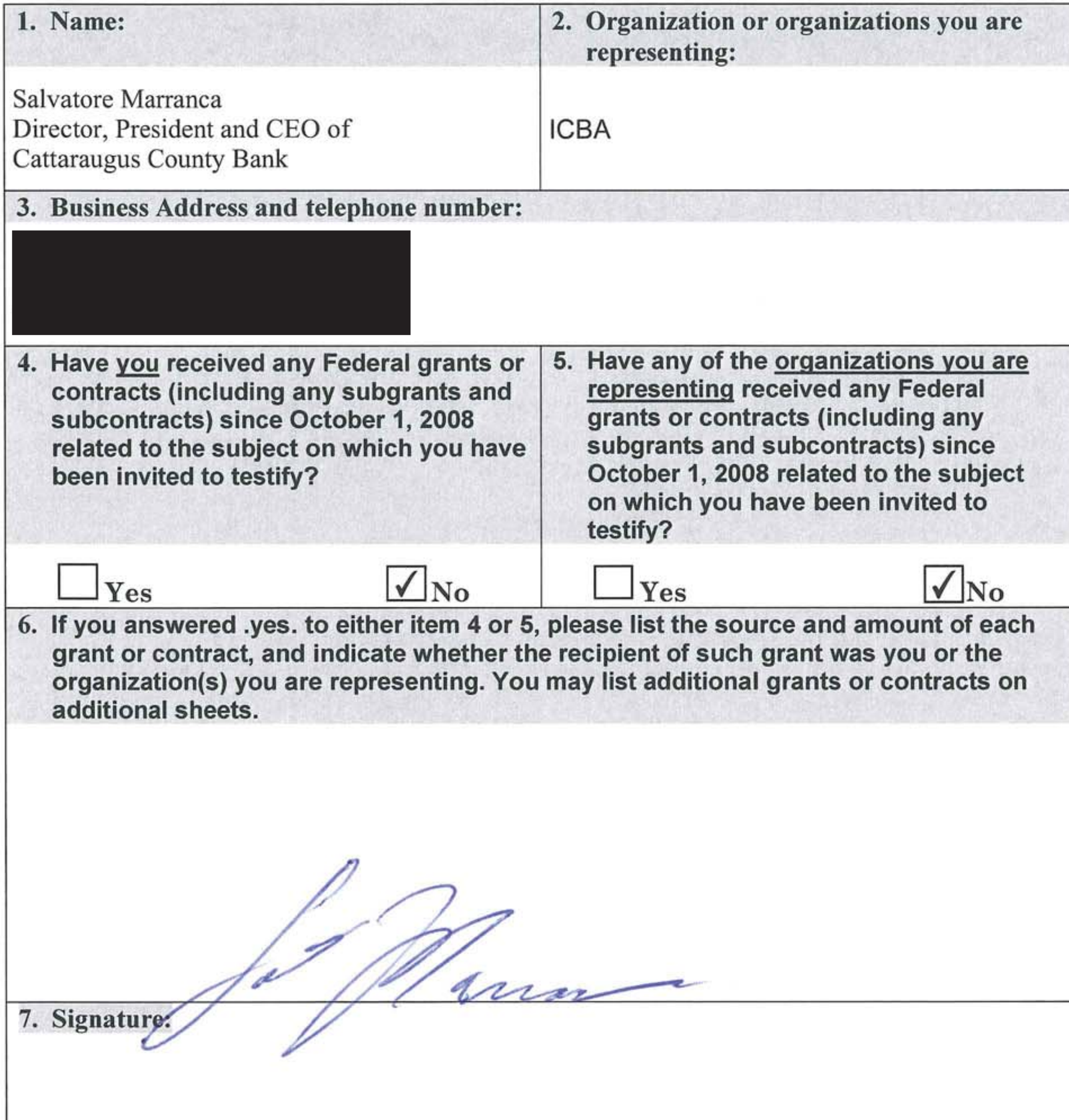

1. Name:	**2. Organization or organizations you are representing:**
Salvatore Marranca Director, President and CEO of Cattaraugus County Bank	ICBA
3. Business Address and telephone number:	
[redacted]	
4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	**5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?**
☐ Yes ☑ No	☐ Yes ☑ No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
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