THE MORNING CALL

Community banks call bill rolling back some Dodd-Frank rules 'relief for Main Street'

Andrew Wagaman

May 23, 2018

Community bankers breathed a sigh of relief after President Donald J. Trump signed a bill Thursday that rolls back some regulatory requirements imposed following the 2008 financial crisis.

The bill, which the House on Tuesday approved with considerable bipartisan support, avoids altering the Dodd-Frank law's most fundamental checks on Wall Street's largest banks, such as J.P. Morgan Chase and Bank of America. Instead, it focuses on re-writing regulations for smaller, less complex financial institutions whose failure would not pose an existential threat to the financial system.

"You can't compare Neffs National Bank, with our $350 million in assets, to $2 trillion Wells Fargo," said Neffs CEO Kevin Schmidt. "Dodd-Frank was intended to punish the too-big-to-fail banks, but its regulations got pushed down onto community banks, and that doesn't make sense."

Proponents say the new regulatory regime will provide customers of these smaller banks with more affordable access to credit, especially via mortgage loaning, and will give these banks more flexibility to base investment strategy on their local knowledge.

Nick DeFrancesco, president of the Pennsylvania Association of Community Bankers, argues post-crisis regulations stifled innovation and left many counties in the state without even one chartered bank headquartered there. Schuylkill County, for example, saw all four of its county-based banks get acquired over a two-year period, he said.

Whereas more than 100 new banks were chartered each year leading up to the crisis, only three opened from 2010 through 2015. During that same time period, about one-third closed or merged, according to data from the Federal Deposit Insurance Corp. Meanwhile, just one savings institution has been chartered since 2010.

This has ostensibly left rural consumers and lower-income urban consumers with little access to the "intimate," relationship-anchored banking that DeFrancesco says community institutions provide.

The bill passed Tuesday reduces capital rules for banks with less than $10 billion in assets, which cuts down on compliance and record-keeping costs. That covers even the larger

community banks in the region — Embassy Bank of the Lehigh Valley, for example, has about $1 billion in assets.

The bill also exempts most of those banks from the complicated "Volcker rule" trading restrictions that have created further compliance headaches disproportionate to the amount of trading these banks actually do, proponents say.

And it no longer requires banks that make fewer than 1,000 first-lien mortgages annually to maintain escrow accounts for higher-priced (typically riskier) mortgage loans. Escrow, or impound, accounts allow banks to ensure property-related expenses such as taxes and insurance are paid, but community lenders say they're costly and impractical.

This exemption will reduce banks' overhead and give some consumers more opportunity to borrow at affordable rates, said Embassy Bank CEO Dave Lobach.

"I believe in regulation, but it needs to be smart," he said. "We have a limited amount of human resources, so we want to invest our time in those things that matter to consumers and investors. If you're spending time on things that merely increase overhead and paperwork for both consumers and bankers, then you're not utilizing your time in the best way."

Critics are skeptical of the idea that excessive regulation has stifled growth. The FDIC reported Tuesday that U.S. banks' net income for the first three months of 2018 ncreased 27.5 percent year-over-year, though that was bolstered by corporate tax cuts late last year.

The bill's most notable, and arguably most contentious, change is raising the threshold at which banks are considered systemically risky and subject to expensive "stress tests" to $250 billion from $50 billion. Critics worry super-regional banks like BB&T Corp., which has about $220 billion in assets, will be subject to too litte oversight. BB&T acquired the largest Lehigh Valley-based bank, National Penn Bancshares, in 2016.

David White, a spokesman for BB&T, downplayed the bill's effect on the bank. BB&T is already managing its company as if it's beyond the $250 billion asset level, he said Thursday.

"But rather than an arbitrary asset threshold, BB&T and other financial institutions have supported a risk-based approach based on multiple factors such as complexity and interconnectedness," he said. "If the analysis of a financial institution indicates greater risk, then it makes sense to increase the regulatory scrutiny on that institution. Regardless of size, regional banks like BB&T are traditional lending institutions that provide little or no systemic risk."

U.S. Rep. Matt Cartwright, a Democrat whose district includes Easton and parts of Northampton County, voted against the bill. While he says he supports reducing "burdensome" regulations on small community banks and credit unions, he rejects exemptions for banks in the $100 billion to $250 billion range that he believes partook in the "bad conduct that nearly tanked the American economy ten years ago."

"While there were provisions in the bill I support, I simply cannot vote in favor of legislation that risks taking us a step closer to problems that led to our country's worst economic disaster since the Great Depression," he said in a statement.

Dodd-Frank hurt communities by hampering the mid-sized financial institutions best equipped to do community reinvestment work, said Alan Jennings, executive director of the Community Action Committee of the Lehigh Valley.

A bank like National Penn, which was nearing $10 billion in assets, was "essentially forced to be sold" because of the new regulations. While BB&T still pays attention to the market, he said, National Penn was an example of a bank "not too big to have forgotten where they came from." Jennings believes the new legislation will prevent larger banks from swallowing up the remaining banks in the $5 billion to $35 billion range.

Others believe consolidation will accelerate because banks approaching $50 billion in assets can now grow without being subjected to the Federal Reserve's stress tests. They'll look to expand into new communities by buying small community institutions.

That's not necessarily a bad thing, says Diego Zuluaga, a policy analyst at the Cato Institute's Center for Monetary and Financial Alternatives. Financial institutions with less than $500 million in assets are struggling to break a profit not only because of regulation, but also due to persistently low interest rates and the cost of adopting the latest technology related to online and mobile banking, he said.

"Some of these banks are uncompetitive for market reasons, not just regulatory reasons," Zuluaga said. "It's important to make competition work, and that involves allowing uncompetitive players to be driven out of business."

Competition also requires low barriers of entry for new banks, and more reform is needed on that front, Zuluaga said. FDIC rules for new banks aim to ensure most don't fail within a year or two of opening, but mandated business plans and capital requirements also having a chilling effect on prospective entrepreneurs.

"Most dynamic sectors have a lot of churn," he noted.