

Testimony of Bradley E. Rock
on behalf of the
American Bankers Association
before the
Committee on Banking, Housing and Urban Affairs
United States Senate
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Mr. Chairman and members of the Committee, my name is Bradley Rock. I am Chairman, President and CEO of Bank of Smithtown, a \$750 million community bank located in Smithtown, New York founded in 1910. I am also Chairman of the Government Relations Council of the American Bankers Association (ABA). ABA, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

I am glad to be here today to present the views of the ABA on the need to reduce or eliminate unnecessary, redundant, or inefficient regulatory burdens that increase costs not only for banks, but also for the customers and businesses that use banks – and that's nearly everyone.

In my testimony, I would like to make three key points:

- Excessive regulatory burden is not just a problem for banks – it has a significant impact on bank customers and local economies.
- The regulatory burden is significant for banks of all sizes, but pound for pound, small banks carry the heaviest regulatory load. The community bank, which has been the cornerstone of economic growth in this country, is in great danger of being regulated right out of business.
- The ongoing review of regulatory costs by the federal bank regulators is very positive; results are what counts, however, and many bankers are skeptical that significant relief from the regulators is possible without congressional action.

The federal banking agencies, which are now in the fourth phase of the 10-year regulatory review required by the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA), are evaluating ways to reduce unduly burdensome regulations. EGRPRA, which became law in 1996, is the last comprehensive regulatory relief bill enacted by Congress. In the decade following EGRPRA's enactment, banks have struggled to shoulder the effects of some of the most imposing legislation of the past 100 years. Much of it was prompted by renewed focus on accounting practices and heightened security in the aftermath of September 11th. While the impetus behind the compliance obligations imposed by the USA PATRIOT Act, the Sarbanes-Oxley Act, and the privacy provisions

of the Gramm-Leach-Bliley Act (GLBA) are reasonable, too often their enforcement and practical effects are not.

When the cumbersome layering of additional rules, issued by the Securities and Exchange Commission (SEC), the Financial Accounting Standards Board (FASB), the Public Company Accounting Oversight Board (PCAOB), and the American Institute of Certified Public Accountants (AICPA) are also taken into account, it is abundantly clear that bank resources are being stretched too thin. Obviously, this is not in the interest of banks, but it also means that banks have fewer resources available to meet the stated policy goals of lawmakers and regulators.

We have submitted comments to regulators recommending changes that involve the Bank Secrecy Act (BSA), including discontinuing currency transaction reports (CTRs) for seasoned customers, eliminating the verification requirement for customers purchasing monetary instruments, and establishing a standard for suspending repetitive SAR filings on continuing activities in which law enforcement has no interest. Other suggested changes involve such issues as appraisal standards, real estate lending standards, and annual audit and reporting requirements.

We have long since reached a point where only the active involvement of Congress can result in a comprehensive reduction of outdated, inefficient, and costly regulatory burdens. A more detailed explanation of some of the areas in which ABA is seeking reform is found at the end of this testimony in the appendix.

I. Regulatory Burden Has an Impact on Bank Customers and Local Economies

Reviewing regulations and their impact on our businesses and communities should be an ongoing process, as the marketplace continues to change rapidly. Outdated laws and regulations only squander scarce resources of banks that could otherwise be used to provide financial services demanded by our customers. New laws, however well intentioned, have added yet more layers of responsibilities on businesses like ours. While no single regulation by itself is overwhelming to most businesses, the cumulative weight of all the requirements is overwhelming. It is like boxing outside of one's weight class. Even the best moves will not, in the end, overcome the disadvantages of being dwarfed by the size of your challenger. New laws add heft to the regulatory burden. Banks are against the ropes.

The burden of regulation has a significant impact on bank customers and local economies. Compliance costs are a significant drain on bank resources, taking precious resources away from meeting the needs of our customers. And every new law, regulation or rule added means two things: more expensive bank credit and less of it. This is likely to hurt small businesses the most, as they cannot go directly to the capital markets, yet need low-cost financing. The result is slower economic growth.

During the past 25 years, the compliance burden has grown so large and is so pervasive throughout all levels of bank management that it is extremely difficult to measure. Research done by the ABA and the Federal Reserve¹ indicates that the total cost of compliance *today* for banks would range from \$34 billion to \$42 billion per year and this does not include compliance costs due to

¹ "Survey of Regulatory Burden," American Bankers Association, June 1992; Elliehausen, "The Cost of Banking Regulation: A Review of the Evidence," Staff Study, Board of Governors of the Federal Reserve System, April 1998.

legislation enacted in the last five years, such as the USA PATRIOT Act and Sarbanes-Oxley. Compliance costs are expected to grow at an even faster pace in the coming years.

Certainly, some of the regulatory cost is appropriate for safety and soundness reasons. But consider the direct impact on bank lending and economic growth if this burden could be reduced by 20 percent and redirected to bank capital; it would support additional bank lending of \$69 billion to \$84 billion. This would clearly have a big impact on our economies. In fact, it represents nearly 10 percent of all consumer loans or 11 percent of all small business loans.

II. Community Banks Are In Danger of Being Regulated Right Out of Business

Regulatory costs are significant for banks of all sizes, but pound for pound, small banks carry the heaviest regulatory load. For the typical small bank, about one out of every four dollars of operating expense goes to pay the costs of government regulation. For large banks as a group, total compliance costs run into the billions of dollars annually.

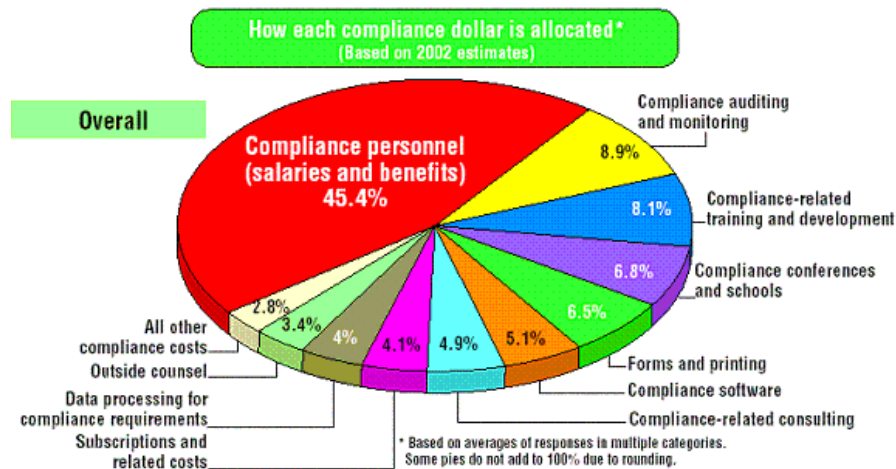
The cumulative effect of new rules and regulations will ultimately force many community banks to look for merger partners to help spread the costs; some will go out of business altogether or consolidate with larger banks. Our members routinely mention regulatory burden as the first or second critical factor threatening the viability of his or her community bank. I can tell you, Mr. Chairman, the pressures to comply with all the regulations and still meet the demands of our customers are enormous. We feel that we must grow the bank rapidly to generate more revenues simply to pay for the ever-increasing regulatory cost. The sad part is that too much time and effort is now devoted to compliance and not to serving our customers.

Bankers at all levels, from bank directors and CEOs to compliance managers and tellers, spend endless hours on compliance paperwork. Much of this work falls heavily on tellers. For example, they fill out the more than 13 million CTRs filed annually. Yet the 35-year-old rules related to CTRs have become redundant and lost their usefulness due to several developments, including formalized customer identification programs; more robust suspicious activity reporting; and, government use of inquiry and response processes.

At Bank of Smithtown, every person in every department has major compliance responsibilities. Because of the complexities involved, my bank pays more than \$100,000 each year to outside firms to help us with the big compliance issues. On top of this, one person on my staff has a full-time job just to coordinate all the activities throughout the bank related to regulatory compliance.

I personally spend about one-and-a-half days per week just on compliance issues. Some CEOs tell me that they are now spending nearly half of their time on regulatory issues. This means that for banking alone, CEOs spend over 5.5 million hours per year on compliance – time that could have been better spent on ways to expanding their businesses and to meet the changing needs of their customers.

Of course, labor costs are a small part of the entire cost required to meet all the compliance obligations that we have. In addition, banks spend billions annually on compliance training, outside compliance support (including accounting firms, consultants and attorneys), compliance related hardware and software, printing, postage, and telephone connections.



Source: *Compliance Watch*, 2003. *Nationwide Bank Compliance Officer Survey*. ABA Banking Journal, June 2003.

Banks that can least afford increasing compliance costs are hit the hardest. Consider a small bank, which can have as few as 20 employees or less. In order to fulfill their compliance obligations, banks of this size often are forced to hire an additional full-time employee just to complete reports related to BSA. Not only is this a huge expenditure of time and money, but bankers wonder if these reports are even being read. The cost versus benefit analysis fails to make the case for many of the rules and regulations banks must follow, and the reports that we generate.

In fact, there are more than ***3,200 banks and thrifts with fewer than 25 employees; nearly 1,000 banks and thrifts have fewer than 10 employees.*** These banks, which serve primarily small communities in non-urban areas, simply do not have the human resources to run the bank *and* to read, understand and implement the thousands of pages of new and revised regulations, policy statements, directives, and reporting modifications they receive every year. According to the Small Business Administration's Office of Advocacy, the total cost of regulation is 60 percent higher per employee

for firms with fewer than 20 employees compared to firms with more than 500 employees due to the fixed costs associated with regulations.²

Banks that are regulated by more than one bank regulatory agency have a particular challenge, in that opinions about what is correct or adequate with regard to certain regulatory requirements differ between agencies. Such banks currently lack one definitive answer about what is required and necessary to comply with any specific aspect of a regulation. Another challenge facing institutions is the fact that compliance regulations can come from a variety of sources such as the SEC, FASB, PCAOB, and AICPA. The system lacks monitoring of the overall increasing regulatory and reporting burden on financial institutions. Just over the last few years, numerous accounting changes have been issued and have cost the industry an enormous amount of valuable staff time and money to implement. A few of the most recognizable rules include: fair value disclosures, accounting for derivatives, accounting for guarantees, accounting for loan loss reserves, accounting for special purpose entities, and accounting for purchased loans. These rules are being issued at a very rapid speed with an extraordinarily short amount of time given to implement them; this presents a significant challenge to all banking institutions. Moreover, we are concerned that a significant amount of time, effort and expense has been directed to rules that have not been demanded by investors and will not be used or even understood by them.

While we recognize there have been positive benefits of the Sarbanes-Oxley Act, banks have experienced inordinately large increases in annual auditing fees as a result of it and new rules developed by the PCAOB. Even non-publicly traded banks have been impacted. Many community

² Crain and Hopkins, "Impact of Regulatory Costs for Small Firms," Small Business Administration, Office of Advocacy, 2001

banks' accounting fees have more than doubled. *One community bank in New York saw its accounting fees jump from \$193,000 in 2003 to more than \$600,000 in 2004.*

Not only have outside auditing fees increased tremendously, but so too have attorneys' fees and insurance costs. Many publicly traded community banks are exploring whether to de-register under the Securities Exchange Act of 1934 because the huge regulatory expenses and the doubling – and even tripling – of accounting and legal costs that result directly from Section 404, Management Assessment Of Internal Controls, and other provisions of the Sarbanes-Oxley Act. We urge that the Committee look at the costs versus benefits in the application of some of the Act's provisions to community banks. We have also asked the SEC to increase the 500 shareholder registration threshold.

The bottom line is that too much time and too many resources are consumed by compliance paperwork, leaving too little time and resources for providing actual banking services. I'm sure I speak for all bankers when I say that I would much rather be spending my time talking with our customers about their financial needs and how my bank will fulfill them than poring over piles of government regulations. The losers in this scenario are bank customers and the communities that banks serve.

III. Congressional Support for Burden Reduction is Critical

The agencies have made considerable progress in the last several years in improving some of their regulations. Nonetheless, not all of the agencies' regulations have been so revised, although we certainly recognize that, in many cases, the agencies are constrained by the language of statutes in reducing the burdens in a meaningful fashion.

We are hopeful that the current review of bank regulations, required under EGRPRA, will provide meaningful relief. We applaud the openness of the banking regulators to the concerns of the industry as they conduct this review. Doubt exists as to whether this effort will be – or even can be – successful in achieving a meaningful reduction in the burden unless Congress becomes an active partner. Most bankers have seen previous regulatory relief efforts come and go without noticeable effect, while the overall level of regulatory burden has kept rising. Results are what matters.

There is a dilemma here: at the same time that the regulatory agencies are undertaking a review of all regulations with an eye toward reducing the overall compliance burden, they must promulgate new rules for the new laws that Congress has enacted. Simply put, any reduction in existing compliance obligations is likely to be obliterated by compliance requirements of new regulations implementing new laws.

It should be noted that even when Congress has acted to reduce a burden, the agencies have at times not followed through. For example, in 1996, Congress amended RESPA so as to reduce the amount of information that must be provided to mortgage customers relating to a lender's sale, transfer or retention of mortgage loan servicing. This change eliminated the requirement that lenders provide historical data on the likelihood of this transfer and that customers acknowledge receipt of this information in writing. ***HUD has never implemented this statutory change to RESPA.*** Thus, since 1996 HUD's regulation continues to require language in the disclosure form, which Congress struck from the statute. This creates an unnecessary burden on banks. ABA pointed this out to Congress years ago and HUD has still not implemented this 1996 statutory change.

Bankers continue to be concerned about “the uneven playing field” in compliance between depository institutions and other financial institutions. While bankers spend increasing amounts of time and money dealing with regulatory red tape, non-bank competitors, including money market funds and mutual funds, are selling savings and investment products to bank customers. The same is true of credit unions and the Farm Credit System, both of which are free from much of the red tape and expenses imposed on banks. Even when the regulatory requirement is the same on paper, such as the case with the Truth in Lending requirements, non-bank competitors are not subject to the frequent, in-depth, on-site examination that banks are subject to. The result is slower growth for banks, leaving fewer community resources available for meeting local credit needs.

Bankers know that their loans will be examined for consumer compliance at least once every two years. They also know that non-bank lenders will not have their loans examined, probably ever, because the Federal Trade Commission (FTC) and the state agencies that have jurisdiction over them do not have the examination and supervision infrastructure to do so. One solution is to fund, by assessment of the non-bank lenders, if necessary, a real supervisory examination program to stop some of the consumer abuse and predatory lending that we hear about constantly. Congress should ensure that the FTC has the resources to actually enforce against non-bank lenders the consumer protection laws currently in effect.

Importantly, the EGRPRA mandate encompasses more than just regulatory action: it calls for the agencies to advise the Congress on unnecessary burdens imposed by statute, which the agencies cannot change but the Congress can. As noted, in many cases, meaningful compliance burden reduction cannot be achieved absent statutory changes. Mr. Chairman, we hope this Committee will seriously consider the recommendations made under this effort.

Conclusion

In conclusion, the cost of unnecessary paperwork and red tape is a serious long-term problem that will continue to erode the ability of banks to serve our customers and support the economic growth of our communities. We thank you for continuing to look for ways to reduce the regulatory burden on banks and thrifts, and to restore balance to the regulatory process. Mr. Chairman, the ABA is committed to working with you and the members of this Committee to achieve this goal.

Appendix

Recommended Changes in Regulation

Currently, the most burdensome of regulations are the combined anti-terrorist, anti-criminal financial information laws. Not only are the demands on banks enormous but they seem to change daily, which is its own form of burden. But there are many other areas that should be addressed. Below is a summary of some recommended areas for reform. ABA is pleased to offer more detailed information to the Committee upon request on any of these points:

a. Bank Secrecy Act (BSA)/Anti-Money Laundering

- **Eliminate CTR Filings for Seasoned Customers**

ABA and its members strongly believe that the current Currency Transactions Report (CTRs) standards have long departed from the statutory goal of achieving a high degree of usefulness. ABA members believe that CTR filing has been rendered virtually obsolete by several developments: formalized customer identification programs, more robust suspicious activity reporting and government use of the 314(a) inquiry/response process. We believe that maintaining the CTR threshold at the current level generates too many reports that capture extensive immaterial activity wasting banker and law enforcement time that could be spent on Suspicious Activity Report (SAR) detection and investigation. Consequently, we believe that the time has come to recognize the redundancy of CTR filings for seasoned customers with transaction accounts to eliminate this inefficient use of resources by bankers and law enforcement.

- **Eliminate Identity Verification for Monetary Instruments Conducted by Customers**

In view of the passage of the USA PATRIOT Act and the regulations implementing section 326 requiring a Customer Identification Program (“CIP”), we recommend that the verification requirement of 31 CFR 103.29(a)(ii) be eliminated, since bank customers purchasing these instruments will have already been identified through their institution’s CIP program.

- **Eliminate Notification to Directors or Designees of SARs**

The federal banking agencies instruct a bank that “whenever [it] files a SAR ..., the management of the bank shall promptly notify its board of directors, or a subcommittee of the board of directors or executive officers designated by the board of directors to receive notice.” (See, e.g. 12 C.F.R. 21.11 (h).) No such requirement exists in the Financial Crimes Enforcement Network’s (FinCEN) parallel SAR regulation.

ABA believes that this expectation imposes a role on directors and executive officers (that who not serve as an institution’s BSA officer) that is inconsistent with rational risk management responsibilities and compromises the board’s independence in evaluating management performance under the board approved BSA compliance program. The requirement diverts scarce board and executive resources from more significant strategic and policy oversight functions. At the same time, it adds further risk to information security issues without any concomitant benefit to the bank. Mandating notification of SAR filing to the board or executive level for all institutions is an unwarranted imposition on, and deleterious to, sound corporate governance.

- **Establish Standard for Suspending SARs on Continuing Activity**

There are many reasons that banks file continuing SARs when the underlying customer transaction activity is not considered inconsistent with reasonable banking behavior. For example, many institutions file SARs out of a literal interpretation of the structuring guidance and in an abundance of caution, when they have no conviction that the customer is engaging in activity that constitutes money laundering.

Accordingly, ABA proposes that when an institution would otherwise file serial SARs on repeatedly similar customer activity, they should be permitted by a clear regulatory interpretation to suspend further SAR filing when: an original and two additional SARs report continuing similar activity by the same customer have been filed; law enforcement has not requested the continued reporting of the identified activity; and when no substantively different conduct alters the nature, significance or criminality of the repeated activity, or merits a SAR identifying the activity as a different type or involving perpetrators not previously identified.

- **Include FFIEC Exam Instruction to Invoke FinCEN Helpline**

ABA considers the FinCEN Helpline to be a valuable source of BSA interpretive guidance. Many bank representatives and agency examiners utilize this service to obtain staff analysis to assist in evaluating compliance issues. This option has helped many bankers and examiners resolve their disagreements about BSA regulatory applications arising during an exam. However, other examiners resist using this resource when their interpretations are challenged by management.

ABA proposes that the FFIEC agencies include in their uniform exam procedures the following mandatory instruction to expedite exam dispute resolution without requiring a banking agency to compromise its supervisory judgment: “Whenever management submits a written rebuttal to an examiner’s BSA exception pertaining to 31 CFR Part 103 and includes therein a request to call the FinCEN Helpline, the examiner shall then call the FinCEN Helpline and, in the presence of the institution BSA Officer, obtain a FinCEN staff advisory interpretation of the issue. If the advisory interpretation does not alter the examiner’s judgment with respect to the exception, the FinCEN interpretation is to be recorded on the exception sheet along with any supplemental management position after the BSA Officer has heard the FinCEN interpretation.”

- **Include FFIEC Exam Instruction on Conducting Transaction Analysis**

Despite agency requirements for a tailored risk-based BSA compliance program and mandatory testing of bank BSA controls, agencies request transaction files and conduct transaction analyses without finding fault with the bank’s audit/testing of the same processes. This is not an appropriate use of resources by agencies and is unduly burdensome for banks.

The FFIEC should adopt the following uniform BSA exam instruction:

“Examiners should not request a bank to assemble files or records for the purpose of conducting transaction testing, or engage in transaction testing, of any provision of a bank’s BSA compliance program before evaluating the adequacy of the bank’s audit or independent testing of the relevant program provision and concluding either (i) that the audit/independent testing is demonstrably not a reliable indicator of bank performance of the program provision

being examined, or (ii) that deficiencies identified by bank audit or independent testing of the program provision have not been timely corrected.”

b. Sarbanes-Oxley Implementation

- **Oversight Critical**

We are encouraged that the Public Company Accounting Oversight Board (PCAOB) has issued new guidance to clarify and streamline the internal control reporting process required by Section 404. We also appreciate SEC Chairman Donaldson’s leadership in hosting an all-day roundtable discussion about ways to improve the Section 404 implementation process. These two events helped address areas that are in dire need of attention. We hope the PCAOB’s action will lead to remedying accounting firms’ very strict interpretation of 404, which has resulted in exorbitant auditing costs. We believe that streamlining, including increasing the number of shareholders for registration purposes, can be done through regulatory processes with Congress’s support. Going forward, it will be necessary to oversee whether accounting firms will recognize and respect the intent of the new PCAOB guidance. Oversight is critical to facilitating these changes.

- **Exemption for Small Depository Institutions**

We have asked the FDIC to exempt depository institutions with \$1 billion or less in assets from the management reporting requirement (and the audit and attestation of that report) and independent membership (other than the chairman) of the audit subcommittee. Today, institutions of less than \$1 billion represent only 14 percent of total industry assets. These standards have imposed serious burdens on the smaller institutions that

frequently result in duplication of these banks' internal audits and are not necessary to safe and sound operation of institutions of less than \$1 billion.

The previous threshold, established by the FDIC in 1993, of \$500 million is not appropriate today given the state of the industry. At the time the threshold was set, banks under \$500 million represented 25 percent of total industry assets. The makeup of the industry has changed considerably since then. While more than 1,200 new banks have been chartered since then, today under-\$500 million institutions represent only 10.2 percent of total industry assets. Moreover, in light of the structural changes which have taken place the widely-held definition of a community bank today is one with assets as large as \$1 billion or even more.

- **Increase Shareholder Threshold for Registration**

To ameliorate the burdens associated with registration under the Securities Exchange Act of 1934, which the SEC set in 1964, for companies with 500 or more shareholders, ABA proposes increasing the triggering shareholder threshold to a number between 1,500 and 3,000. This level would appropriately establish a registration threshold comparable in effect to the level enacted in 1964 in terms of market presence. That is to say it is the same market presence today that 500 shareholders would have occupied in 1964 would require six times the dollar investment, or six times the shareholders. Recent activities that by the SEC recognize that the cost of compliance with reporting requirements is relatively greater for smaller companies than for larger issuers. Yet new requirements have significantly increased the costs to small companies.

The SEC regulations also provide that a company cannot seek to de-register until the number of shareholders of record is below 300. Sections 12(g)(4) and 15(d) should be similarly updated to place the threshold for de-registration within the range of 900 to 1,800 shareholders of record.

c. Eliminate Cross-Marketing Restrictions

ABA supports elimination of the prohibition in the Gramm-Leach-Bliley Act on cross-marketing between banks and non-financial portfolio companies where the Financial Holding Company (FHC) that owns the bank also has an investment position in a non-financial portfolio company made through its securities affiliate. No such prohibition exists when the investment position in a portfolio company is made through an FHC's insurance affiliate.

d. Problems in the Consumer Protections on Bank Sales of Insurance Law

Section 47 of the Federal Deposit Insurance Act establishes certain protections for consumers who purchase insurance products from depository institutions. These protections include a disclosure that insurance products are not backed by the Federal Deposit Insurance Corporation, that such products may involve an investment risk, and that the purchase of an insurance product cannot be conditioned upon the approval of a loan. This disclosure is intended to distinguish insurance products from other banking products, especially insured deposit products.

Section 47, however, does not define the term "insurance product." As a result, the statute has been interpreted to apply to all types of insurance products, even insurance products for which the disclosure either is not necessary or is potentially confusing to the consumer. To address this

problem, we recommend modifying the scope of the disclosure requirement to only apply to products wherein there is an investment risk, e.g. not fixed rate annuities or credit insurance.

e. Control of Shares by Trusts

We propose a safe harbor from the attribution rules of Section 2(g) (2) of the Bank Holding Company Act: (1) for shares held in trust through a regulated employee benefit plan; or (2) for mutual fund shares held in trust provided any investment adviser or affiliate with the power to vote 25 percent of the shares of the investment company transfers the vote to the beneficial owners or an independent entity; or (3) for shares held in a common or collective fund.

The purpose of this safe harbor is to exempt certain bank and bank holding company employee investment holdings from being improperly attributed to the bank holding company when those holdings are held through an employee benefit plan or a common or collective fund, or the employee assets are invested in mutual fund shares held in trust. Without this exemption, bank holding companies, by virtue of their employees' activities, could be deemed to control the mutual fund or other company in which the plan or trust has invested.

f. Provide Parity for Savings Associations

ABA recommends eliminating disparate treatment of thrifts under the federal securities laws eliminating the investment adviser and broker-dealer registration requirements that apply to thrifts, but not banks, under the Investment Advisers Act (IAA) and the Securities Exchange Act of 1934.

Thrifts and banks provide investment adviser, trust and custody, third party brokerage, and other related services in the same manner, but have been subject to disparate requirements under the

SEC's interpretation of the securities laws. There is no logical basis to structure the regulatory oversight of thrifts and banks differently. Removing the disparity will reduce regulatory burden by providing cost savings to affected thrift institutions and enhance competition that will benefit consumers.

g. Flood Insurance Compliance Problems

The Flood Disaster Protection Act of 1973 should be amended to streamline and simplify flood insurance requirements; resolve compliance problems when the official flood map is more than 10 years old; increase the “small loan” exception (currently \$5,000) and allow adjustments for inflation on a regular basis; and to allow exceptions to flood insurance requirements for agricultural real estate where the value of most of the collateral is represented by land, not permanent structures.

In addition, the forced-placement rules should be changed to allow lenders to force-place flood insurance within 30 days (instead of the current 45 days) of notifying the borrower and mandatory civil monetary penalties should be eliminated when a regulator finds a pattern and practice of certain violations of the National Flood Insurance Program to provide regulators with greater flexibility to tailor their actions more closely to individual cases.

h. Clarify Citizenship of National Banks & Federal Savings Associations

The National Bank Act generally provides that national banks are “citizens” of the states in which they are “located.” However, the term “located” is not defined in statute, and the federal courts have not defined the term consistently. Since 1992, federal courts have disagreed about the meaning of “located,” resulting in national banks having multiple state citizenships. Additionally, to avoid inconsistent treatment of federally chartered financial institutions under the diversity statute, we

recommend a change in the Home Owners' Loan Act to consider that a federal savings and loan is a citizen in the state where its home office is located for federal court jurisdiction.

i. Establish Protections for Information Provided to Banking Agencies

ABA proposes amending the Federal Deposit Insurance Act to provide that when a depository institution submits information to a bank regulator as part of the supervisory process, the depository institution has not waived any privilege it may claim with respect to that information. Recent court decisions have created ambiguity about the privileged status of information provided to supervisors when outside of the narrow confines of the actual examination. However, the purpose of providing confidentiality for examiner information is to encourage open communication between the regulator and the regulated financial institution. The process of preserving safety and soundness applies just as clearly to additional information supplied to regulators in any part of the supervisory process. The bank agencies have supported the change and we urge Congress to adopt these important protections for bank customers.