

July 19, 2011

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*Testimony of*

**Albert C. Kelly, Jr.**

*On behalf of the*

**American Bankers Association**

*before the*

**Committee on Banking, Housing, and Urban Affairs**

*of the*

**United States Senate**



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Chairman Johnson, Ranking Member Shelby, and members of the Committee, my name is Albert C. Kelly, Jr., Chairman and Chief Executive Officer, SpiritBank, a \$1.3 billion bank headquartered in Bristow, Oklahoma. I am also the chairman-elect of the American Bankers Association. I appreciate the opportunity to present the views of the ABA on the new Bureau of Consumer Financial Protection (Bureau). The ABA represents banks of all sizes and charters and is the voice of the nation's \$13 trillion banking industry and its two million employees. ABA is uniquely qualified to comment on the issues related to the Bureau. Not only will the agency's rulemaking impact every bank – large and small – but ABA's membership represents the full range of banks over \$10 billion that will be under direct supervision by this new agency.

SpiritBank has survived many economic ups and downs for 95 years. Our long tradition of service is not unique among banks. In fact, there are 2,735 banks – 35 percent of the banking industry – that have been in business for more than a century; 4,937 banks – 64 percent – have served their local communities for more than half a century. These numbers tell a dramatic story about the staying power of banks and their commitment to the communities they serve. It is a testament to the close attention to customer service.

My bank's focus, and those of my fellow bankers throughout the country, is on developing and maintaining long-term relationships with our customers. We cannot be successful without such a long-term philosophy and without treating our customers fairly.

We are very proud of our relationship with the people and small businesses we serve. They are, after all, our friends and neighbors. The success of SpiritBank is inextricably linked to the success

of our customers and our community. Let me give you just a glimpse of SpiritBank's close ties with our community:

- We held \$847 million in small business loans within our communities at year-end 2010. The new rigors of regulation and capital requirements have meant that we cannot continue to lend at this level.
- We funded 25,960 mortgage loans for families in ten states last year, none sub-prime, for a total of \$3.8 billion.
- We contributed over \$550,000 dollars last year and our 330 employees have logged thousands of hours of service to schools, charitable organizations, and civic and community organizations throughout our area – in a year in which our investors saw no return to them. We far exceeded this amount in years when the economy has been good.
- We started an Entrepreneurial Spirit Award in one of our large communities, launching 20 to 30 companies each year at an annual cost to us of \$100,000 each year.

***The banking industry fully supports effective consumer protection.*** We believe that Americans are best served by a financially sound banking industry that safeguards customer deposits, lends those deposits responsibly, and processes payments efficiently. My bank's philosophy – shared by banks everywhere – has always been to treat our customers right and do whatever we can to make sure that they understand the terms of the loans they are taking on and their obligations to us. Traditional FDIC-insured banks – more than any other financial institution class – are dedicated to delivering consumer financial services right the first time. Not only do we have the compliance programs and top-down culture to prove it, we are required to have the financial wherewithal – in terms of capital, liquidity and asset quality – to be there when our customers need us.

***Fair service to our banking customers is inseparable from sound management of our banking business.*** Yet despite this axiom, the Dodd-Frank Act erected a Bureau that divides consumer protection regulation from safety and soundness supervision. Therefore, it is critical that improvements be made to assure this new Bureau is accountable to the fundamentals of safe and sound operation, to the gaps in regulating non-banks that motivated financial reform, and to the principles of consistent regulatory standards consistently applied.

There are several features of the Bureau that make improved accountability imperative. In addition to the weakening of any connection between the Bureau's mission and safety and soundness concerns, Dodd-Frank gave the Bureau expansive new quasi-legislative powers and discretion to re-write the rules of the consumer financial services industry based on its own initiative and conclusions about the needs of consumers. The prerogative of Congress to decide the direction and parameters of the consumer financial product market has essentially been delegated to the Bureau. The resulting practically boundless grant of agency discretion is exacerbated by giving the head of the Bureau *sole authority* to make decisions that could fundamentally alter the financial choices available to customers.

Furthermore, the proliferation and fragmentation of enforcement authority that Dodd-Frank has distributed among the Attorneys General in every state and the prudential regulators unleashes countless competing interpretations and second-guessing of the supposed baseline "rules of the market." This will result in complicating and conflicting standards.

At risk is the entire body of rules that has governed the development, design, sales, marketing, and disclosure of all financial products; they are subject to change under the Bureau, and could change dramatically in many instances. When developing and offering products, firms rely on the basic rules of the road, knowing that they are subject to careful changes from time-to-time. This uncertainty can cause firms to pull back from developing new products and new delivery systems. It also makes banks think twice about various types of lending if they are uncertain what the rules will be when they try to collect the loan a few years out. This problem should not be underestimated.

For all these reasons and others, it is ABA's first priority to improve the accountability of the Bureau. Establishing accountability supersedes other important priorities regarding the Bureau, including ensuring appropriate bank-like supervision of non-banks for consumer protection. During consideration of the legislative proposals that became the Dodd-Frank Act in the last Congress, ABA recommended provisions designed to increase the accountability of the CFBP because we were greatly concerned about the concentration of authority in a single director of this agency. Our concern was focused on the fact that the Bureau has authority over already supervised insured depositories as well as unsupervised or lightly supervised non-banks. Our concern remains the same. We urge the Congress to pass statutory provisions that ensure such accountability before the Bureau is established with a single director.

To restore the necessary accountability of the Bureau, ABA offers several recommendations:

- Strengthen accountability by making meaningful structural changes;
- Reinforce the focus of the Bureau's authority on the regulatory gaps; and
- Improve consistency in the application of consumer protection standards.

I will address each of these broad suggestions in turn and propose specific steps that Congress should consider to address the concerns about the Bureau's accountability. Before that, though, I think it is very important to dispel a myth that continues to color the debate on the Bureau: that community banks like mine are exempt from the new Bureau. ***Community banks are not exempt.*** All banks – ***large and small*** – will be required to comply with rules and regulations set by the Bureau, including rules that identify what the Bureau considers to be “unfair, deceptive, or abusive.” Moreover, the Bureau can require community banks to submit whatever information it decides it “needs.”

The Bureau will have direct supervisory authority for consumer compliance of larger banks (with assets greater than \$10 billion) – which adds another layer of regulation and supervision – and can join the prudential regulator by doubling up during any small-bank exam at the Bureau's sole discretion. It is also true that bank regulators will examine smaller banks for compliance at least as aggressively as the Bureau would do independently. In fact, the FDIC has created a whole new division to implement the rules promulgated by the new Bureau, as well as its own prescriptive supervisory expectations for laws beyond FDIC's rule-making powers. Thus, the new legislation will result in new compliance burdens for community banks and a new regulator looking over our shoulders.

This is no small matter. The CFPB, while significant, is only one change among hundreds that will adversely affect the banking industry and the communities we serve. Already there are 2,762 pages of proposed regulations and 607 pages of final regulations – and this is before the CFBP undertakes any new changes or rulemakings. It is important to understand that our bank, indeed, any small business, can only bear so much. Most small banks do not have the resources to easily manage the flood of new rules.

The totality of all the changes, brought about by Dodd-Frank, including those expected under the Bureau, and the excessive regulatory second-guessing by the regulators has consequences for our communities. Higher costs, restrictions on sources of income, limits on new sources of capital, and excessive regulatory pressure, all make it harder to meet the needs of our communities. Jobs and local economic growth will slow as these impediments inevitably reduce the credit that can be provided and the cost of credit that is supplied. Fewer loans means fewer jobs. Access to credit will be limited, leaving many promising ideas from entrepreneurs without funding. Capital moves to other industries, further limiting the ability of banks to grow. Since banks and communities grow together, the restrictions that limit one necessarily limit the other.

Let me now turn to specific recommendations for improvements and ABA's thoughts on the several new legislative proposals that are under consideration.

## **I. First Priority: Strengthen Accountability with Meaningful Structural Changes**

ABA believes that a board or commission structure is appropriate to address the unfettered authority of the Bureau's director to impose new rules. Having only one Senate-confirmed director vests too much power in one person and lacks any effective checks and balances. A board or commission would help to provide accountability and balance. It would also broaden the perspective on any rulemaking and enforcement activity of the Bureau, and would provide needed balance and appropriate checks in the exercise of the Bureau's authority. It will facilitate continuity of the organization and enhance predictability about rulemaking over time.

ABA believes that the board or commission should include members with consumer finance business experience and direct safety and soundness regulatory expertise. Such expertise provides an important and necessary perspective as standards are set and enforcement activities undertaken. Such an important feature will also improve accountability and help redress the separation between consumer protection and sound financial management.

ABA also urges Congress to consider requiring one of the seats in the board or commission be filled with the recently created, statutorily-mandated position of the Vice-Chairman for Supervision of the Federal Reserve Board. We believe that the inclusion of the Vice-Chair for Supervision provides necessary and current safety and soundness experience that directly addresses a pivotal deficiency of the existing structure. The Vice-Chair for Supervision is a unique official who has oversight responsibility both for large financial holding companies (which include the nation's

biggest banks and credit card issuers) and state chartered community banks that are Federal Reserve members. This broad responsibility and expertise would be invaluable to achieving the missing accountability for safety and soundness that the current structure lacks.

Another fundamental structural flaw of the Bureau's structure is that *only* the Director is appointed by the President and approved by the Senate. A board or commission structure corrects this shortcoming.

ABA also supports changing the voting standard for the Financial Stability Oversight Council's (FSOC) review of Bureau rule-making *to a simple majority* rather than a two-thirds vote. It should clearly be sufficient to set aside a Bureau rule if a simple majority of the nation's top regulators believes the Bureau has acted in a manner that adversely impacts the safety and soundness of the American banking or financial system. The stakes are too high to let one agency's rule create such significant risk. The very purpose of the FSOC was to avoid problems that could lead to risks that threaten the economy. To ignore the majority viewpoint of those with this responsibility is completely counter to the mission of this council. Congress should erase the super-majority requirement for FSOC authority set in Dodd-Frank and replace it with a simple majority requirement.

In addition, ABA believes that the standard for the FSOC review of Bureau actions – systemic risk – is also flawed. Much harm can be inflicted that would impair whole subsets of legitimate market players without necessarily rising to the level of a banking, let alone a financial, system risk. For example, a Bureau rule that severely threatens the viability of community banks will not create a system risk. But each bank that disappears from the community makes that community poorer. Customers that have been served by local banks for decades may face fewer choices, less access to credit, and higher costs. Will the FSOC really conclude that the loss of large numbers of community banks rises to the level that demands a systemic risk ruling? ABA strongly urges Congress to re-calibrate the review standard by which the FSOC may act in setting aside a Bureau rule so that action may take place on less than system-wide impacts or risks.

Furthermore, the FSOC review process for Bureau rules is administratively cumbersome and complicated, filled with timing pitfalls. For example, a petition must be filed that attests to objecting agency "good faith" within ten days of rule publication; it must be transmitted "contemporaneously" to Congressional committees; a stay of 90 days duration may be applied for, but without a stay the petition will be deemed denied if the FSOC does not issue a decision in 45

days. As constructed, this convoluted process represents precisely the kind of bureaucracy that gives government bureaus a bad name. ABA urges Congress to fix this review process so that there is at least some reasonable expectation that it can be successfully invoked.

## II. Reinforce the Focus of the Bureau's Authority on Regulatory Gaps

Even the strongest proponents of the Bureau acknowledge the fact that traditional banks were not the cause of the financial crisis. Rather, unsupervised non-bank lenders and unregulated packagers of collateralized mortgage obligations (CMOs) were allowed to take excessive risks in spite of *existing* laws that could have stemmed the tide of corrosive market conduct by non-depositories. The system failed to enforce laws – *already on the books* – against predatory practices by many of those firms and it failed to bring market discipline to bear on underwriting standards against which bankers were hard pressed to compete. Yet here we are, the surviving bankers, facing a new bureaucracy charged with making sense of the often conflicting, never intuitive, and always burdensome compliance obligations.

As we noted above, establishing accountability is the number one priority. Once that goal is achieved, the Bureau must be held accountable for directing its resources to the glaring gap in regulatory oversight – a failure to supervise and pursue available enforcement remedies against *non-bank* lenders committing predatory practices or other consumer protection violations. To this end, ABA sees value in Section 1016(c)(6) of the Dodd-Frank Act requiring the Bureau to report on actions taken “with respect to covered persons which are not credit unions or depository institutions.” In addition, we welcome current efforts to define the Bureau’s non-bank supervisory scope as it prepares for the future exercise of that supervisory authority.

ABA believes that the best way to keep the Bureau accountable to the Dodd-Frank objectives in section 1021(b) would have been to have the Bureau concentrate solely on rationalizing the laws and powers already on the books before passing any new authority. Unfortunately, in the process of transferring existing unfair and deceptive acts or practices authority, the unwarranted addition of “abusive” was inserted.

This addition opens wide all manner of after-the-fact excuses for rewriting the conditions of transactions entered into by customers who had complete information and competitive alternatives. It is an end run around the well-established statutory criteria that Congress and the courts have defined for conduct that is either deceptive or unfair. ABA strongly urges the Congress to eliminate the term “abusive” from the Bureau’s prohibitions. This is the most effective method of keeping the

Bureau focused on and accountable to the task of reforming the more-than-adequate authorities it has inherited from its predecessor regulators and shaping those into simpler, more effective, and less burdensome consumer protections.

### **III. Improve Consistency in the Application of Consumer Protection Standards**

As discussed above in detail, the Bureau represents an unaccountable regulatory entity. While this alone is bad enough and should be addressed, the problem is magnified by other authorities granted in Dodd-Frank. The Act gives license to pile on additional state law requirements and gives unfettered authority to State Attorneys General and prudential regulators – acting on their own initiative – to enforce Bureau statutory authorities and rules. Both of these expansive powers erode Bureau accountability for achieving uniform rules for all consumers to be protected by and all providers to abide by. Even if one can make the Bureau answerable for its market defining rules, neither Congress, nor bankers nor customers can rely on such rules remaining intact in the states where they all reside. This broad delegation of legislative license, interpretive power and prosecutorial discretion – without adequate check by either the Bureau or other federal banking agencies – exposes all banks to uncertain market expectations, compounded compliance obligations, and potentially crippling litigation risk.

Accordingly, ABA recommends that Congress consider three possible constraints on these threats to consistent consumer protection standards consistently applied:

- Adopt statutory language prohibiting states from imposing additional consumer protection requirements without meeting the same cost benefit, credit access and burden reduction objectives that Dodd-Frank imposes on the Bureau (and demonstrated with the same level of data analysis expected of the Bureau).
- Adopt statutory language precluding prudential regulators or enforcement authorities from establishing rules, guidance, supervisory expectations or prosecutorial actions that extend obligations with respect to consumer financial products or services beyond requirements contained in rules of the Bureau.
- Adopt statutory language limiting State Attorneys General from seeking remedies of any conduct by a covered person occurring prior to the last exam report date of any exam by the Bureau or a prudential regulator.

The premise of the Bureau of Consumer Financial Protection was that it would result in a single set of rules of the road for consumers, industry and investors to abide by for the benefit of all. If we are to hold the Bureau accountable to this premise, we must hold accountable all those who derive authority from its existence to abide by the same rules of the road. To do otherwise – by allowing new rules to be written or applying new interpretations each time a state border is crossed – would completely undermine the reliance of all citizens on the Bureau’s rules.

## **Conclusion**

The banking industry fully supports effective consumer protection. Traditional FDIC-insured banks have a long history of delivering consumer financial services right the first time and banks have the compliance and top-down culture to prove it.

It is an inescapable fact that fair service to our banking customers is inseparable from sound management of our banking business. Yet despite this axiom, the Dodd-Frank Act erected a Bureau that divides consumer protection regulation from safety and soundness supervision. It is for this reason that Congress should act to enhance the accountability of the Bureau by dealing with the problems brought about by the extensive new powers of the agency, the unfettered authority of the Director to impose new rules, the separation of consumer protection from financial institution safety and soundness, the gaps in regulating non-banks, and the expanded and unaccountable enforcement authority of prudential regulators and state attorneys general.

My bank’s philosophy – shared by banks all across this country – has always been to treat our customers right and do whatever we can to make sure that they understand the terms of the loans they are taking on and their obligations to us. We will continue to do this, but now there will be many new hurdles that we will have to jump to serve our customers’ most basic needs that will inevitably add cost, time, and hassle for my customers.

Banks are working hard every day to make credit and financial services available. Those efforts will be made more difficult by the hundreds of new regulations expected from the Dodd-Frank Act. I worry about how my bank will handle all the new compliance obligations; I cannot imagine how the median size bank with \$156 million in assets and 37 employees can handle this truckload of new compliance obligations. Even more troubling is what it means for my community. The more time bank personnel devotes to parsing regulatory requirements, the less time they can devote to the financial and credit needs of bank customers. Thus, it is critically important that

Congress be vigilant in overseeing the regulatory actions of the Bureau and other rules stemming from the Dodd-Frank Act to assure they do not restrict access to responsive financial products by responsible American families.