

The Dodd-Frank Bill Has Enormous Consequences for Community Banks

The Dodd-Frank Act will dramatically and negatively affect *all* banks – *large and small*. Some provisions will have a direct negative impact, such as the sheer volume of new regulations and new reporting burdens, many of which will flow from the new rules set by the Consumer Financial Protection Bureau (CFPB). There are other provisions which ostensibly provide some relief for community banks, but market competition and other unintended consequences may quickly reverse any “static” or “initial” savings. These include the loss of interchange income (despite an exemption from mandated, below market pricing for debit transactions). Here are some things to consider:

➤ *5,000 Pages of New Regulations*

Congress consistently underestimates the complexity and volume of the regulations resulting from new laws. Based on the number of pages of regulations resulting from previous laws, **the Dodd-Frank Act will result in more than 5,000 pages of new regulation for traditional banks.** This is in addition to the 50 new or expanded regulations affecting banks over the last two years.

➤ *Loss of Interchange Income on Debit Transactions*

Despite claims to the contrary, **community banks will be dramatically – and negatively – affected by the mandate that the Federal Reserve Board must set price limits on debit card interchange** (i.e., the small cost that retailers have to pay for the many benefits of processing debit card transactions). Currently, this **interchange revenue supports both the massive infrastructure necessary to sustain our incredibly efficient global payments system, as well as many everyday services banks offer to local consumers, like free checking accounts, basic banking services to low-income consumers, cost-free ATM withdrawals, fraud protection, and the like.**

With much of this revenue disappearing as a result of the legislation, these services are placed at risk and/or made more expensive for bank customers. In effect, Congress has merely transferred the cost of banking services from the likes of big-box retailers to everyday consumers. **While the legislation states that smaller banks have an exemption from the Federal Reserve price setting rules (meaning smaller banks prices would be higher than large bank competitors), that exemption will provide little or no benefit to community banks.** Since the use of smaller bank-issued debit cards would cost retailers more to process than those from larger bank competitors, there is an *enormous financial incentive* for retailers to drive business away from small bank cards to the lower-cost alternative offered by the big banks. This means community banks must lower their prices to those of their competitors or risk losing their customer base – and in doing so, community banks will face severe limits on their ability to offer local consumers low-cost services.

➤ *Consumer Financial Protection Bureau Rules Apply to All Banks*

All banks – *large and small* – will be required to comply with rules and regulations set by the CFPB, including rules that identify what the bureau considers to be “unfair, deceptive, or abusive.” The CFPB can require community banks to submit whatever information it decides it needs and the **CFPB can examine community banks** at its discretion on a “sampling basis.” Thus, the new legislation will result in enormous new compliance burdens for community banks and a new regulator looking over their shoulders.

Over

➤ *New Capital Standards*

All banks – including community banks – will be prohibited from using trust preferred securities to raise Tier 1 capital at their holding companies going forward. This will eliminate a popular source of capital that often is down-streamed to a bank. In addition, the agencies will be imposing more onerous capital rules on banks, large and small, and will force all banks to maintain higher levels of capital than expected in the past, thus reducing loan volume.

➤ *Precedent for Using the FDIC as a Government Revenue Raiser*

Both the increase in the insurance coverage levels and the last minute provision to raise the minimum level of the Deposit Insurance Fund to 1.35 percent were used as a way to **increase federal government revenues and meet the “pay-go” requirements**. Pay-go (or pay-as-you-go) rules require that any new spending must be offset by new sources of revenue so that there is no addition to the federal budget deficit. Premiums paid to FDIC are considered revenue to the federal government as FDIC is “on-budget.” **Thus, the actions set a precedent to use premiums as a revenue raiser to support other government spending programs.** It also undermines the integrity of the insurance assessment process and could ultimately undermine depositor confidence in the FDIC, as the fund will be seen as a political fund to be used for other purposes. Such an approach, in terms of its impact, is a tax on bank capital, and every dollar of bank capital serves as the basis for making loans of eight dollars or more.