TESTIMONY OF

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ON

S. 650, THE ECONOMIC GROWTH AND REGULATORY
PAPERWORK REDUCTION ACT OF 1995

BEFORE THE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND REGULATORY RELIEF
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

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ROOM 216 HART SENATE OFFICE BUILDING

INTRODUCTION

Mr. Chairman and members of the Subcommittee, I am pleased to present the views of the Federal Deposit Insurance Corporation on S. 650, the Economic Growth and Regulatory Paperwork Reduction Act of 1995, and related issues. I enthusiastically support the purposes of the bill and, with a few exceptions, am pleased to endorse the specific changes in the law.

Over the past 25 years, a variety of new laws and regulations affecting banks in the areas of safety and soundness, crime detection, and consumer protection have been imposed on financial institutions. While these laws were enacted to protect consumers and the deposit insurance funds, the cumulative effect has imposed significant additional costs on the financial transactions that are essential to sustain a vital and competitive economy. At times, the burden falls disproportionately on insured banks and thrifts, as compared with other types of financial institutions, resulting in significant competitive disadvantages. In addition, regulatory burden generally has a disproportionate affect on smaller institutions. One-quarter of the banks supervised by the FDIC have fewer than 13 employees on a full-time basis, a small number to deal with the complexity and sheer volume of regulatory and legislative requirements.

To begin my testimony today I will share with you the results of an informal survey of banks conducted by the FDIC on the potential savings that might be associated with the repeal or modification of specific legislative or regulatory requirements. Second, I will comment on the legislation introduced by Chairman Shelby, S. 650, the Economic Growth and Regulatory Paperwork Reduction Act of 1995. Next, I will review current efforts of the FDIC to alleviate regulatory burden in the safety and soundness and consumer compliance areas -- some commenced at our own initiative, others with the impetus of legislation. Finally, I will propose additional statutory changes to further reduce regulatory burden on insured institutions.

FDIC SURVEY OF THE COSTS OF SPECIFIC REGULATORY BURDENS

Regulatory burden came into being through accretion. Each law and related regulation may be only marginally burdensome, but taken together their cumulative effect has become greatly burdensome.

In accordance with section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994, I have initiated a complete review of the agency's regulations and policy statements in an effort to identify those that have become obsolete or those for which the cost to comply substantially outweighs the intended benefits. I want to commend Congress for examining the level of burden imposed by statute. Working through laws and regulations developed over many years will require time, effort, and considerable attention, but it can and should be done. The challenge for Congress and the regulators is to identify those laws and regulations that may be modified, streamlined or eliminated without adversely affecting the safety and soundness of the banking industry or necessary protections for consumers. To accomplish this task, we must test regulations against specific criteria: 1) whether the regulations are necessary to ensure a safe and sound banking system, 2) whether the regulations enhance the functioning of the marketplace, or 3) whether the regulations can be justified on strong public policy grounds related to consumer protection.

Within the past month we conducted an informal survey of just over 60 institutions that the FDIC supervises in order to gauge the potential cost savings from the elimination of specific legislative requirements and regulations currently on the books. The items included in the survey were based on provisions of S. 650 that we support and believe would result in identifiable savings. The regulatory and legislative requirements surveyed included: Truth in Lending and Truth in Savings disclosures, loan data collection and reporting, auditor attestation requirements for bank compliance with laws and regulations, as well as the costs of various applications and notifications.

A broad cross-section of institutions by size and location provided dollar estimates of their costs in meeting 15 very specific regulatory requirements.

While the survey was informal -- and, therefore, cannot be used to make industry-wide estimates -- we believe the results support two general conclusions. First smaller institutions bear higher proportionate costs than larger ones. When measured in relation to net income, the estimated costs incurred from the 15 requirements surveyed ranged from over 16 percent at very small institutions to just over one percent at the largest.

Second, the responses clearly suggest that positive cost savings could be achieved if the surveyed requirements were eliminated. For all recurring requirements included in the questionnaire, the median cost of compliance per bank was reported to be approximately $40,000 per year. In addition, respondents reported that the median cost estimate of submitting various non-recurring applications and notifications ranged from $500 to $20,000 per action.

Taken together, we estimate that the savings from completely eliminating all requirements covered in the survey could increase the annual rate of return on assets from 5 to 10 basis points on a pre-tax basis for institutions the FDIC supervises. The results of this survey are discussed in greater detail in

Appendix A to this testimony. The FDIC also is pursuing other specific efforts to reduce regulatory burden, which are discussed at the conclusion of the testimony.

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The bank and thrift regulatory agencies can and should pursue efforts to reduce regulatory burden within their existing authority, but we must recognize that a substantial share of the burden on depository institutions derives directly from statutes that are beyond the jurisdiction of the agencies to change. In this regard, it is incumbent on the agencies to monitor the effectiveness and impact of applicable statutes and to make appropriate recommendations to Congress for changes in those statutes to reduce unnecessary burden and improve effectiveness. Included in this testimony, and set out in detail in Appendix B, are the FDIC's suggestions on provisions of law that can and should be amended or eliminated because they do not conform to any of the three criteria set out at the beginning of this testimony.

I also want to commend you Mr. Chairman, Senator Mack and this Subcommittee for your considerable efforts at dealing with regulatory burden. S. 650, the Economic Growth and Regulatory

Paperwork Reduction Act of 1995 is a strong attempt to address these issues.

In reviewing S. 650, as you have requested, we have identified provisions that we support as drafted, those we support but with some modification, and those few that we do not favor. FDIC staff recently provided the Subcommittee staff with technical suggestions on the bill.

Truth in Lending

The Truth in Lending Act ("TILA") was enacted 27 years ago to enable consumers to shop comparatively for credit by requiring lenders to disclose interest rates and other information about credit terms and costs in a uniform way. TILA, as implemented by Regulation Z, has been largely successful in providing bank customers with comparable information on interest rates applicable to credit that enhances the effective functioning of the marketplace. It also has been successful at remedying many of the deceptive and misleading lending practices it was enacted to correct. Unfortunately, Regulation Z, has become substantially more complicated, as it has been adapted to fit the variety of loan products introduced since 1968. Hence, the real value of TILA to the efficient functioning of the marketplace and to consumers has been obscured because of the complexity of the required disclosures.

The complexity of TILA can be demonstrated in a variety of ways. First, the Federal Reserve Board's Official Staff Commentary on Regulation Z, which provides official interpretations, is longer than the regulation itself.

Second, the complexity of Regulation Z is such that the FDIC cited more than 2,700 of the 3,500 institutions we examined in 1994 for at least one violation. The majority of these violations were technical rather than substantive in nature, however, and were most often the result of recording errors rather than material misrepresentations to consumers that would require reimbursement. As a result, the FDIC asked only 279 of the 2,700 institutions cited for violations in 1994 to reimburse a total of $2.8 million to customers based upon violations cited under Regulation Z.

Third, the banks that responded to our survey indicated that TILA is a relatively costly law to comply with on an annual basis. Specifically, the median reported dollar cost of $10,000 to comply with TILA was almost twice as high as for any other survey item. Clearly, Regulation Z is overdue for major revision.

The FDIC is supportive of the revisions to TILA prescribed by S. 650. We believe the Federal Reserve Board should have the flexibility to streamline or eliminate any TILA disclosures that do not provide appreciable benefits to consumers. We also believe that the Federal Reserve Board should have the authority to exempt certain transactions from these requirements. In addition, the Federal Reserve Board should review the application of the right of rescission and consider exempting certain transactions from these provisions where appropriate. Finally, we are supportive of those provisions which would modify TILA as a result of the Rodash decision.

The FDIC supports the changes to the Real Estate Settlement Procedures Act ("RESPA") and TILA prescribed by sections 101, 102 and 104 of S. 650. We believe that granting the Federal Reserve Board the authority to conform TILA with RESPA, where possible, will reduce regulatory burden for financial institutions and avoid confusion and complexity for consumers.

Consumers today rarely rescind credit transactions with insured financial institutions. In fact, many consumers complain that the inability to waive their right of rescission is inconvenient and costly since it delays the disbursement of funds. Therefore, the FDIC supports exempting all refinancing and consolidations of credit secured by first liens from the right of rescission as contained in section 114 of S. 650. These transactions would continue to be subject to early "good faith estimate" disclosures required by RESPA, so consumers would continue to have the opportunity to evaluate the implications of their actions.

In addition, the FDIC supports granting the Federal Reserve Board the flexibility to expand the ability of consumers to waive their right to rescind transactions beyond those circumstances constituting "personal financial emergencies," as captured in section 119 of the legislation. The Federal Reserve Board would have the ability to determine how such a waiver would be administered, and through the rulemaking process public comment could be solicited.

The FDIC has no objection to section 115 of the bill which replaces the current $5 or $10 tolerance level for finance charges prescribed by Regulation Z in 1981, with a statutory tolerance level of $100. We believe it is reasonable to allow a higher tolerance level than Regulation Z currently provides for closed-end credit secured by real estate, as these transactions are typically large dollar transactions. This provision would provide greater flexibility to institutions without substantially changing the practical level of protection afforded to the consumer.

The Community Reinvestment Act of 1977

In July of 1993, President Clinton asked the federal bank regulatory agencies to undertake sweeping reform of the Community Reinvestment Act ("CRA") regulations to reduce unnecessary regulatory burden and focus the CRA examination program on more objective, performance-based assessment standards. For the past 22 months, the agencies have worked jointly to produce comprehensive reform of the CRA regulations. To initiate the process, the agencies held hearings in seven locations across the country during 1993, and heard from hundreds of witnesses including representatives from financial institutions, the business community, consumer and community groups, and state and local government officials. Proposed regulations were circulated twice for public comment, which together produced almost 14,000 letters. From this outpouring of public comment, the agencies developed a final CRA rule, which was approved by each agency in April.

The FDIC believes the new CRA rule accomplishes the goals established at the outset, particularly in the area of reducing regulatory burden. The new CRA rule provides for an effective and meaningful evaluation of the performance of an institution without burdensome paperwork and recordkeeping requirements and without undue reliance on ratios and formulas. In keeping with the original intent of the CRA, the new rule encourages institutions to meet the credit needs of their community, consistent with safety and soundness.

First, the new CRA rule emphasizes performance in lending, investment and service, rather than process and paperwork, and provides institutions with considerable flexibility in meeting the credit needs of their communities. The new rule eliminates the requirement that institutions prepare CRA statements, review them annually and document them in the minutes of the board of directors' meetings. Institutions are no longer required to justify the basis for community delineations or to document efforts in marketing or ascertaining community credit needs. Resources formerly devoted to such procedural requirements -- time, money and personnel -- are now available for making loans and investments and providing services in the community.

Second, the new CRA rule distinguishes between large and small institutions by providing a streamlined examination process and exemption from data collection on loans to small business and small farms for independent banks and thrifts with assets under $250 million, or banks and thrifts with assets under $250 million that are members of a holding company with total assets under $1 billion. Under the streamlined examination procedure, regulators will determine whether an institution's loan-to-deposit ratio and lending record are reasonable relative to its size, financial condition and management expertise, and the credit needs of its community. The streamlined examination provides meaningful relief to 81 percent of the banking industry.

All institutions, regardless of size, have the option of being evaluated on the basis of a strategic plan rather than on lending, service and investment tests. A strategic plan is required to specify measurable goals, and to be aired in advance of adoption for public comment. After the comments have been addressed, the institution must submit the plan for agency review. Thereafter, the institution will be evaluated based upon how well it meets or exceeds the goals it has established for itself in the strategic plan. This approach encourages greater management involvement in an institution's effort to meet the credit needs of its community while reducing the regulatory burden of the institution for compliance with CRA.

The FDIC believes the new CRA regulation provides meaningful relief in the area of regulatory burden, particularly for small banks. The streamlined examination and the focus on lending rather than creating a paper trail, as well as the reduced reporting requirements when compared with the previously proposed regulations, will reduce substantially the burden CRA previously placed on small and large institutions alike.

S. 650 contains some provisions that overlap with changes already made by the new CRA rule. For example, section 133 of

S. 650 contains a provision requiring the agencies to publish the list of institutions to be examined. This is required by the new CRA rule. In addition, the agencies currently publish a list of the CRA ratings of the institutions we examine. Section 134 of the bill addresses special purpose banks. Under the new CRA rule, wholesale and limited purpose banks may request approval to be assessed under a Community Development Test emphasizing community development lending and investment performance.

The FDIC is concerned that some provisions of S. 650 would effectively preempt the positive changes in the new CRA rule. First, we urge the committee to reconsider the need to include the "small bank exemption" provision in section 132 of the bill. The FDIC firmly believes that the new CRA rule substantially reduces the compliance burden for small banks. Periodic examinations are an effective way to ensure that insured institutions are providing credit and service in their communities. The new streamlined examination methods are designed specifically to provide maximum flexibility for institutions and to ensure consistency in evaluation criteria, while reducing the burden of compliance on small institutions.

Second, from the FDIC's perspective, the safe harbor created by section 133 of S. 650 is not necessary at this time. First, the FDIC rarely receives CRA protests. Of the 2,749 applications subject to CRA on which the FDIC took action in 1994, only eight were protested on CRA grounds.

In addition, when the FDIC considers an application from a state-chartered institution, we must consider a variety of factors prescribed by the Federal Deposit Insurance Act. These statutory factors include, but are not limited to, the financial history and condition of the institution and the convenience and needs of the community to be served. Although the CRA rating of an institution is important in this process, particularly in assessing the degree to which the institution is serving the convenience and needs of the community, it is not conclusive.

We urge the Subcommittee to allow the agencies to implement the new rule and to evaluate its effectiveness in reducing regulatory burden before instituting further changes to the CRA, such as a small bank exemption and a safe harbor. The new CRA rule should be given an opportunity to demonstrate that it does what the agencies intend -- allow banks, large and small alike, to focus on lending, not on paperwork. If we have an effective regulation, there will be more confidence in the CRA ratings and less reason for protest.

The FDIC has some concern with two other sections of S. 650. Sections 131 and 231 of the bill would insert similar language prohibiting the agencies from imposing recordkeeping and/or reporting requirements on institutions unless the requirements would lessen regulatory burden. The FDIC is concerned that such a provision could be interpreted as limiting our ability to have access to loan data in the course of an examination. Such limitations would critically impair our ability to conduct a meaningful examination. We recommend clarifying these provisions in a way that ensures that the agencies' access to relevant lending data during the examination process is not called into question.

Section 231 of S. 650 would prohibit agencies from requiring institutions to collect and report loan data under the CRA. Our new CRA regulation imposes some additional data collection and reporting requirements on large banks. This is balanced, however, by the usefulness of the information collected. The data, which will be collected on small business and small farm loans, will give a more comprehensive view of how the reporting institutions are meeting the credit needs of their communities.

HMDA data alone presents an incomplete view of a bank's lending, since it only focuses on mortgage lending. The small business and small farm loan data will help to complete the picture of how an institution meets the credit needs of its community. This will benefit many institutions that are not given full credit today in their CRA ratings for the entire scope of their lending efforts. To limit burden, the data collection requirements for large banks are streamlined, and do not require loan-by-loan reporting. Instead, information will be collected by census tract and will be reported in the aggregate by the agencies, not by the banks. Once again, we urge the Subcommittee to reconsider the aspects of S. 650 that would affect efforts to implement the new CRA regulation. The final regulation is greatly improved over the current regulation, as well as the two prior CRA proposals, in terms of the level of burden on financial institutions. The FDIC believes everyone will benefit from full implementation of the CRA reforms.

Truth in Savings

The Truth in Savings Act ("TISA") requires institutions to provide accurate and uniform disclosures and terms of advertising to enable consumers to shop comparatively for financial savings products. While TISA provides the consumer with some valuable information, Regulation DD is overly complicated. S. 650 would substantially streamline TISA. Institutions would only be required to disclose the method they use to calculate the interest rate.

While the FDIC supports reducing the complexity and regulatory burden imposed by TISA, we caution the Subcommittee that such a sweeping amendment would eliminate some of the initial disclosures that provide meaningful assistance to bank customers in their effort to comparison shop for deposit products. For example, institutions would not be compelled to disclose minimum balance requirements, service charges or penalties for early withdrawal of funds. While it would seem logical for banks to disclose this information to their customers as a matter of good business, it was the lack of such disclosures that in large part prompted the enactment of TISA. We recommend that the Subcommittee consider legislation that directs the Federal Reserve Board to review Regulation DD and revise those specific sections that do not enhance the ability of consumers to make informed decisions about deposit accounts and products.

Streamlining Government Regulation

Examinations. Section 221 would extend the maximum permissible examination cycle for certain small institutions from 12 or 18 months to 24 months. We believe extending the examination cycle in this manner would tend to establish 24 months as the norm for the time between examinations, which we believe would not be prudent. It was the FDIC's experience in the mid-1980s, that examination cycles were stretched out for smaller institutions on the theory that they did not present systemic risk problems. In fact, serious problems developed in the interim and those problems went undetected for some time. In some cases, they ultimately caused significant losses to the deposit insurance funds. Although we are in a relatively stable period at the moment, it also has been our experience that conditions in the industry can deteriorate rather quickly, especially in the highly competitive and rapidly changing environment of today. Moreover, the regulators are most effective when the examination process is used to encourage sound banking practices and strong management and to observe the philosophy and practices of management and the changes that occur over time between examinations. We believe examinations every two years may not be frequent enough for those purposes.

At the same time, we are mindful of the need to reduce supervisory regulatory burden, especially on smaller, well-capitalized and well-managed institutions. We believe this is best accomplished, however, by streamlining the process, increasing offsite monitoring to reduce onsite examination time, and staffing the examination with no more examiners than needed in order to keep to the necessary minimum demands on the resources of the institution and its management.

It is true that bankers are concerned about the burden of examinations. The FDIC recently began surveying bankers for suggestions on ways to improve the quality and effectiveness of safety and soundness examinations. The effort, which is expected to run for one year, is aimed at detecting and changing aspects of the examination process that are ineffective or inefficient. Over the next year, approximately 3,500 FDIC-supervised commercial banks and savings banks are expected to undergo safety and soundness examinations. At the end of these examinations, the institutions will be given a three-page survey that asks questions about the appropriateness and thoroughness of examination procedures; the quality and professionalism of the FDIC team that conducted the review; and the usefulness of the written and oral reports from the FDIC regarding examination findings. Respondents will have the option to remain anonymous or to give their names so that the FDIC can seek follow-up information or clarifications. Participants also will be able to speak with a senior management official of the FDIC to discuss any additional problems or issues.

We also are asking our banks if they prefer having safety and soundness examinations conducted concurrently with or at different times than compliance examinations. Concurrent examinations may not be practical for all institutions, as space constraints and personnel resources may be insufficient to facilitate simultaneous examinations. The FDIC recognizes that an examination can be disruptive to the normal business of a bank, particularly for smaller institutions and we are making an effort to develop examination schedules that will accommodate the preferences expressed by banks with respect to concurrent or separate examinations whenever practical.

While it is too early in the survey process to provide even preliminary results, we expect that the program will provide a valuable source of information on how the FDIC can minimize the regulatory burden on banks while, at the same time, improving the effectiveness and quality of our safety and soundness examination program.

As a result of these efforts, we urge the Subcommittee to reconsider the need and justification for extending the examination cycle beyond 18 months. We also note parenthetically that many states follow a 12- or 18-month examination cycle so that FDIC coordination with state examinations can more readily be maintained if an 18-month examination cycle is retained.

Applications. With respect to section 204(c) of the bill, the FDIC supports the elimination of prior approval for the establishment of a domestic branch by institutions that operate safely and soundly. Today, the establishment or relocation of a branch is not the major business decision it once was. The bank regulatory agencies have other sufficient enforcement tools to stop unsafe or unsound expansion.

In 1994, the FDIC approved over 1,200 applications to establish or relocate a branch, including three that were protested on CRA grounds. None of the three were denied. Given this record, there is simply no justification on either safety and soundness or community service grounds for continuing to require institutions to endure the costs and delays, however short, that are associated with the preparation and processing of applications for prior approval to establish a branch.

In addition, we suggest that the scope of section 204(c) be broadened to include applications to relocate a branch as well as to establish a branch. As a corollary, we suggest that institutions only be required to give the FDIC or their primary federal regulator a simple notice of the location of the new or relocated branch. It is necessary for the regulators to know the location of all branches in order to schedule examinations and to prepare for emergencies.

The FDIC also supports section 207 of the bill, which would exclude automated teller machines and remote service facilities from the definition of "domestic branch." Remote service facility is defined as an automated teller machine, cash dispensing machine, point-of-sale terminal, or other remote electronic facility where deposits are received, checks paid or money lent. We do not see a compelling reason for an agency to approve these facilities in advance or even to have prior notice of their establishment. It is time for the statutes to catch-up to changed technology. The FDIC approved over 700 of these facilities in 1994 and volume will likely pick up in the future.

Eliminating the prior approval requirement will significantly reduce burden for the industry and the agency.

Reporting Requirements and Certain Exemptions. The FDIC supports section 210 of the bill, which would revise section 32 of the FDI Act to eliminate notice requirements in certain cases involving a new member of a bank's board of directors or senior executive officer. The FDIC regards the existing requirements as unnecessary impediments to the routine management of depository institutions. It is entirely appropriate that, as revised, the prior notice requirement is confined to institutions that are either undercapitalized or otherwise in a troubled condition.

Section 212 of the proposal would liberalize the requirements governing insider lending. We support the creation of an exemption for extensions of credit available to a wide group of employees. Similarly, we support eliminating reporting requirements related to loans that executive officers receive from other banks that exceed limits available at their own bank, as well as the requirement that corporate quarterly reports include information on loans to officers. We would go further, however, by amending section 22(g) of the Federal Reserve Act to allow home equity loans of up to $100,000 and loans secured by readily marketable assets. In addition, we suggest amending section 22(g)(4) of the Federal Reserve Act, which requires each agency to promulgate separate regulations to provide for additional exceptions to the "other loans" category. A uniform Federal Reserve regulation would suffice.

Finally, we fully support the branch closure provisions of section 214 of the bill. These provisions substantially mirror the federal regulators' interagency policy statement on branch closings and would reduce regulatory burden by eliminating the need to give prior notice of decisions to close remote service facilities, same neighborhood relocations, and certain branches acquired through mergers.

Elimination of Appraisal Subcommittee. Section 213 of the bill would abolish the Appraisal Subcommittee and transfer certain of its functions to the Federal Financial Institutions Examination Council. We fully support this approach. There is no justification for a separate semi-autonomous Appraisal Subcommittee. We suggest that the language make clear that the Subcommittee would be obligated to return funds to the Treasury only after it has wound-up its affairs in an orderly manner and has satisfied its obligations and commitments to creditors and others, including the current grant to the Appraisal Foundation.

Regulatory Burden Review. The FDIC supports section 223 of the bill, which would require a review of all agency regulations no less frequently than every 10 years. Such a review is entirely appropriate. Indeed, it will be the FDIC's policy to review regulations as often as every five years to assure that they continue to serve the intended purposes effectively and efficiently without undue burden to financial institutions. We hope that the Subcommittee would clarify the intent of section 223(e) with respect to the role of the Federal Financial Institutions Examination Council (FFIEC) in the procedure in order to assure that the process of regulatory review is not unintentionally encumbered or slowed. The FFIEC can serve an important function by providing interagency coordination and consistency in the efforts of bank regulators to reduce regulatory burden, as long as the efficiency of its involvement is assured.

The FDIC supports section 235 of S. 650, which would repeal call report requirements for small business and small farm loans. The CRA regulatory reform effort has considered those reporting requirements extensively and has required reporting by larger institutions for CRA purposes. There is no reason to maintain duplicative reporting requirements.

<u>Home Mortgage Disclosure Act</u>

Section 236 of S. 650 amends the Home Mortgage Disclosure Act ("HMDA") by increasing from $10 million to $50 million in assets the size of institutions that are exempt from reporting. This section also provides the Federal Reserve Board with the authority to exempt institutions if it determines that the compliance burden outweighs the usefulness of the data required to be disclosed.

The FDIC supports this provision, as it would substantially reduce regulatory burden on small banks, without significantly reducing the level of data reported on residential lending. Currently, 3,187 FDIC-supervised banks are required to report under HMDA. Raising the reporting threshold to $50 million would exempt 33 percent of these reporters, but would result in a total reduction in the level of data reported by FDIC-supervised institutions by only 6 percent. The resulting cost savings to smaller individual institutions, however, would be material.

We also support section 236(b) of the bill that relieves the burden associated with having HMDA data available at each branch location. The public will still have the ability to access the data. Institutions would be required to provide notice at their branch locations that the information is available for review at the institution's home office, or the data will be provided directly to members of the public requesting it either in paper or electronic format no later than 15 days after receipt of a written request.

FDIC Board Composition

Section 243 of the bill would add a State bank commissioner to the FDIC board. We support the concept of assuring state bank regulatory experience on the FDIC board. We do not support a six-member board for the FDIC where half of the board members would have primary responsibilities that do not involve the FDIC. It is our view that the FDIC's independence as guardian of the insurance funds can be assured more effectively if a clear majority of its board members have primary allegiance to, and responsibility for, the FDIC. This statement is not meant in any way to derogate from the strong sense of commitment that the Comptroller of the Currency and the Director of the Office of Thrift Supervision bring to their service on the FDIC board. It is instead meant to recognize that where a board member has substantial responsibilities for directing another agency, the FDIC by definition cannot have the director's primary attention. The FDIC is too important an agency and its responsibilities too significant for half of its board members to be so distracted. For that reason we urge that consideration be given to keeping the FDIC board at five persons, while designating that one of the seats be held by an individual with state bank regulatory experience. This would allow the board member to commit full-time to FDIC matters, which would not be possible if the board member were required to manage a state banking department at the same time, while still assuring state regulatory expertise on the FDIC board.

We believe that having such state bank supervisory experience on the FDIC board would complement our continuing strong efforts to coordinate supervisory activities with state banking departments. This effort has been a central theme of the FDIC's functions and activities for sixty-one years, and a particular interest of mine as FDIC Chairman.

Regulatory Impact on Cost of Credit and Credit Availability

We support the thrust of section 301 that removes the requirement that auditors of banks attest to the institution's compliance with designated laws and regulations and allows an exemption for minority membership on an institution's audit committee of insiders. However, we suggest that the provision calling for individual regulators to issue regulations on this exemption is unnecessarily burdensome and confusing, given the FDIC's current role in issuing audit regulations for all FDIC-insured institutions, after consultation with the other agencies.

Self-testing

The goal of fair lending laws is to ensure that the free flow of credit is not impaired by market distortions created by illegal discrimination on repugnant grounds, such as race, national origin, sex or age. The best way to ensure that this goal is met is by enlisting the help of all financial institutions in identifying and correcting illegal discriminatory behavior. Hence, the FDIC strongly supports the use of self-testing by financial institutions as the most comprehensive approach to assuring compliance with fair lending laws and to effecting corrective action that resolves any problems. This view is reflected in the recent decision of the Federal Reserve Board to propose amendments to Regulation B to permit financial institutions to request race, color, gender, religion and national origin from all applicants. We are pleased to see that this view is shared by the Subcommittee and reflected in S. 650. We offer the following comments for consideration.

First, section 302 provides institutions with certain protections to encourage their use of self-testing. To further encourage self-testing, the Subcommittee should consider expanding this provision to include language that would shelter an institution's self-testing results from discovery in the context of civil litigation. However, under the normal rules of discovery, if an institution elects to use the results of its self-testing in its defense, this protection would be waived. Second, section 302 of S. 650 prohibits the regulators from reviewing the self-testing report. We believe that institutions should have the option of sharing self-testing results with their regulators. We recommend, therefore, that the language be changed to allow regulators to review self-testing reports if the institution voluntarily provides the information to the agency.

Finally, we believe that the terms "test or review" are too broad to describe the type of information to which the agencies may not have access. We believe that such terms could be interpreted broadly to prevent the agencies from having access to the kind of internal review and audit materials necessary to conduct a normal compliance examination. Hence, we would suggest clarifying the language to avoid such consequences.

Due Process Protections

Section 311 of the bill would affect the FDIC in administrative proceedings when it is acting in its regulatory capacity, when it is acting as conservator or receiver, or in its corporate capacity as an assignee of assets of a receiver of a failed insured depository institution. The bill would apply a more stringent standard than currently applies to the FDIC when it seeks to obtain pre-judgement attachment of assets or other injunctive relief. Section 311 of the bill would require the FDIC to show immediate or irreparable injury as a condition for obtaining such relief.

We oppose this provision to the extent it would affect our roles as conservator, receiver, and corporate liquidator of a failed financial institution under section 11(d)(19) of the FDI Act. The authority to seek temporary injunctive relief in the form of asset freezes without having to show irreparable and immediate loss allows the FDIC, in appropriate cases, to move quickly to prevent fraudulent conveyances or concealment of assets. The statutory power provided under section 11(d)(19) is consistent with similar statutory injunctive provisions where Congress deems a type of action to merit relief from this common law requirement.

There are times, such as soon after a failure, when we urgently require an injunction to prevent dissipation of assets. On such occasions, we might not yet have sufficient information to satisfy the irreparable and immediate injury standard, and in some cases it can be difficult to establish irreparable harm when money damages, as opposed to land or some other unique asset, are at issue. Congress wanted special status to be applied to cases involving money damages when deposit insurance funds were at risk. Without that authority, the FDIC may be powerless to prevent dissipation of assets. A consequence could be that losses to the deposit insurance funds from bank failures would increase.

Further, the law as it stands does not deprive borrowers or other defendants, such as directors and officers of failed institutions, of due process protections. Under sections 8 and 11 of the FDI Act, the FDIC must still establish in court that an asset freeze is in the public interest, that the FDIC has a substantial likelihood of winning its case, and that the inconvenience to the defendant is outweighed by the potential harm to the FDIC as receiver or in another capacity. Moreover, the law in its present form, has a limited impact because it is temporary and does not determine ultimate entitlement. Assets are placed under court supervision, and defendants may still obtain money for legal expenses, or sell the assets for adequate consideration after obtaining prior court approval. Present law is intended to prevent parties from making fraudulent or abusive transfers or dissipation of assets until the FDIC's suit for collection can be heard by a court on the merits. Thus, the due process rights are fully protected.

THE FDIC's SPECIFIC BURDEN REDUCTION EFFORTS TO DATE

As discussed earlier, regulatory burden falls disproportionately on small institutions. In recent years, the FDIC has become sensitive to the issue of regulatory burden because state nonmember banks are typically small -- half have 25 or fewer employees; a third, 13 or fewer. We are continuing to review our regulations, policies, and procedures and seek to simplify or eliminate them where appropriate. In doing so, we have also recognized that the banks with the best examination ratings need a lighter regulatory hand than those that give us concern. I will highlight previous and ongoing efforts of the FDIC to identify and change areas where burden can be reduced without impairing regulation for safety and soundness purposes or necessary consumer protections.

Safety and Soundness Examinations

The FDIC has acted to minimize the burden of its safety and soundness examination program through careful allocation of resources, a simpler and better focused examination report format and an increased emphasis on coordination with other federal and state bank supervisors. For example, as permitted by statute, well-capitalized insured depository institutions below $250 million in total assets are subject to less frequent examinations -- if they are rated 1 under the CAMEL rating system, as are well-capitalized CAMEL 1- and 2- rated institutions with total assets of $100 million or less. To promote better consistency among examinations, the FDIC has adopted a Uniform Report of Examination form with the other Federal banking agencies.

To minimize the burden of duplicative and overlapping examinations, the FDIC coordinates its safety and soundness examinations with state banking authorities and in most cases alternates responsibility for examinations of CAMEL 1- and 2-rated institutions with state authorities. We also coordinate safety and soundness examinations of subsidiary banks of large multibank holding companies with other federal and state bank supervisors to eliminate overlap. We have also worked with the Federal Reserve Board and with state regulators to develop a coordinated and unified supervisory program for U.S. operations of foreign banking organizations.

In addition, the FDIC and other federal regulators recently reached an agreement with the National Association of Securities Dealers to coordinate the examination of broker-dealers affiliated with insured depository institutions operating on bank premises.

Compliance Examinations

The FDIC has also undertaken initiatives in the consumer compliance area to minimize and reduce the burden on banks. With the creation of a new Division of Compliance and Consumer Affairs in 1994, the FDIC began a comprehensive review of its compliance examination activities to identify specific areas for modification. To reduce the time and burden associated with onsite compliance examinations, we are streamlining the process by providing examiners with better analytical tools and computer software. For example, to reduce the time examiners spend onsite in banks conducting compliance examinations, the FDIC is expanding and enhancing its offsite pre-examination analysis. The use of specialized data integration software will enable examiners to perform a substantial amount of loan portfolio analysis at the field office, instead of in the bank.

In conjunction with our efforts to streamline the compliance examination function we will be surveying a cross-section of banks over the next month to solicit their views about how that process may be improved. The responses we receive will be compared with a survey conducted again in twelve months to enable us to measure the success of the modifications we are implementing in the compliance examination process.

To ensure a consistent application of the new CRA examination criteria, the agencies will be working together through the FFIEC to develop standardized procedures and to coordinate examiner training. Through this joint effort, we can ensure a well-executed implementation of the new regulation.

Regulation Review and Streamlining

As mentioned earlier, in accordance with section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994, the FDIC is undertaking a comprehensive review of its regulations and policy statements to streamline, eliminate or modify them where possible. The purpose of the review is to improve efficiency and reduce unnecessary costs, as well as to eliminate inconsistencies, and duplicative requirements. We have developed a schedule for an orderly review of the various regulations and policy statements and have targeted several for early attention. Where appropriate, we are working on an interagency basis to review comparable regulations and policies at all the agencies on a uniform basis. In this regard, we claim an early success in the new CRA regulation.

As I noted at the outset, through a broad range of other previous initiatives that parallel the goals of section 303, the FDIC has sought to change or modify existing regulations to reduce the regulatory burden on banks while improving the regulation of safety and soundness. The breath and scope of efforts is illustrated by the following examples of recent actions taken to reduce burdensome supervisory requirements:

- The FDIC has implemented pursuant to statute a prompt corrective action regimen under which well-capitalized and well-managed institutions are freed of prohibitions and restrictions otherwise applicable to under-capitalized institutions.

- Institutions with a CAMEL rating of 1 or 2, and that exceed $5 billion in total assets, are eligible for the holding company exception when complying with the FDIC's rules and regulations regarding annual audits. These institutions may now use the holding company's audit committee and submit holding company reports in order to satisfy the FDIC's requirements. Thus, such an institution is no longer required to have its own separate audit committee and need not file annual reports prepared at the institution level as previously had been required.

- The FDIC adopted a final rule clarifying regulatory capital treatment for net unrealized holding gains and losses on "available-for-sale" securities. Including unrealized gains and losses in regulatory capital could cause bank capital levels to be unnecessarily volatile, without appreciable benefit to the safety and soundness of the banking system. The FDIC's rule excludes most of these unrealized gains and losses from Tier 1 capital, thereby minimizing the possibility that temporary fluctuations in market interest rates could cause an institution to fall below its minimum capital requirements.

• The FDIC has acted to waive, under certain conditions, burdensome disclosure requirements related to a bank's commission on securities transactions for bank customers. This waiver eliminates a disparity in the rules for state nonmember banks in relation to other banks, which are not required to provide the disclosures. In addition, it alleviates the problem many banks faced in determining the amount of their fee in advance or immediately after a trade. The FDIC's new waiver authority conforms to authority the Federal Reserve Board and Comptroller of the Currency already have.

• Statutes requiring regulations on real estate lending, safety and soundness standards and external audits and attestations have been implemented with simple, short regulations and supplemented with less draconian supervisory guidelines.

• The FDIC recently withdrew a proposed rule on contracts that may be adverse to a bank's interests. We determined that potential abuses can be handled through normal supervision and existing authority and that it is therefore not necessary to implement additional regulations pursuant to section 30 of FDI Act.

• Banks rated satisfactory or better for CRA purposes have a streamlined and expedited application process when establishing or relocating an automated teller machine instead of filing a formal application and awaiting approval.

• The FDIC adopted a final rule reducing the amount of risk-based capital that FDIC-supervised banks must maintain for low-level recourse transactions. For risk-based capital purposes, when assets are transferred with recourse, capital normally must be held against the full outstanding amount of the transferred assets regardless of the level of recourse retained by the transferor. The final rule relieves banks of this excessive regulatory capital burden by limiting the amount of risk-based capital required to be held in low level recourse transactions to the maximum amount of loss possible under the recourse agreement.

• In 1992 the FDIC, under the auspices of the FFIEC, adopted a uniform policy concerning the frequency and timing of changes to the Report of Condition and Income (call reports) and similar reports filed by other depository institutions. Changes in regulatory reporting requirements impose a burden on institutions because they must make modifications to their recordkeeping and reporting system to accommodate the reporting changes. Limiting the frequency of changes and providing lead time between the announcement of the change and its effective date reduce regulatory burden. Under the interagency policy, changes in regulatory reporting requirements are to be announced prior to the start of the calendar year in which the revisions will take effect, thereby giving institutions at least 90 days advance notice.

• The FDIC Board adopted a formal appeals process on March 21, 1995, that provides FDIC-supervised institutions with an avenue to appeal material supervisory determinations including CAMEL, compliance and CRA ratings, the adequacy of loan loss reserve provisions and cited violations of law or regulation.

• The FDIC has adopted a new approach for collecting deposit insurance premiums. Effective April 1, 1995, for the semiannual assessment period beginning July 1, 1995, the assessment amount will be calculated by the FDIC rather than by each institution. This will improve the accuracy of the computations and relieve institutions of the burden of performing the calculations. Furthermore, assessments will be collected via direct debits initiated by the FDIC through automated clearing house processes which reduces paperwork for insured institutions.

Our efforts to identify areas for regulatory relief are ongoing and we continue to seek out opportunities to make further inroads into burden reduction.

ADDITIONAL REGULATORY RELIEF MEASURES

Appendix B provides a description of additional statutory changes that we believe would help to reduce regulatory burden. Our proposed amendments add to the efforts of the Subcommittee to reduce burden without compromising safety and soundness. For example, we recommend repealing section 39 of the FDI Act that requires federal banking agencies to prescribe operational and managerial standards for all insured depository institutions. The standards required by section 39 are widely viewed as unnecessary micromanagement of financial institutions.

Another recommendation, that is mentioned earlier in the testimony, is to amend section 22(g) of the Federal Reserve Act to expand the statutory exceptions to the restrictions on loans to executive officers to include home equity lines of credit. This amendment would provide flexibility in lending to executive officers without compromising safety and soundness.

We have provided language on these and additional suggestions for reducing burden in seven other areas to the Subcommittee staff and would be pleased to assist them further in regulatory and legislative relief efforts.

CONCLUSION

Let me again state that we are encouraged that Congress is committed to reducing regulatory burden. The FDIC too is engaged in an intensive effort to identify regulations and policies that may be modified, streamlined or eliminated, without compromising safety and soundness or essential consumer protections. We are pleased that Congress is engaged in efforts to identify statutory requirements that also add to the level of burden without compensating benefits.

We encourage Congress to continue review the many laws and resulting regulations that institutions find most burdensome. This review should be subject to the criteria I referred to at the outset of my testimony: 1) whether the laws are necessary to ensure a safe and sound banking system, 2) whether the laws enhance the functioning of the marketplace, and 3) whether the laws can be justified on strong public policy grounds related to consumer protection. Against these criteria, the laws should be reviewed with respect to their underlying premises and whether they achieve their purposes. In addition, the costs and any side-effects should be examined to determine whether there are simpler, less-costly and more straightforward means of achieving those ends.

The regulatory burden on the banking industry grew incrementally over a number of decades -- rule by rule, requirement by requirement, report by report. The time has come to search through the baggage to determine what is really necessary to carry forward. We welcome the opportunity to work with you Mr. Chairman, this Subcommittee, and the Congress in this important effort.

APPENDIX A

Costs of Selected Regulatory and Legislative Requirements: An Informal Survey

In conjunction with current efforts to reevaluate the benefits and costs of various legislative and regulatory requirements for the banking industry, the FDIC conducted an informal, voluntary survey of a small group of banks it supervises. (A copy of the questionnaire is attached.) Each institution was asked to estimate its total cost — both direct and indirect — of compliance with the requirements contained in the survey. A cross section of institutions was chosen with regard to size and location. Sixty-one banks participated, representing every region of the country. The smallest participant had assets of only $4.6 million at year-end 1994; the largest had $9.2 billion of total assets. Random sampling could not be used with only 61 banks, so the results are representative of only the institutions selected, but not the banking industry generally.

This study differed from others that have been conducted in recent years. For reasons of time and burden on the institutions surveyed the FDIC focused only on specific provisions for regulatory relief generally supported by the FDIC rather than on overall regulatory cost or broad categories of regulation or legislation. Respondents were asked only to report costs associated with specific requirements that would not otherwise be incurred.

Recurring Regulatory Costs

The annual cost estimates for the recurring legislative and regulatory requirements included in the survey are presented in Table 1. The reported costs of compliance for each question varied considerably among institutions; therefore, median values (the midpoint of estimates received) are used to describe the results. This measure was chosen because it is not affected by extremes in either direction.

Table 1
FDIC REGULATORY BURDEN SURVEY
Estimated Recurring Costs Incurred by a Single Bank: Selected Initiatives

Legislative Initiatives	Median Annual Dollar Cost for Reporting Institutions	Cost as Percent of Net Income (Median for Reporting Institutions)
Truth in Lending Act beyond basic interest rate information	$10,000	1.03%
Truth in Savings Act beyond basic interest rate information	5,400	0.67
Savings from consolidation of RESPA/TIL disclosure requirements	5,000	0.38
Right-of-Rescission provision of Truth in Lending Act	2,500	0.20
Accountant attestations on internal controls & regulatory compliance	3,000	0.28
Pass-through insurance disclosures to employee benefit plan depositors	1,250	0.08
Federal Reserve Act reporting of loans to executive officers	550	0.04
Federal Deposit Insurance Act reporting of bank stock collateral	250	0.01
Small business and agricultural credits reporting	500	0.05
HMDA limit raised to $50 million (for applicable institutions only)	3,000	1.46
Total Recurring Regulatory Costs	**$42,394**	**3.35%**

Consumer and Supervisory Issues. Several questions dealt with various aspects of consumer protection requirements. For instance, respondents indicated that the median cost of providing customers with Truth in Lending information over and above disclosure of the basic, annual percentage rate was $10,000 per annum. The comparable figure for Truth in Savings was $5,400. Lower estimated costs were reported for the overlapping information requirements in RESPA and Truth in Lending and for the cost of right of rescission under Truth in Lending. To put these dollar figures in perspective, in no case did the reported cost of any specific regulation exceed 1.1 percent of net income in 1994 for the relevant institutions.

Other questions focused on supervisory issues. For instance, the median cost of obtaining an outside auditor to attest to an institution's assertions regarding its compliance with internal controls, regulations, and legal requirements was reported to be $3,000. No other question regarding supervisory issues yielded median cost estimates that exceeded $1,250.

Reporting Burden. With respect to reporting burden, the cost of providing data on small loans to business and agriculture was less than $500 for half of the respondents. On a per loan reported basis, the median cost was $1.70. A proposal has been offered to increase the cutoff for the Home Mortgage Disclosure Act (HMDA) reporting exemption from an asset level of $10 million to $50 million. Banks in the $10 million to $50 million range estimated that the median cost of collecting, reporting, and making public HMDA data was $3,000 per year (just under 1.5 percent of net income). The responses regarding HMDA costs are presented in Table 2. The median cost per application received was $119.

Table 2
FDIC REGULATORY BURDEN SURVEY
HMDA Costs For Selected Size Categories

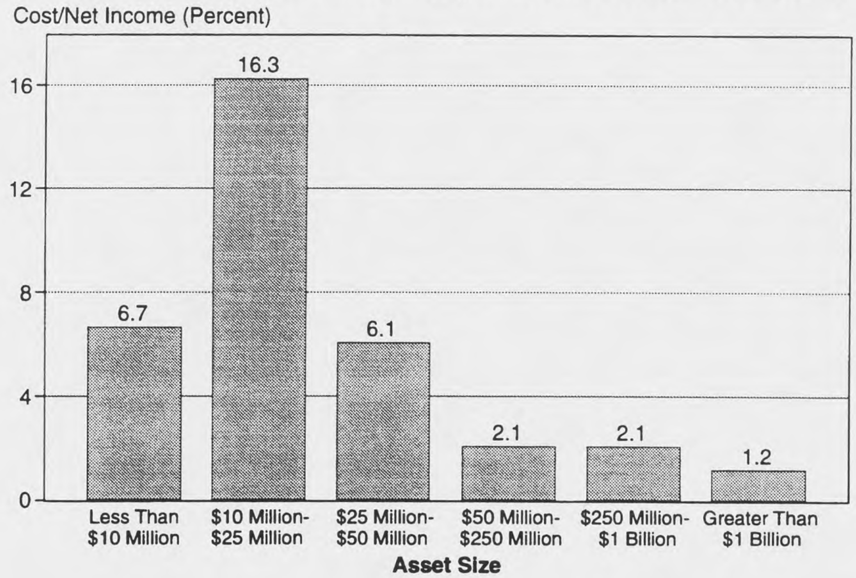
Institution Size (Assets)	Median Annual Dollar Cost for Reporting Institutions	Cost as Percent of Net Income (Median for Reporting Institutions)	Special Measures (Median for Reporting Institutions)
$10 to $25 million	$ 2,300	1.19%	$ 97.31 / Application
$10 to $50 million	3,000	1.46	$118.80 / Application
Greater than $50 million (Institutions not affected by current proposals)	22,000	0.25	$ 17.52 / Application

Total Recurring Costs. For all recurring requirements included in the survey, the median annual cost of compliance was reported to be approximately $40,000 per institution (3.35 percent of net income). If those requirements had not been in place, the responses suggest that half the institutions would have seen a pre-tax increase in their return on assets of more than 5 basis points.

Differences by Size of Institution

The FDIC survey confirmed the findings of other studies which have shown that small institutions generally bear a higher proportional regulatory burden than large ones. Smaller institutions reported that a clearly higher proportion of their budgets is devoted to meeting the recurring requirements

FDIC REGULATORY BURDEN SURVEY
Median Recurring Costs for Reporting Institutions: Selected Initiatives



addressed in the survey. Specifically, the proportion of net income devoted to these items ranged from over 16 percent at the smaller institutions to just over one percent at the largest. As may be seen in Table 2, the cost to comply with HMDA requirements was proportionally higher for small institutions than for larger ones.

The Cost of Various Applications/Notifications

Respondents also were asked to estimate the cost of various applications and notifications that they periodically submit to the FDIC (see Table 3). The estimates for these items ranged from a median cost of $500 for a notification of a change in senior management to $20,000 for reporting

Table 3
FDIC REGULATORY BURDEN SURVEY
Estimated Costs: Selected Applications/Notifications

Legislative Initiatives	Number of Institutions Responding to Question	Median Annual Dollar Cost for Reporting Institutions	Cost as Percent of Net Income (Median for Reporting Institutions)
Establishment or relocation of a branch	40	$5,000	0.15%
Change in senior executive officer or Board of Directors	39	500	0.04
Exercise of trust powers	14	1,000	0.02
"Phantom" merger or corporate reorganization	15	20,000	0.23
FDIC permission to conduct activities not allowed national banks	13	2,500	0.07

major corporate reorganizations. These estimates were based on a subset of the institutions queried, as not all participants had experience in all types of actions.

Overall Costs

Because the survey was informal and voluntary, it could not employ a statistically-representative sample of institutions. Thus, it is not possible to provide statistically-based industry-wide estimates of the potential cost savings from the elimination of the requirements in question. However, to approximate the larger scale of savings for all FDIC-supervised institutions, the figures from the participating banks were generalized to all such institutions. (All FDIC-supervised institutions to which that requirement was applicable were assigned the same proportional costs as those responding to the survey.) For applications and notifications, the overall cost was obtained by multiplying the actual number of filings with the FDIC in 1994, times the estimated per unit cost. Because of the variability of the estimates received, a range of costs was developed based on the median and mean answers in each category.

Using the median cost estimate for each category, the total compliance costs for all questions in the survey for FDIC-insured institutions would sum to approximately $500 million in 1994. Because several institutions reported unusually high estimates of costs for each question, the mean estimate was always higher than the median for each question. Using the mean estimates as a basis for aggregating, the total cost of compliance for those selected requirements for all FDIC-supervised institutions was slightly more than $1 billion. Therefore, the range of costs for compliance of FDIC-supervised institutions can be credibly set at $500 million to $1 billion. These figures compare to total net income of all FDIC-supervised institutions for 1994 of $12.6 billion.

Results Relative to Other Surveys

In recent years two other surveys of banking institutions were undertaken regarding the costs of regulations. These surveys covered a much broader range of regulations than did the FDIC survey. In 1991, the American Bankers Association (ABA) asked a sample of their members about the "cost of regulation" in general; their industry-wide estimate based on the survey answers was $10.7 billion. The Independent Bankers Association of America (IBAA), which surveyed its community banks in 1992 on 13 broad regulations, estimated that compliance costs for all such institutions were $3.2 billion.

Because the questions asked by the FDIC were much narrower and more specific than those contained in the two earlier surveys, our cost estimates are proportionately lower. Moreover, the cost estimates involved a much different set of institutions. Each estimate of total cost was related to total assets of the relevant population of banking institutions to facilitate comparison of the various results. After that adjustment, the estimates from the FDIC survey ranged from 15 to 30 percent of the industry-wide ABA figure of total compliance costs and from 10 to 20 percent of the IBAA figure for all community banks. This was probably a reasonable result given the more limited scope of the FDIC survey.

SURVEY QUESTIONS ON REGULATORY BURDEN

1. What is the overall, estimated <u>annual</u> cost to your institution of Home Mortgage Disclosure Act (HMDA) data collection, review, and reporting, including the cost of making the results available to the public?

   $ ______________

2. What is the overall, estimated <u>annual</u> cost of all other disclosures required by the Truth In Lending Act beyond the disclosure of the basic, annual percentage rate?

   $ ______________

3. What is the:

   a. Percentage of home loans and lines of credit subject to rescission under the Truth In Lending Act that has been rescinded at your institution in recent years?

      ______ %

   b. Overall, estimated <u>annual</u> cost of compliance with the right-of-rescission provision of the Truth In Lending Act?

      $ ______________

4. What is the amount of estimated, <u>annual</u> savings which could be attained from the coordination and/or consolidation (i.e., elimination of overlaps as well as of differences in definitions and coverage) of disclosure requirements of the RESPA and the Truth in Lending Act?

   $ ______________

5. What is the overall, estimated annual cost of providing customers with the disclosures required by the Truth in Savings Act, over and above those revealing the rate and method used to calculate interest?

$ ______________

6. You currently are required to report data on various types and size categories of small business and agricultural credits on the June call report. What is the overall, estimated annual cost of having to comply with this reporting requirement?

$ ______________

Note: Banks are required to report on Part II of Schedule RC-C of the June call both the number, and amount outstanding, of business loans with original amounts of $1 million or less and of outstanding farm loans with original amounts of $500,000 or less. Included are loans secured by nonfarm, nonresidential properties, commercial and industrial loans, loans secured by farm land, and other loans to farmers.

7. What is the anticipated cost of providing required disclosures to employee benefit plan administrators regarding the availability of pass-through deposit insurance coverage on employee benefit plan deposits (effective July, 1995 as outlined in FIL-14-95)?

a. Initial cost $ ______________

b. On-going cost $ ______________

8. Section 36 of the FDI Act requires attestation by an institution's independent public accountant to management's assertions regarding internal controls and compliance with FDIC regulations and federal laws. What is the overall, estimated annual cost of compliance with this requirement?

$ ______________

Note: Section 36 (c) of the FDI Act requires an institution's independent public accountant to attest to, and report separately on, the assertions of the institution's management contained in any internal control report required by Section 36(b)(2) of the Act. Section 36(e) of the FDI Act requires the institution's independent public accountant to apply procedures agreed upon by the FDIC to objectively determine the extent of compliance of the institution with laws and regulations designated by the FDIC.

9. Proposals have been made regarding the streamlining of notice and application processes. What is the overall, estimated cost of preparation and submission of an application or notice for:

a. Establishment/relocation of a branch?

$ ______________

b. Change in senior executive officer/board of directors (pursuant to Section 32 of the FDI Act)?

$ ______________

c. Exercise of trust powers?

$ ______________

d. "Phantom" merger/corporate reorganization?

$ ______________

e. An application to conduct activities not permissible for national banks (pursuant to Section 24 of the FDI Act)?

$ ______________

10. What is the estimated, <u>annual</u> cost to your institution of maintaining and reporting data required by Section 22 (g) of the Federal Reserve Act regarding loans to executive officers--both from outside sources and from your institution?

$ ______________

Note: Section 22(g)(6) of the Federal Reserve Act requires executive officers to report to their Board of Directors, detailing the extensions of credit from another institution whenever the aggregate amount of those extensions exceed the permissible limits from their own institution. Section 22(g)(6) is made applicable to insured nonmember banks through Section 18(j) of the FDI Act. Section 22(g)(9) of the Federal Reserve Act requires that each institution include with its call report data on all loans to executive officers since the filing of the previous call report made pursuant to Section 22(g).

11. Section 7(j)9 of the FDI Act requires reporting of credit extensions secured by 25 percent or more of any class of stock of an insured depository institution. What is the overall, estimated annual cost of this reporting requirement?

$ ______________

Note: Section 7(j)9 of the FDI Act requires any financial institution and any affiliate that has credit outstanding which is secured directly or indirectly by 25 percent or more of any class of shares of another insured depository institution to file a report with its federal banking agency. A copy also is required to be filed with the appropriate federal banking agency of the institution whose stock secures such extensions of credit.

12. Are there any other areas of banking law or regulation which you feel are particularly costly to your institution that you feel should be eliminated?

Regulation ______________________________________

Estimated annual cost $ ______________

Regulation ______________________________________

Estimated annual cost $ ______________

APPENDIX B

ADDITIONAL REGULATORY RELIEF MEASURES

The FDIC also believes the following additional statutory changes would help significantly to reduce regulatory burden. We recommended their inclusion in the bill.

- **Repeal section 39 of the FDI Act.** Section 39 requires the Federal banking agencies to prescribe standards, by regulation or guideline, for all insured depository institutions relating to asset quality, earnings, stock valuation, various operational and managerial matters, and compensation. The standards required to be prescribed by the agencies represent an extraordinary foray into the micromanagement of a depository institution and are unnecessary to ensure safety and soundness. Not only are the standards difficult and burdensome for the agencies to establish, but the agencies already have sufficient authority to deal with abuses and unsafe or unsound practices on a case-by-case basis under section 8 of the FDI Act and other provisions of law and regulation. The guidelines which the agencies may issue in satisfaction of this statute are likely to be more confusing than helpful.

- **Repeal section 37(a)(3)(D) of the FDI Act.** Section 37(a)(3)(D) requires the Federal banking agencies to develop jointly a method for insured depository institutions to provide supplemental disclosure of the estimated fair values of their assets and liabilities, to the extent feasible and practicable, in any balance sheet, financial statement, report of condition, or other report of any insured depository institution required to be filed with a Federal banking agency.

  Section 37(a)(3)(D) has not only been difficult and burdensome for the agencies to implement but also places additional regulatory burden on insured depository institutions by requiring them to disclose a variety of information, much of which the agencies already are able to obtain. For example, financial statements that are filed annually with the agencies by institutions subject to the audit and reporting requirements of section 36 of the FDI Act (i.e., institutions with $500 million or more in assets) and any other institution with financial statements prepared in accordance with Generally Accepted Accounting Principles already include information on the fair value of their financial instruments. While not all of an institution's assets and liabilities are financial instruments, the vast majority are. Other real estate (which is one of the more significant assets that is not a financial instrument) is carried on an institution's balance sheet at an amount that does not exceed fair value less estimated selling costs. Also, certain securities are carried at fair value on the balance sheet and, for those securities that are not carried at fair value on the balance sheet, supplemental disclosure of their fair value is provided.

In addition, institutions with assets in excess of $100 million will be required to disclose the fair value of their off-balance sheet derivatives beginning March 31, 1995. For institutions subject to section 36 of the FDI Act (i.e., institutions that pose the largest risk to the insurance funds), the fair value disclosures required by section 37(a)(3)(D) essentially duplicate much of the information that they already disclose. For the few assets and liabilities for which fair value is not currently disclosed, it may not be feasible or practicable to determine fair value. Moreover, the agencies have the authority under section 36 of the FDI Act to require fair value disclosure as they determine to be necessary.

- **Amend section 11(a)(1)(D) of the FDI Act**. Section 11(a) of the FDI Act prohibits the FDIC from providing pro rata or "pass-through" deposit insurance coverage to employee benefit plan deposits that are accepted by an insured depository institution at a time when the institution may not accept brokered deposits under section 29 of the FDI Act. Consequently, if an institution accepts employee benefit plan deposits at a time when it is unable to accept brokered deposits (i.e., when it is undercapitalized), such deposits would only be insured up to $100,000 per plan (as opposed to $100,000 per participant or beneficiary). Under existing law, the depositor, rather than the institution, would be penalized for the institution's behavior.

  By limiting "pass-through" coverage on employee benefit plan deposits, the burden is placed on plan administrators every time a deposit is made to inquire as to an institution's capital category and ability to accept brokered deposits before placing plan deposits with the institution, even though many plan administrators may not be aware of such restrictions. Even if they are aware of such restrictions, plan administrators must inquire each time as to the institution's continuing ability to provide "pass-through" coverage. Not only are the "pass-through" restrictions burdensome and unfair to plan administrators and participants, but they also are burdensome to the institution by subjecting it to frequent requests for information concerning its ability to offer "pass-through" insurance to employee benefit plan deposits.

We suggest amending section 11(a)(1)(D) of the FDI Act to prohibit undercapitalized institutions from accepting employee benefit plan deposits. The effect of the suggested amendment would be to provide "pass-through" deposit insurance coverage to employee benefit plan deposits that are accepted by an institution that violates the law and accepts such deposits at a time when it is undercapitalized. Under the amendment, the institution, rather than the depositor would be penalized, which is consistent with the way brokered deposits are treated under the law.

- **Repeal section 29A of the FDI Act**. Section 29A requires deposit brokers to file notices with the FDIC and imposes certain recordkeeping and reporting requirements on deposit brokers. The FDIC believes that the requirements of section 29A serve no useful supervisory purpose and that the receipt and use of brokered deposits can be monitored through call reports and the examination process. The effect of repeal would be to reduce the burden on deposit brokers who have no reason to know what their clients are doing with the brokered funds, and on any institutions that may be acting as deposit brokers, as well as on the FDIC in receiving and maintaining reports filed by deposit brokers. Repeal would in no way change the existing restrictions on depository institutions accepting brokered deposits. The amendment would also eliminate what appears to be an incipient problem whereby individuals or entities file the notice with the FDIC that they are acting as deposit brokers and claim or misrepresent themselves to potential customers as "registered," "licensed," or "approved" by the FDIC.

- **Conform the interest-rate limitations contained in section 29 of the FDI Act**. As currently drafted, section 29 contains three separate and dissimilar provisions that limit the rate of interest payable by insured institutions that are not well-capitalized.

  The first of these provisions is section 29(e) which prohibits an adequately capitalized institution that has received a waiver to accept brokered deposits or an institution for which the FDIC has been appointed conservator from paying interest on brokered deposits that significantly exceeds the rate paid on deposits of similar maturity in the institution's normal market area or the national rate paid on deposits of comparable maturity, for deposits accepted outside the institution's normal market area.

The second provision limiting interest rates is section 29(g)(3). This section provides that any insured depository institution (other than a well-capitalized institution) that solicits deposits by offering significantly higher rates of interest than the prevailing rates in the institution's normal market area is deemed to be a "deposit broker." This provision essentially limits the rate that institutions that are not well-capitalized may pay on deposits obtained without the intermediation of a third-party broker.

The third provision limiting interest rates is section 29(h). This section prohibits an undercapitalized institution from soliciting deposits by offering rates of interest that are significantly higher than the prevailing rates of interest in the institution's normal market areas or in the market area in which such deposits would otherwise be accepted.

Computing effective yields in an institution's normal market area or in any particular area is conceptually difficult. There is a need to simplify and harmonize these provisions by eliminating the references to "normal market area" and "market area in which such deposits would otherwise be accepted" and replacing these "point-of-origin" or "geographically-determined" interest rate restrictions with a single interest-rate restriction that is independent of the geographic origin of the deposit.

- **Repeal section 30 of the FDI Act**. Section 30 prohibits an insured depository institution from entering into a written or oral contract with any person to provide goods, products, or services to or for the benefit of the institution if the performance of such contract would adversely affect its safety or soundness.

  Since enactment of section 30, there has been a significant decrease in the types of activity that the statute was intended to eliminate (i.e., abuses involving contracts made by or on behalf of an insured depository institution that seriously jeopardize or misrepresent its safety or soundness). This decrease is due in part to increased awareness of the potential for contracts to be structured in a manner that is adverse to an institution's safety or soundness and the use of alternative supervisory actions by the agencies to address such abuses if they arise. Not only has section 30 been difficult and burdensome to implement, but the agencies already possess adequate supervisory authority under section 8 of the FDI Act and other provisions of law and regulation to address adverse contracts.

- **Amend section 22(g) of the Federal Reserve Act**. Section 22(g) of the Federal Reserve Act prohibits a member bank from extending credit to its executive officers except in the amounts, and for the purposes, and upon the conditions specified therein. Section 18(j)(2) of the FDI Act and section 11(b) of the Home Owners' Loan Act make such restrictions applicable to nonmember banks and savings associations, respectively. Among the exceptions to the prohibition on loans to executive officers specified in section 22(g) are loans secured by a first lien on a dwelling of an executive officer which is expected to be owned by the executive officer and loans to finance the education of the children of an executive officer. The following amendments would expand the statutory exceptions to the restrictions on loans to executive officers to include home equity lines of credit up to $100,000 and loans secured by readily marketable assets up to 50 percent of fair value. The effect of such amendments would be to provide additional flexibility in lending to executive officers without compromising safety and soundness standards.

SUMMARY OF STATEMENT BY CHAIRMAN HELFER
FEDERAL DEPOSIT INSURANCE CORPORATION
ON REGULATORY BURDEN AND RELATED ISSUES
MAY 2, 1995, SENATE BANKING COMMITTEE

The FDIC supports the purposes of H.R. 650, the Economic Growth and Regulatory Paperwork Reduction Act of 1995 and, with a few exceptions, endorses the specific changes in the law.

Chairman Helfer begins her statement by setting forth three specific criteria that should be used to test the necessity for and effectiveness of current laws and regulations. These are: 1) whether the regulations are necessary to ensure a safe and sound banking system, 2) whether the regulations enhance the functioning of the marketplace, and 3) whether the regulations can be justified on strong public policy grounds related to consumer protection.

The Chairman then discusses the results of an informal survey of banks conducted by the FDIC on the potential savings that might be associated with the repeal or modification of specific legislative or regulatory requirements. Next, her statement comments on the legislation introduced by Chairman Shelby, S. 650. Then, she reviews current efforts of the FDIC to alleviate regulatory burden in the safety and soundness and consumer compliance areas -- some commenced at the FDIC's own initiative, others with the impetus of legislation. Finally, she proposes additional statutory changes to further reduce regulatory burden on insured institutions.

FDIC Survey

Within the past month, the FDIC conducted an informal survey of just over 60 institutions that the FDIC supervises in order to gauge the potential cost savings from the elimination of specific legislative requirements and regulations currently on the books. The regulatory and legislative requirements surveyed included: Truth in Lending and Truth in Savings disclosures, loan data collection and reporting, auditor attestation requirements for bank compliance with laws and regulations, as well as the cost of various applications and notifications. While the survey was informal -- and, therefore, cannot be used to make industry-wide estimates -- the FDIC believes the results support two general conclusions. First, small institutions bear higher proportionate costs than larger ones. Second, the responses clearly suggest that positive cost savings could be achieved if the surveyed requirements were eliminated. Taken together, the FDIC estimates that the savings from completely eliminating all requirements covered in the survey could increase the annual rate of return on assets from 5 to 10 basis points on a pre-tax basis for institutions the FDIC supervises.

Comments on S. 650

The FDIC believes that S. 650 is a strong attempt to address regulatory burden and the effectiveness of applicable statutes.

Truth in Lending. The FDIC is supportive of the revisions to TILA prescribed by S. 650.

The Community Reinvestment Act of 1977. The FDIC urges the Subcommittee to allow the agencies to implement the new CRA rule and to evaluate its effectiveness in reducing regulatory burden before instituting further changes to the CRA, such as a small bank exemption and a safe harbor. The new CRA rule should be given an opportunity to demonstrate that it does what the agencies intend -- allow banks, large and small alike, to focus on lending, not on paperwork. If the regulation is effective, there will be more confidence in the CRA ratings and less reason for protest.

Truth in Savings. While the FDIC supports reducing the complexity and regulatory burden imposed by TISA, the agency cautions the Subcommittee that such a sweeping amendment would eliminate some of the initial disclosures that provide meaningful assistance to bank customers in their effort to comparison shop for deposit products. The FDIC recommends that the Subcommittee consider legislation that directs the Federal Reserve Board to review Regulation DD and revise those specific sections that do not enhance the ability of consumers to make informed decisions about deposit products and accounts.

Examinations. The FDIC does not believe it is prudent at this time to extend the maximum permissible examination cycle for certain small institutions from 12 or 18 months to 24 months. It was the FDIC's experience in the mid-1980s, that examination cycles were stretched out for small institutions on the theory that they did not present systemic risk problems. In fact, serious problems developed in the interim and these problems went undetected for some time. In some cases, they ultimately caused significant losses to the deposit insurance funds. The FDIC recommends no change in the law with respect to the examination cycle.

FDIC Board Composition. The FDIC supports the concept of assuring state bank regulatory experience on the FDIC Board. The agency, however, strongly suggests that consideration be given to keeping the Board at five persons for administrative ease, while designating that one of the seats be held by an individual with state bank regulatory experience. This would allow the individual to commit full-time to FDIC matters. The addition of another part-time member to the FDIC Board would result in over half of the board members being part-time.

<u>Other Provisions</u>. The FDIC supports provisions of the bill with respect to branch approvals and closures, notice requirements for new board members or senior executive officers, liberalization of the requirements governing insider lending, abolishment of the Appraisal Subcommittee, review of agency regulations every ten years, repeal of call report requirements for small business and small farm loans, increasing the size of banks required to report under HMDA, and self-testing for compliance with the fair lending laws. The FDIC opposes the provisions of the bill with respect to due process that undermine our ability to protect a bank conservatorship or receivership.

Current Efforts of the FDIC to Reduce Regulatory Burden

The testimony also reviews specific burden reduction efforts that the FDIC has already taken. The examples fall in the categories of safety and soundness examinations, compliance examinations, and regulation review and streamlining. In addition, in accordance with section 303 of the Riegle Community Development and Regulatory Improvement Act of 1994, the FDIC initiated a complete review of the agency's regulations and policy statements in an effort to identify those that have become obsolete or those for which the cost to comply substantially outweighs the intended benefits.

Additional Statutory Suggestions to Reduce Regulatory Burden

The FDIC offers additional statutory changes that would help reduce regulatory burden without compromising safety and soundness. For example, the FDIC recommends repealing section 39 of the FDI Act that requires federal banking agencies to prescribe operational managerial standards for all insured depository institutions.

The FDIC concludes by urging Congress to continue to review the many laws and resulting regulations that institutions find most burdensome. The review should be subject to the same criteria referred to in the outset of the testimony.