



Testimony of

Ed Templeton

President and CEO of SRP FCU

***“Rising Regulatory Compliance Costs and
Their Impact on the Health of Small Financial Institutions”***

On behalf of

The National Association of Federal Credit Unions

Before the

House Financial Services Committee

Subcommittee on Financial Institutions and Consumer Credit

United States House of Representatives

May 9, 2012

Introduction

Good morning, Chairman Capito, Ranking Member Maloney, and members of the Subcommittee. My name is Ed Templeton and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). Thank you for holding this important hearing. We appreciate the opportunity to share our views on the impact that rising regulatory compliance costs are having on credit unions and their member-owners.

I am the President and CEO of SRP Federal Credit Union, headquartered in North Augusta, South Carolina. I have been with SRP in this capacity for nearly 25 years. SRP has \$600 million in assets and serves more than 100,000 members at over 20 branches across the entire Central Savannah River Area community in both South Carolina and Georgia. I also serve as Treasurer on the Board of Directors at NAFCU.

I formerly served on the NAFCU Education Committee and was President of the Columbia Chapter of Credit Unions. I received my BBA from Augusta College, graduated from the Georgia School of Banking and the BAI School of Bank Administration at the University of Wisconsin.

As you know, NAFCU is the only national organization that exclusively represents the interests of our nation's federally chartered credit unions. NAFCU is comprised of over 800 member-owned and operated credit unions. NAFCU member credit unions collectively account for approximately 66% of the assets of all federally chartered credit unions.

Background on Credit Unions

Historically, credit unions have served a unique function in the delivery of necessary financial services to Americans. Established by an Act of Congress in 1934, the federal credit union system was created as a way to promote thrift and to make financial services available to all Americans. Credit unions have been widely recognized as a banking alternative for those who would otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to fill a precise public need – a niche still filled today for nearly 94 million Americans.

Every credit union is a cooperative institution organized “for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes.” (12 U.S.C. §1752(1)). While over 75 years have passed since the Federal Credit Union Act (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain as critically important today as they were in 1934:

- Credit unions remain singularly committed to providing their members with efficient, low-cost, personal service.
- Credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

The nation’s approximately 7,100 federally insured credit unions serve a different purpose and have a fundamentally different structure than banks. Credit unions exist solely for the purpose of

providing financial services to their members while banks strive to make a profit for their shareholders. As owners of cooperative financial institutions united by a common bond, all credit union members have an equal say in the operation of their credit union – “one member, one vote” – regardless of the dollar amount they have on account. These singular rights extend all the way from making basic operating decisions to electing the board of directors. Federal credit union directors also generally serve without remuneration – a fact epitomizing the true “volunteer spirit” permeating the credit union community.

Today, credit unions continue to play a very important role in the lives of millions of Americans from all walks of life. As consolidation among financial depository institutions has progressed, and the delivery of financial services has become much less personal at some large banks, consumers are not only focused on services provided but also the quality and cost of what is available to them. While many large banks have increased their fees and curtailed customer service as of late, credit unions continue to provide their member-owners with high quality personal service at the lowest cost possible. This is evidenced, most recently, by the thousands of Americans that turned to their local credit unions as national banks proposed new monthly fees on basic banking services.

Credit Union Performance & the Financial Crisis

While lending practices of many other financial institutions contributed heavily to the nation’s subprime mortgage debacle, credit unions and other community based financial institutions were not the cause of the housing and financial crises. As the Subcommittee is aware, this point has been made by members of the House Financial Services Committee on both sides of the aisle.

Still, credit unions have consistently been among the most highly regulated of all financial institutions, facing restrictions ranging from who they can serve to their ability to raise capital.

Despite the fact that credit unions are already heavily regulated, were not the cause of the financial crisis and actually helped blunt the crisis by continuing to lend to credit worthy consumers during difficult times, they are still firmly within the regulatory reach of provisions contained in the *Dodd-Frank Act*. The additional regulatory requirements mandated in this massive overhaul have added to the overwhelming number of compliance burdens for credit unions. Undoubtedly, an immense amount of time, effort, and resources will be expended at credit unions as they struggle to keep up with new regulation.

Increasing Compliance Burdens at Credit Unions

Today's hearing could not be more timely or more important to our nation's credit unions. NAFCU appreciates the opportunity to discuss the impact of increased regulatory burden on credit unions today and how this uncharted territory, including the creation of the Consumer Financial Protection Bureau (CFPB), could impact credit unions in future years. While the focus of today's hearing is on small financial institutions, **all** credit unions have felt the impact of increased regulatory burden.

While not the direct subject of this hearing, providing credit unions relief from the outdated arbitrary member business lending cap and allowing credit unions access to supplemental capital would provide some needed regulatory relief from outdated restrictions.

In April 2011, NAFCU surveyed its membership about what they were experiencing with respect to increased regulatory burdens. Almost all of the survey respondents (96.4 percent) said that their credit union spends more staff time on regulatory compliance issues today than it did in 2008, and most of those respondents did not expect to spend any less time on compliance issues over the next 12 months (96.3 percent). Survey participants further stated that, on average, 14.1 percent of staff time, as measured by their credit union's total full-time equivalents, was spent on compliance issues in 2010. The majority of the responding credit unions (82.7 percent) indicated that this number had increased when compared to 2009, while the remaining 17.3 percent did not see any change. None of the credit unions responding experienced a decrease in the staff time spent on regulatory compliance issues in 2010.

My credit union is experiencing the same thing, as we recently doubled our compliance officers from one to two. Additionally, my staff and I spend much more time today focused on compliance issues than we did just a few short years ago.

While three quarters of the survey respondents indicated that their credit union was, at the time, not considering reducing any products and/or services as a result of the increased regulatory burden, almost two thirds said they have increased or were considering increasing fees on products and/or services due to the increased regulatory burden cost or loss of other income due to recent regulatory changes. In addition, one quarter of responding credit unions stated that they were anticipating accepting mergers or were considering merging itself out as a consequence of the increased regulatory burden.

My testimony below will outline how the *Dodd-Frank Act* is creating new challenges and uncertainty for credit unions. The mandates of the new CFPB could lead to an overwhelming tide of new compliance burdens. It will be incumbent upon the Bureau and Congress to ensure that the CFPB also meets its goals of streamlining regulation and protecting small entities in every action that it takes.

Challenges for credit unions do not only come from Dodd-Frank and the CFPB, but also the National Credit Union Administration (NCUA). While the government-wide review of regulation appears to be a right step, it will be up to the NCUA and other agencies to ensure that real changes are made and not just given lip-service.

Finally, regulatory burden also come from a number of outdated laws on the books. We hope Congress will take steps to pass legislation that will help relieve some of these heavy burdens on our nation's credit unions.

New Burdens Stemming from the Dodd-Frank Act

One of the biggest impacts on my credit union from the *Dodd-Frank Act* has been the hastily crafted debit interchange provision added in the Senate. While my credit union was supposed to be unaffected by this provision, that has not been the case. We have seen market forces drive our average debit interchange rate down about 1-2 cents per transaction (depending on PIN or signature usage) since its enactment. Furthermore, in order to comply with the new routing requirements stemming from this provision, my credit union had to re-issue hundreds of plastic cards at a cost of over \$2.00 per card. While you may hear reports that some small institutions

have not been impacted by these new rules, there are other small ones like mine out there that have felt the impact. As discussed below, the biggest impacts from *Dodd-Frank* remain to be seen.

Dodd-Frank Rulemaking Underway

While NAFCU encourages in-depth review of existing regulations, credit unions already find themselves struggling to keep their heads above water as a steady stream of Dodd-Frank related regulation moves forward.

As widely publicized, the CFPB estimated that its first rule on international remittance transfers would require 7.7 million total employee hours of work for the industry to implement and comply with. This mindboggling headline strikes at the very core of what credit unions fear most – Dodd-Frank mandated regulation will be finalized so quickly, and so often, that community-based financial institutions simply won't be able to keep up. In a recent letter to JPMorgan Chase stockholders, CEO Jamie Dimon estimated that over the next few years 3,000 employees will be devoted full time toward helping the megabank come into compliance with regulatory changes. While my credit union will be subject to a number of the same regulations, I have just two employees working on compliance issues. I just hope we can keep up and continue to serve our members.

It is worth noting that revisions that led to the CFPB's final rule on international remittance transfers were originally proposed by the Federal Reserve, but as mandated in Dodd-Frank, finalized by the CFPB. On the same day the rule was finalized, the CFPB simultaneously issued

a proposed rule and request for comment that sought feedback on the disclosure process for recurring remittance transfers. The proposed rule also sought comment on whether it should allow an exception for institutions that infrequently provide such services. NAFCU appreciates the Bureau's decision to seek more input regarding the unique problems that arise with preauthorized or reoccurring electronic fund transfers. We hope that this is an openness that will continue in both word and deed.

Under the proposed rule, an exception for remittance transfer providers, presumably made to accommodate small financial institutions, falls far short of offering any tangible relief to credit unions who operate in this space. Those providers making less than 25 international remittance transfers a year would be exempt and therefore free of the extensive disclosure requirements that are mandated for those providers above that threshold. This arbitrary and exceptionally low number will not provide relief for credit unions.

Furthermore, a vast majority of credit unions who provide remittance transfer services rely on open network systems. By the CFPB's own admission, under the rule already finalized, it will be exceedingly difficult for open network systems, as currently configured, to comply. This leaves credit unions with two plausible choices – stop doing international remittance transfers, a service that many members utilize and value, or pay for a massive reconfiguration of the payment networks needed to comply. It should be noted that Congress only recently gave credit unions the ability to do remittances for all consumers in their field of membership, in an effort to reach the under- or un-banked. The cooling of remittances will very likely discourage those populations from using credit unions.

While the international remittance transfer rule was the first and only rule related to *Dodd-Frank* to be finalized by the CFPB thus far, there are an overwhelming number of upcoming Dodd-Frank mandates that will directly impact credit unions. The CFPB's mandates are particularly daunting as related to Regulation Z, the implementing regulations for the *Truth in Lending Act* (TILA). Nearly every aspect of current compliance requirements with respect to operating a mortgage portfolio has the ability to change.

By January 2013, the CFPB is expected to expand the scope of coverage under the *Home Ownership and Equity Protection Act*, address mortgage origination and mortgage servicing standards, amend rules associated with the *Truth in Lending Act* and *Financial Institutions Reform, Recovery, and Enforcement Act*, change requirements for escrow accounts and issue rules under *Dodd-Frank* relative to what constitutes a "qualified mortgage." While many of the details are yet to emerge, the sheer pace at which these new rules are scheduled to be implemented should cause serious pause. Even if they are well-intentioned and ultimately bring about positive changes, there is a burden on small institutions in just keeping up.

With respect to mortgage lending, NAFCU would like to take this opportunity to recognize the CFPB's efforts in collecting information from credit unions as they work to streamline mortgage disclosure forms to be provided to consumers at settlement. A colleague of mine that also sits on NAFCU's board participated in the recent Small Business Regulatory Enforcement Fairness Act review panel on this topic, and was encouraged that the Bureau appears to be carefully considering the impact of this action on small institutions. NAFCU is hopeful that these panels will be held in the future, and input given will translate into commonsense rulemaking that

doesn't create additional and unnecessary compliance burdens for credit unions. That will be the true test.

Review of Existing Regulations

In January of last year, President Obama announced a government review of existing regulations. We hope that this ongoing review by the Administration and the efforts by Congress can recognize what credit unions like mine know all too well – the problem is not necessarily one single bill or regulation, but the cumulative effect of new regulations piled on top of each other, without studying the cumulative effects placed on small financial institutions that don't have an army of lawyers with which to comply. These burdens do not just come from one or two regulators, but from a panoply of federal agencies and laws that can impact our business. For small financial institutions, this is almost a death by a thousand cuts.

As part of this review, National Credit Union Administration (NCUA) Chairman Debbie Matz informed the Obama Administration that, since NCUA began to review their regulations every three years, they have been successful in reducing regulatory burdens. However, I can say from a credit union perspective that despite their claimed "success", burdens on credit unions remain. It is still unclear to credit unions whether there is a true process for NCUA to eliminate regulations or if they have set or met any particular benchmarks in reducing compliance burdens.

In the past two years, NCUA has made changes to its Regulatory Flexibility (RegFlex) program. Under the RegFlex regime certain well-run credit unions were exempt from a number of regulatory requirements. Recently, NCUA expanded the RegFlex program to include all credit

unions, but it also eliminated two very beneficial RegFlex provisions relative to fixed assets and personal guarantees. NAFCU feels that NCUA can and should do much more to eliminate outdated regulation. Even small tweaks to NCUA's rules can have a major impact on operations. Furthermore, NCUA should actively embrace and take into consideration technology advancements when promulgating regulations – that would be one way to ease some burden.

Updating Outdated Regulations

Despite its good intention, the creation of the new CFPB is potentially problematic for credit unions as the Bureau will have rule writing authority over credit unions of all sizes, meaning all stand to face new compliance burdens from the CFPB every time a rule is updated or a new regulation is released.

As the CFPB ramps up, NAFCU has actively participated in the Bureau's request for comment on an array of issues including regulatory streamlining. To truly understand how the onslaught of regulation scheduled to be finalized through Dodd-Frank will impact credit unions, one must look at the regulatory environment that already exists. NAFCU is hopeful that the CFPB will use its authority not only to identify, but also to streamline and simplify regulation where possible. If the CFPB and other regulators will not do this in a timely and effective manner, Congress must step in and do so. Amending or eliminating outdated regulation must be a priority as unnecessary day-to-day compliance costs at credit unions represent resources that could otherwise be used to help members purchase a new car or start a new small business.

A prime example of an outdated compliance burden is the redundant and unnecessary requirement in the Electronic Funds Transfer Act and its implementing rule (Regulation E – 12 CFR 1005.16) requiring automated teller machine (ATM) operators to provide two separate notices to consumers regarding the imposition of a fee for use of the ATM. The first is a fee disclosure on the ATM screen where a consumer is required to affirmatively indicate whether he or she accepts the fee. If the fee is declined, the transaction is cancelled. NAFCU fully supports this type of prudent disclosure. However, Regulation E also requires ATM operators to attach a physical placard to the ATM stating that a fee may be charged. If the physical placard isn't attached, the law creates a right of action against ATM operators. Unfortunately, there are unscrupulous individuals out there who go around removing these from the machines. Consequently, my staff must spend time constantly policing all of SRP's ATM machines at various branches to ensure documentation, as the threat of frivolous lawsuits is very real.

NAFCU strongly supports the bipartisan legislation (H.R. 4367) introduced by Financial Service Committee members Blaine Luetkemeyer (R-MO) and David Scott (D-GA) that would eliminate the unnecessary placard fee disclosure requirement. NAFCU has also urged the CFPB to exercise its broad authority to address this outdated regulation.

Another increased burden for credit unions comes from recent changes in the exam process. Part of the response to the economic crisis was to create new layers of regulation and institute more aggressive enforcement of existing law. In order to aggressively enforce new and old regulations and to avoid a repeat of the crisis, regulators have increasingly tightened examination standards. Exam cycles are shorter, adding an element of burden to credit unions as staff time and resources

are dedicated to prepare and respond to the exam. It is with this in mind that we also urge the committee to move forward and vote on the *Financial Institutions Examination Fairness and Reform Act* (H.R. 3461) introduced by Chairman Capito and Ranking Member Maloney.

As you know, H.R. 3461 will bring additional transparency and consistency to the examination process by establishing an Office of the Ombudsman within the Federal Financial Institutions Examination Council. The legislation would apply to both the NCUA and the CFPB and could help foster consistency in the exam process as credit unions navigate a new regulatory landscape.

It is important to understand that the current NCUA exam manual is more than five years old, with outdated law and citation. They are currently in the process of revision, but this will likely take another two years before completion. How can a credit union be expected to be in full compliance when their exam manual is filled with law that is no longer applicable? This is extremely burdensome for all credit unions.

In addition to these two examples, I cannot overstate how critical it is for the CFPB to review and simplify the complex regulatory framework credit unions already face. Such an effort could help mitigate layering regulation upon regulation to the detriment of credit unions and their member-owners.

Another example of CFPB using its authority to simplify compliance matters for credit unions without any substantive change to the protection afforded to consumers, would be reviewing the adverse action notices required under Regulation B (Equal Credit Opportunity Act - ECOA) and

very similar risk-based pricing notices required under Regulation V (Fair Credit Reporting Act - FCRA). In July 2011 the Federal Reserve finalized two rules on model adverse action notices and risk-based pricing notices to implement section 1100F of the Dodd-Frank Act pertaining to credit score information. These two very closely linked issues cause confusion as the FCRA's adverse action notice requirements have no implementing regulation. In order to comply with the FCRA's adverse action notice, creditors may use the model forms included in Regulation B intended to implement the ECOA. The rest of the FCRA, however, is implemented through Regulation V. NAFCU believes this unnecessarily complicated situation offers CFPB an opportunity to rewrite the regulations in a way that is simple and more straightforward. We hope that they will use their authority to address this in a timely and efficient manner.

At SRP FCU we spent an enormous amount of time adjusting our software to accommodate the risk-based pricing disclosure requirements described above. Staff attention to this issue encompassed a number of departments at my credit union including IT, credit, and compliance. Making commonsense changes to streamline the model forms for risk-based pricing and adverse action notices would immediately diminish the number of staff hours necessary to produce the requested information without altering the content of what SRP provides to the members.

Attached for the Subcommittee's review, please find NAFCU's detailed response to the CFPB's request for comment on regulatory streamlining (Docket No. CFPB-2011-0039). Again, NAFCU and its member credit unions remain hopeful that steps are taken to update and streamline existing regulation before new regulation is simply pushed through and layered on top of it.

Cost-Benefit Analysis

One thing that is unfortunately missing from far too many regulations and laws is a robust cost-benefit analysis for the changes that are sought. This is particularly important with not-for-profit credit unions. Are the benefits to the consumer greater than the cost of compliance? At a not-for-profit credit union, each dollar spent on compliance is a dollar unavailable for serving members or providing them with the loan that they need.

Federal agencies are required to conduct cost-benefit analysis before they issue certain proposed or final rules. These requirements have been added incrementally by various statutes and executive orders over the past 50 years. The elements of analysis usually include some or a combination of the following: quantitative and qualitative estimates of costs and benefits, effects on the national economy, consideration of a range of alternatives, selection of the alternative that is least costly, most cost-effective, or least burdensome, or an explanation of why that alternative was not selected.

Many of the current requirements have substantial exclusions and exceptions, giving federal agencies substantial discretion to decide whether an analysis is required. For example, some requirements do not apply to rules that are issued without a prior notice of a proposed rulemaking, and agencies can avoid regulatory flexibility analyses if they certify that their rules do not have a “significant” economic impact on a “substantial” number of “small entities”. At NCUA, only credit unions under \$10 million in assets are currently considered “small entities”. NCUA should consider raising the “small entities” benchmark. For example, the CFPB uses \$150 million for the Small Business Regulatory Enforcement Fairness Act review panels.

The number of *economically significant* regulations—those costing the regulated community more than \$100 million or having a significant adverse impact on competition, employment or **productivity**—has increased substantially.

These major, complex, and costly rulemakings are a primary focus of the *Regulatory Accountability Act of 2011*, a bill to modernize the Administrative Procedure Act (APA).

The APA requires agencies to regulate openly, with notice to and comment from the public, and subject to judicial review. Over time, the APA's procedural protections grew in importance as Congress passed vague laws delegating more and more to agencies. Agencies have become so skilled at their own regulatory procedures that they routinely find ways to legally circumvent them. With increased judicial deference to agency decisions and weak Congressional oversight, federal agencies now possess legislative power nearly equal to that of Congress.

The legislation would update and modernize the regulatory process in several important and balanced ways:

- Requires Advance Notice of Potential Rulemakings to increase public participation in shaping a regulation before it is proposed.
- Requires that agencies must choose the lowest cost option or explain why another was chosen, or demonstrate a compelling need to protect public health, safety, or welfare.

- Gives interested parties the opportunity to hold agencies accountable when they rely on data that does not meet the standards of the Information Quality Act.
- Provides for on-the-record administrative hearings for major regulations so that interested parties will be able to question agency personnel responsible for developing the regulation.
- Places additional requirements on agencies' use of interim final regulations and provides for expedited judicial review of whether that approach is justified.
- Makes regulations on which a hearing has been held subject to the more rigorous "substantial evidence" test in legal challenges rather than the current "arbitrary and capricious" standard.

The *Regulatory Accountability Act of 2011* will make the regulatory process more transparent, agencies more accountable, and regulations more cost effective. NAFCU believes many of the rules flowing from Dodd-Frank could be vastly strengthened by these measures, while maintaining their original objectives. Additionally, we feel that many more could be narrowed or abandoned altogether, after a thorough cost-benefit analysis.

Other issues with current agency adherence to the APA include:

- Analysis is only done prior to regulation (if it is done at all);
- Analysis usually focuses on the implementation cost and time even though the annual compliance burden is just as big of a component;

- Once regulations are passed and “in place” it is very hard to remove the continual daily compliance burden;
- Regulators rarely, if ever, look back at promulgated rules to see if they are equitable or effective in reaching their original goal.

Conclusion

The greatest challenge facing many credit unions is cumulative impact of the rapidly growing number of regulatory burdens in the wake of the financial crisis. While any one single regulation may not be particularly burdensome, the layering of new regulation on top of old and outdated regulation can completely overwhelm small financial service providers like credit unions. Unfortunately, every dollar spent on compliance, whether stemming from a new law or outdated regulation, is a dollar that could have been used to reduce cost or provide additional services or loans to members.

It is with this in mind that NAFCU continues to urge the committee to move forward with legislation that will provide regulatory relief from outdated laws and regulations for credit unions.

We thank you for your time and the opportunity to testify before you here today on these important issues to credit unions and ultimately our nation’s economy. I welcome any questions you may have.



**National Association
of Federal Credit Unions**
3138 10th Street North
Arlington, VA 22201-2149

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March 2, 2012

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1801 L Street, NW
Washington, D.C. 20036

RE: Docket No. CFPB–2011–0039

Dear Ms. Jackson:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents federal credit unions, I am writing to you regarding the Consumer Financial Protection Bureau’s (CFPB) request for comment on regulatory streamlining. NAFCU very much appreciates the CFPB’s early identification of the critical importance of streamlining regulations.

Over the last several years, there has been an ever-increasing regulatory burden for credit unions, particularly in the area of lending. In general, credit unions are smaller institutions, with lesser economies of scale; consequently, these constant changes have a more significant impact on their ability to serve their member-owners. Further, given that every dollar a credit union must pay starts with a member at a teller window, the changes have a very direct impact on credit union member-owners. There are a number of steps the CFPB can take to streamline and simplify the complex regulatory framework for credit unions. Following is a detailed explanation of several regulatory issues that NAFCU urges the CFPB to simplify.

Regulation Z

There are several small issues with Regulation Z, primarily relating to mortgages and credit cards, which could be improved with relatively modest changes.

Mortgages

Lender Cost of Funds

The CFPB should use its authority to eliminate the “lender cost of funds” disclosure that the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the Dodd-Frank Act) requires on mortgage disclosures. This is one of NAFCU’s top

priorities for the streamlining process as the disclosure does not provide any useful information and, in some cases, may be misleading. The implication of the disclosure is that the lender is making a profit spread between the cost of funds and the rate the borrower is paying. Important components that make up the ultimate price, such as interest rate risk and credit risk are ignored by the disclosures and consequently will be ignored by borrowers. The purpose of the Know Before You Owe project is to simplify and clarify disclosures for consumers. Instead, this disclosure provides consumers additional information that they likely will not understand and that has only a tangential bearing on the cost of the mortgage.

Further, in the context of mortgage loans sold into the secondary market, the disclosure is also potentially misleading. The mortgage lender likely does not know the cost of funds for the investor at the time these disclosures are made. Consequently, the best that could be accomplished in this context is for the Bureau or some other entity to publish an average rate on a daily, weekly or monthly basis that could be used to make the disclosure. Providing borrowers an average rate that may be days or weeks old, we believe, detracts from the purpose of the disclosures.

NAFCU recommends the CFPB consider using its authority under section 104 of the Truth In Lending Act (TILA), which enables the Board to exempt disclosures that “are not necessary to carry out the purposes” of the Act. Alternatively, the Bureau could use its exemption under section 105, which permits the Board to exempt statutorily required disclosures based on a five factor balancing test. Either exemption would apply to this proposed disclosure, which provides little if any value and only confuses a process which the agency’s Know Before You Owe project is designed to clarify.

Waiting Period after Re-disclosure

The agency should also make changes to the rules implementing the Mortgage Disclosure Improvement Act (MDIA). Lenders are currently required to provide early disclosures three days after a mortgage application is received. Lenders must also provide updated or final disclosures at settlement. If the annual percentage rate (APR) changes beyond a certain threshold or if certain fees exceed a threshold, new disclosures must be provided. Further, section 1026.19(1)(2)(ii) requires that at least three days pass between re-disclosure and closing. Truth in Lending (Regulation Z), 76 Fed. Reg. 79,801 (proposed Dec. 22, 2011) (to be codified at 12 C.F.R. pt. 1026). NAFCU recommends the CFPB modify the three day waiting period. While well intentioned, the three day minimum is potentially harmful and, at the very least, bothersome to borrowers who understand the changes and want to move forward with closing the loan. The regulation only allows for a waiver of the waiting period if waiting will create a bona fide personal financial emergency for the borrower; however, the only example the regulation provides that would qualify is if the borrower will lose his home to foreclosure if funds are not released. *Id.* at 79,986. There are a number of other potential scenarios that may create such a hardship but lenders are wary of moving forward without more guidance. Further,

there are dozens of other legitimate reasons for a borrower to wish to move forward with the loan that certainly fall short of a “bona fide personal financial emergency.”

NAFCU recommends the agency consider three different options. First, if the agency insists on keeping a non-negotiable, minimum wait time, it should allow borrowers to move forward after one business day. One business day would still provide borrowers sufficient time to examine the changes. Further, the rule could still allow borrowers to have up to three business days after re-disclosure to examine the documents if they so choose. Permitting a minimum one day wait would minimize the hardships for people who have compelling reasons to move forward but who fail to qualify for the bona fide personal hardship exception. Additionally, a one day minimum period would still ensure that borrowers would have time to consider the changes on their own and would protect against borrowers being pressured into the change at closing. Second, the CFPB should consider relaxing the waiver requirement and allowing borrowers to waive the three day period at their discretion. Third, the agency should, at the least, provide more guidance as to what constitutes a bona fide personal financial emergency.

Credit Cards

Ability to Repay and Non-working Spouses

The CFPB should modify one aspect of the existing rule regarding the ability to repay a credit card account. Currently Regulation Z does not permit a credit card issuer to consider household income when determining whether a consumer has the ability to repay a credit card account. 12 C.F.R. § 1016.51. Requiring that issuers determine the ability to repay based solely on personal income, even in cases where there is sufficient household income to make payments is shortsighted and disproportionately impacts non-working spouses. This rule serves little practical purpose in terms of ensuring the debt will be repaid. In cases where there is a steady household income, creditors should be permitted to consider that income, rather than only the applicant’s personal income. The applicant presumably has access to the household income to pay the credit card bill and the inquiry should end there. The rule forces non-working applicants to seek the spouse’s approval for any extension of credit.

The rule is also incongruent. The rule only permit lenders to consider personal income, while at the same time requiring consideration of all household liabilities when making the determination of whether the debt is likely to be repaid. In addition to this aspect of the proposal being inconsistent, it, again, will only exacerbate the negative impact on non-working spouses. Issuers should be permitted to take into consideration household income on which the applicant states he or she can rely. The current rule negatively impacts all non-working spouses and greatly reduces the availability of credit for all non-working spouses.

Reevaluation of Rate Increases

The CFPB should consider modifying 12 C.F.R. § 1026.59, which requires credit card issuers to reevaluate rate increases. If a card issuer increases the APR on the account for virtually any reason, it is then required to reevaluate the APR at least every six months for an indefinite period of time. NAFCU understands the purpose behind the requirement, however, to require reevaluations every six months indefinitely for *all* APR increases is unduly burdensome. Under the current rule, a cardholder's credit score could drop by 50 percent (or more) and the credit card issuer would still be required to reevaluate the APR every six months as long as the account is active. This requirement is problematic for two reasons. First, it is a waste of resources as the issuer is required to reevaluate an account every six months when there is very little possibility that the APR will be reduced in the near future. Second, the requirement creates a perverse incentive as it drives up the cost on already risky accounts, which encourages lenders to close the account rather than work with the borrower. Accordingly, the CFPB should terminate the obligation in instances where the cardholder's credit score has dropped dramatically. This change is all the more reasonable given that most issuers will review a consumer's account upon request.

If a cardholder suffers a decrease in credit score of 5 percent, for example, it will take him a considerable amount of time to repair his credit to the point that he is eligible for the initial APR he received prior to his score decreasing. There is no benefit to consumers in requiring card issuers to reevaluate accounts every six months given the length of time it will likely require to repair the credit score. There are, however, considerable costs involved for the institution in reevaluating each account every six months. Terminating the obligation in instances where the cardholder's credit score has dropped dramatically is a reasonable way in which to balance the institution's costs against the consumer protection concerns advanced in the *Credit Card Accountability, Responsibility and Disclosure Act* (CARD Act). Further, the credit card market is highly competitive and it will likely ensure that consumers who are able to quickly repair their credit will be able to take advantage of better rates. Consumers who suffered a credit problem and have since repaired that problem will undoubtedly receive solicitations at a better rate if their current card issuer refuses to lower the APR. Indeed the credit card market is one area in which there are virtually no barriers to a consumer moving from one company to another if a better price is offered. NAFCU understands the need for consumer protection and government oversight. However, the CFPB should set some limits on the reevaluation requirement in cases where a borrower has suffered a serious decline in creditworthiness.

NAFCU urges the CFPB to alter the rules regarding household income and to simplify the reevaluation requirement in cases where a cardholder's credit score has dropped significantly.

Annual Statement of Billing Rights

The CFPB should eliminate the requirement that lenders provide borrowers an annual statement regarding their billing rights, as required by 12 C.F.R. § 1026.9. Institutions are already required to disclose all relevant information regarding the consumer's billing rights during the application and account opening process. Institutions should only be required to send an updated statement if the policy has changed. Further, these statements can be made available online and in branches and would eliminate this costly and generally useless burden.

The Annual statement of billing rights is one of three annual disclosures (privacy policies and error resolution policies are discussed below) that institutions must regularly provide. Eliminating all three of these annual disclosures is a top priority for NAFCU. The CFPB indicated it will look at five primary factors in determining whether to adopt a proposed change. Those factors are:

- The potential benefits and costs of the proposed change for consumers and regulated entities;
- The likelihood that the Bureau would be able to achieve benefits consistent with the underlying statute;
- The speed with which the public would realize the benefits;
- The governmental and private resources it would take to realize the benefits; and
- The state of the evidence with which to judge the previous four factors.

In the case of all of the annual disclosures, the benefit to regulated entities is significant as they would save considerable amounts of time and money printing and sending the annual disclosures. The change could be made consistent with the underlying statute. Further, the CFPB has considerable authority to implement TILA as it sees fit, if certain disclosures or requirements are redundant or unnecessary. The benefits would be realized immediately for financial institutions and would not require any governmental resources beyond changing the regulation. While the change may seem modest, it would save institutions a significant amount of money printing and sending the disclosures. Additionally, the change would free up valuable time for employees who would otherwise need to carry out the process. On balance, the factors heavily weigh in favor of eliminating the requirement.

General Concerns with Regulation Z

The CFPB specifically asked if the transaction threshold for coverage under Regulation Z should be increased. Currently, lenders that make twenty-five or fewer non-home secured loans a year are not covered by Regulation Z. Similarly, lenders that make five or fewer home secured mortgages per year are not covered by the rule. NAFCU recommends increasing the threshold exemption to 50 loans per year for all loan types.

Additionally, for the special rules for private student loans, NAFCU recommends a similar exemption. Specifically, a lender should not be required to comply with the existing rules for private education loans included in 12 C.F.R. §§ 1026.46-50 unless it makes at least fifty private student loans per year. The disclosures required for private student loans are lengthy and complicated. Further, the rule is so broad that virtually any loan that a borrower intends to use for education purposes is subject to the rule. Consequently, some lenders have chosen not to extend credit if the loan might be construed as a private education loan as the costs of compliance outweigh the income that can be derived from extending a small number of covered loans. Accordingly, NAFCU recommends an exemption from the requirements if a lender makes fewer than fifty private student loans per year.

Regulation E

ATM Fee Disclosure

NAFCU's top priority is eliminating the redundant and unnecessary requirement that automated teller machine (ATM) operators place a fee disclosure notice *on* the ATM, as required by 12 C.F.R. § 1025.16(c)(1). The requirement is outdated, unnecessary and has spawned a number of frivolous lawsuits. Plaintiffs have filed suit claiming the disclosures are not large enough, despite the fact that the statute and regulation do not contain size requirements and only state that the disclosure must be conspicuous. Further, it is impossible for ATM operators to ensure compliance as the sign on the ATM can simply be removed or obscured.

All ATMs include a fee disclosure on the screen during the transaction and provide consumers an opportunity to terminate the transaction without paying any fee. The on-screen disclosure should be sufficient to notify consumers. The utility of the physical sign disclosure is all the more questionable since that disclosure must only state that there may be a fee, but not the actual amount of the fee.

Accordingly, NAFCU has two recommendations. First, NAFCU encourages the CFPB to eliminate the disclosure requirement included in 12 C.F.R. 1025.16(c)(1). While this disclosure is required by statute under 15 U.S.C. § 1693b(d)(3)(A)(i), the statute also provides the CFPB authority to prescribe regulations that "contain such classifications, differentiations, or other provisions" that "provide for such adjustments and exceptions for any class of electronic fund transfers...as in the judgment of the [agency] are necessary or proper to effectuate the purposes of this subchapter, to prevent circumvention or evasion thereof, or to facilitate compliance therewith." *Id.* at § 1693b(c). The broad authority accorded the CFPB is sufficient to allow an exception for signs located on ATMs. The requirement is duplicative at best as more detailed on-screen disclosures are provided on every ATM. Consequently, an exception would not undercut the consumer protections provided by the statute. Alternatively, if the CFPB refuses to eliminate the requirement, it should consider adding an additional provision to the regulation that holds harmless an ATM operator that can show it did affix a sign to an

ATM. While this option is not as helpful, it would be useful in cases where a vandal or prospective litigant removes the disclosure from an otherwise compliant ATM.

The factors the CFPB will use in determining what proposal to adopt all weigh in favor of eliminating this requirement. The potential costs and benefits for consumers and regulated entities weigh heavily in favor of eliminating the provision. Not only does the disclosure provide little, if any, benefit, it has grown increasingly costly for ATM operators as a result of litigation. In the case of not-for-profit, member owned credit unions; these costs are passed on directly to the member-owners. As discussed above, the statute provides the CFPB considerable authority to make adjustments as it sees fit to effectuate the act. The benefits would be realized immediately as ATM operators would not need to contend, going forward, with frivolous lawsuits spurred by an out of date consumer protection requirement that provides consumers little in the way of actual protection. There would be virtually no governmental or private resources required to realize the benefits. Accordingly, the CFPB should eliminate this requirement.

Account Truncation

NAFCU recommends the CFPB allow financial institutions to truncate account numbers in some cases. Regulation E requires a periodic statement for accounts from which electronic fund transfers may be made. 12 C.F.R. § 1005.9(b). Practically speaking, any checking and savings account falls under the regulation's coverage. Further, § 1005.9(b)(2) requires the periodic statement to include the account number. NAFCU recommends permitting truncation of the account number on the periodic statement. Truncating the account number is a useful way to help combat fraud and identity theft. Indeed, § 1005.9(a) specifically allows for truncation to as few as four digits for receipts at ATMs or other electronic terminals. Understandably, there is a heightened concern that ATM receipts will be quickly discarded in a public place. Periodic statements are, perhaps, less likely to be discarded in a public place, nonetheless, allowing for truncation would help protect consumers by minimizing fraud risks. There is little, if any, reason not to allow truncation in this instance.

Annual Statement Regarding Error Resolution

Regulation E currently requires an annual notice concerning error resolution. The CFPB should eliminate this requirement. Institutions are already required to provide the notice at account opening. Institutions should only be required to send an updated error resolution notice if the institution's policy has changed. Error resolution policies are generally available at branches and online and the CFPB could require the document be made available online in place of the current requirement. Requiring institutions to mail the same policy year after year serves little benefit. Indeed many consumers likely assume the disclosure means there has been some change to the policy. NAFCU recommends the agency eliminate the requirement to send error resolution policies every year if the policy has not changed. For all the same reasons discussed above in the

section regarding the annual statement of billing rights, NAFCU believes the CFPB's factors for consideration weigh in favor of making this change.

Regulation P

The agency should also eliminate the requirement that financial institutions send customers annual privacy notices. This requirement is included in 12 C.F.R. § 1016.5. Again, institutions are already required to provide the privacy notice at account opening. The CFPB should eliminate the annual requirement and instead only require a notice after account opening if the institution's privacy policy has changed. Privacy policies are also generally available at branches and online. Requiring institutions to mail the same privacy policy year after year serves little benefit. NAFCU recommends the agency eliminate the requirement for annual privacy policy disclosures in cases where the policy has not changed. For all the same reasons discussed above in the section regarding the annual statement of billing rights, NAFCU believes the CFPB's factors for consideration weigh in favor of making this change.

Regulation C

Under Regulation C, institutions that refinance a single loan in a calendar year must file a Home Mortgage Disclosure Act (HMDA) report. NAFCU recommends instituting a minimum threshold of at least fifty refinance transactions before an institution is subject to the rule. A threshold of fifty would make the rule consistent with Regulation Z, without undercutting the policy rationale of HMDA. Institutions that refinance fewer than fifty transactions per year are arguably not even offering refinancings in the normal course of business. An institution that extends fifty or fewer such transactions is likely only doing so as an accommodation to existing customers. Granted, a threshold exemption will result in a small number of loans going unreported. However, Regulation C will still capture the vast majority of all mortgage loans and refinancing transactions. Further, the very small cost of slightly fewer reporting entities is outweighed by the fact that these entities are likely more willing to extend credit for a refinancing on a case-by-case basis if they can do so without automatically becoming subject to the HMDA reporting requirements.

The agency should also alter the requirement for lenders to guess an applicant's race or natural origin. Currently, if an applicant declines to answer the question, the loan officer is required to provide his or her best guess based on observation or the applicant's surname. Given the breadth and depth of data gathered under HMDA, it does not seem necessary to require lending officers to report their educated guesses. Further, many applicants may find such a guess offensive. Simply put, there is sufficient data to further the goals of HMDA without forcing lending officers to guess the race or national origin of applicants.

Regulation V

Regulation V, which implements the *Fair Credit Reporting Act* (FCRA) requires lenders making firm offers of credit to include certain opt-out disclosures. Specifically, 12 C.F.R. § 1022.54(c)(1) requires a “short notice” regarding opt-out rights. Additionally, 12 C.F.R. § 1022.54(c)(2) requires a “long notice” that includes some of the same information included in the short notice and some additional information. NAFCU recommends streamlining the notices and permitting institutions to provide a single disclosure.

It would also be helpful if the CFPB streamlined and simplified the adverse action notices required under Regulation B and the very similar risk-based pricing notices required under Regulation V. The FCRA and the *Equal Credit Opportunity Act* (ECOA) have virtually identical adverse action notice requirements. In addition, the FCRA has a very similar, but different, risk-based pricing notice requirement. Further complicating the issue, the FCRA’s adverse action notice requirements have no implementing regulation. In order to comply with the FCRA’s adverse action notice, creditors may use the model forms included in the Board’s Regulation B, which implements the ECOA. The rest of the FCRA, however, is implemented through Regulation V.

What’s more, the adverse action notice required by Regulation B and the risk-based pricing notice required by Regulation V are virtually identical and are given under similar – but not the same – circumstances. An “adverse action” notice is given if the consumer was denied credit or there was a change in terms of an existing credit arrangement. A risk-based pricing notice is provided to a consumer that receives credit, based in whole or in part on his credit score, on terms that are materially less favorable than the most favorable terms available to a substantial proportion of consumers.

The policy underlying the risk-based pricing notice is identical to the policy underlying adverse action notices (to inform consumers that lenders – or others – are examining their credit history). The content of the two different disclosures is virtually identical. The circumstances under which the disclosures must be made are very similar. Yet, lenders must look to two different regulations to determine how to comply. Further complicating the matter is that the Federal Reserve Board chose to implement most of the FCRA through Regulation V but chose to implement one discrete section (the adverse action notice requirement) through Regulation B.

This is a case where two closely linked issues that had the potential to be confusing have, indeed, grown incredibly complex as a result of the way in which the regulations were implemented. Understandably, some of the issues are a result of the way in which the underlying statutes were written. This is, however, an issue where the CFPB could simplify matters for financial institutions without any substantive change to the protections afforded consumers. NAFCU is not seeking fewer notices or less detailed disclosures. Rather, we only ask that the CFPB reconsider the way in which these closely

Consumer Financial Protection Bureau

March 2, 2012

Page 10 of 10

related statutes are implemented and re-write the regulations in a way that is simple and straightforward.

Conclusion

NAFCU appreciates the opportunity to provide input regarding regulations that can be modified or streamlined, and we very much appreciate the CFPB's decision to make this one of the first items on its regulatory agenda. Credit unions have been forced to contend with a significant number of regulatory changes over the last several years, particularly in regards to TILA and Regulation Z. We are hopeful that the CFPB will move forward and eliminate some of the less useful, redundant or unnecessary provisions in the regulations that it oversees. Should you have any questions or concerns, please feel free to contact me or Carrie Hunt, NAFCU's General Counsel and Vice President of Regulatory Affairs at 703-842-2234.

Sincerely,

A handwritten signature in black ink, appearing to read "Fred", written in a cursive style.

Fred R. Becker, Jr.
President/CEO