

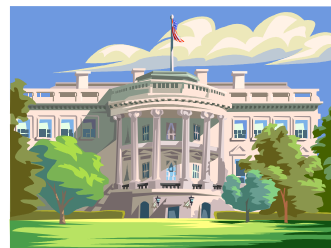
Community Bankers Association of Illinois



Summary of 2012 Federal Policy Priorities

The Community Bankers Association of Illinois supports fair competition in financial services, the separation of banking and commerce, state and federal regulatory and chartering choice, and a balanced financial system that does not bias one financial services sector over another. CBAI also opposes the concentration of economic and financial resources. Based on these principles, CBAI supports the following 2012 Federal Policy Priorities to help community banks better serve their communities and operate profitably and safely:

- **Support Passage of Community Bank Regulatory and Tax Relief Measures as Contained in the Bi-Partisan Supported Communities First Act (H.R. 1697 and S. 1600)**
- **Positively Influence the Implementation of the Dodd-Frank Wall Street Reform Act by Shoring Up, Defending, and Extending the Gains Made by Community Banks and Mitigating the Negative Effects of Adverse Provisions**
- **Downsize Too-Big-To-Fail Banks and Financial Firms Over a Five-Year Period**
- **Stop Overzealous Bank Regulatory Examinations**
- **Support Tiered Regulation and Supervision for Community Banks**
- **Support Positive Tax and Accounting Changes**
- **Support Mortgage Lending Reform**
- **Support GSE Secondary Market Reform**
- **Oppose Any Expansion of the Farm Credit System (FCS)**
- **Oppose Any Expanded Powers for Tax-Exempt Credit Unions**
- **Support Equitable Capital Rules for Community Banks**
- **Oppose Harmful Overdraft Program Regulations**
- **Maintain the Federal Home Loan Bank System**
- **Permanently Close the ILC Loophole**
- **Fairly Compensate Fannie Mae and Freddie Mac Preferred Shareholders**



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Detailed 2012 Federal Policy Priorities

Support Passage of Community Bank Regulatory and Tax Relief Measures as Contained in the Bi-Partisan Supported Communities First Act (H.R. 1697 and S. 1600)

Regulatory, tax, and paperwork requirements impose a disproportionate burden on community banks, thus diminishing their profitability and their ability to attract capital, support the credit needs of their customers, serve their communities, and contribute to their local economies. Credit unions and other nonbank financial institutions are not subject to the same laws and regulations as community banks. This places community banks at a competitive disadvantage and increases costs to consumers.

CBAI enthusiastically supports passage of the bi-partisan Communities First Act (CFA), which will relieve this disproportionate burden and lead to a more vibrant community banking sector. The Independent Community Bankers of America (ICBA) introduced this legislative initiative to include targeted regulatory and tax relief for community and rural banks, bank holding companies, municipalities, LLCs, small businesses, and individual savers.

CFA provisions include: extending the 5-year net operating loss (NOL) carry back; restoring bank reliance on external credit ratings; exempting high cost community bank originated mortgages that are held in portfolio from escrow requirements; lowering the origination and program fees for rural and small business borrowers; and permitting highly-rated and well-capitalized community banks to file short form Call Reports in two non-sequential quarters each year.

The original CFA was introduced several years ago and many of its original provisions have since become law. The current House and Senate bills enjoy strong bi-partisan support. **CBAI is pleased that Illinois Congressmen Mike Quigley (D-5th), Robert Dold (R-10th), Randy Hultgren (R-14th), Tim Johnson (R-15th), and Donald Manzullo (R-16th) are cosponsors of this important legislation (as of January 2, 2012).**

Positively Influence the Implementation of the Dodd-Frank Wall Street Reform Act by Shoring Up, Defending, and Extending the Gains Made by Community Banks and Mitigating the Negative Effects of Adverse Provisions

CBAI is working with regulators and legislators on implementation of the Dodd-Frank Wall Street Reform Act. The mortgage meltdown and ensuing financial crisis were so severe that Congress was determined to respond with a legislative reform measure. During the reform debate, community banks were actively engaged in the process and had a seat at the table during all phases of the discussions. This involvement served our interests well. Community banks earned 16 separate victories, carve outs and exemptions which would not have been possible by ignoring political reality and opposing all reform efforts.

Regulators are now 18 months into the rule-writing phase of implementation of the Act. CBAI's goal is to retain and strengthen those beneficial provisions and oppose and mitigate those provisions that are detrimental to Illinois community banks. The Act was certainly not perfect and much work remains to be done, including:

Rein in the Large Banks and Financial Firms

CBAI supports subjecting mega banks to rigorous regulatory scrutiny including higher capital and liquidity requirements. The Financial Stability Oversight Council's (FSOC) definition of systemically risky institutions must be very broad and include as many interconnected nonbank financial firms as possible. The contingency resolution plans required of large banks and financial firms are essential and must be credible and effective so that they provide regulators with tools for forced downsizing and the failure of institutions.

Level the Playing Field with Community Banks

CBAI enthusiastically supported the increase in FDIC insurance coverage to \$250,000 and the new rule implementing a change in the deposit assessment base calculation which positively impacted 98% of community banks and will save community banks an estimated \$4.5 billion over the next three years. The benefits of this change in the assessment base became effective in April of 2011.

CBAI also supports implementation of the provision in the Act to shield banks under \$10 billion in assets from FDIC insurance premium increases that will result from increasing the Deposit Insurance Fund (DIF) reserve ratio from 1.15% to 1.35%. In addition, CBAI supports the permanent extension of unlimited FDIC insurance coverage for noninterest-bearing accounts which expires on December 31, 2012.

Ensure that the Consumer Financial Protection Bureau (CFPB) Focuses On Large Banks, Financial Firms and the "Shadow" Financial Industry

In 2011, CBAI staff and Illinois community bankers met with Professor Elizabeth Warren of the CFPB, in both Washington, D.C. and Chicago, to urge the CFPB to focus on the true causes and real culprits of the mortgage meltdown and the financial crisis -- the largest banks in the country and the "shadow" financial industry.

The goal of the CFPB should be to hold the large bank and nonbank financial service providers up to the existing high standards for compliance with consumer laws, rules, and regulations currently required for community banks. Community banks should not endure any additional consumer regulatory burdens on top of the crushing burdens they already face on a daily basis.

CBAI supports a broad definition of non-depository "covered persons" subject to CFPB rules, examinations, and enforcement. The Association also encourages CFPB to use its authority to grant community and rural banks broad relief, thereby permitting them to serve the unique needs of their customers and not hinder new product development and innovation.

The CFPB has worked closely with community banks and consumers on the proposed consolidation of the Truth in Lending Act (TILA) disclosures and the mortgage disclosures required by the Real Estate Settlement Procedures Act (RESPA). These overlapping documents are difficult for attorneys, compliance officers, and even the regulators themselves to understand (not to mention customers). We congratulate the CFPB for thoroughly vetting these consolidated disclosure forms with valuable input from community banks and encourage this practice in the future as the Bureau proposes new consumer disclosures.

***Ensure that the Small Debit Card Issuer Exemption is Shielding Community Banks
from the Negative Effects of Debit Card Interchange Price-Fixing***

CBAI vigorously opposed the Durbin Amendment's Federal Reserve price-fixing of debit interchange fees partly because the Fed has no business regulating these private transactions. Also, in determining costs, the Fed was only permitted to consider the "reasonable and proportional" costs incurred by the issuer to authorize, clear and settle the debit transactions. Community banks know these are only part of the "true and actual" costs a bank incurs in offering and operating a debit card program. CBAI estimated that if the proposed rule was implemented the reduction in income would render many debit card programs unprofitable and unsustainable. Unfortunately, the Durbin Amendment was included in the Dodd-Frank Act.

Community banks, on the strength of more than 10,000 comment letters to the Fed, were able significantly change the initially proposed rule to include other legitimate costs in the debit card fee. The final Federal Reserve rule titled, Regulation II, Debit Card Interchange Fees and Routing, is an improvement over the proposed rule, but it remains a serious concern for CBAI. The concern is based on the fact that retailers are not passing on their interchange savings to consumers – and thus reaping windfall profits. CBAI is committed to determining whether the small debit card issuer exemption is indeed shielding community banks from the negative impact of debit card interchange price-fixing.

Community Bank Exemptions and Tiered Regulation

CBAI will continue to press for exemptions for community banks and tiered regulations as the regulators implement all aspects of the Dodd-Frank Act.

Downsize Too-Big-To-Fail Banks over a Five-Year Period

CBAI urges Congress and banking regulators to continue reforming our financial system and significantly reduce the probability and severity of a future financial crisis. The taxpayer bailout of big banks and financial firms must never happen again!

An unfortunate result of the financial crisis was that the largest banks in the country have only grown larger. In 2009, the four largest financial institutions controlled 56% of domestic banking assets (up from 35% in 2000), while the top 10 U.S. banks controlled 75% of domestic banking assets (up from 54% in 2000). The four largest banks also controlled a majority of the product markets for home mortgages, home equity loans, and credit card loans. These financial behemoths cannot be effectively managed, supervised, capitalized, or resolved and must be broken up or downsized over the next five years.

CBAI urges expansion of the Volker Rule to carve out business lines not essential to the basic business of commercial banking and for these lines to be spun off into separate firms.

CBAI also supports restoration of the Glass-Steagall Act (GSA) and the clear separation between banking and commerce. The GSA was breached by the Gramm-Leach-Bliley Act in 1999, and it took less than 10 years for the giant banks to incur enormous losses that triggered subsequent taxpayer bailouts and the Great Recession.

The "shadow" financial industry must also be regulated to the same rigorous extent as community banks. The "shadow" banks were a major contributor to the mortgage meltdown and the financial crisis and must be aggressively regulated to protect the economy and the taxpayer.

Stop Overzealous Regulatory Examinations

CBAI continues to express extreme concerns to bank regulators and Congress about overzealous bank regulatory examinations that negatively impact community banks' ability to serve their communities, lend to small businesses and individuals, and foster economic recovery. Overzealous bank regulators continue to contribute to community bank failures across America.

Public regulatory enforcement actions are being rained down on community banks. These public documents harm the banks' reputations in their communities, liquidity, and threaten survival. There are few if any public regulatory enforcement actions against the too-big-to-fail banks. This hideous double standard must end.

Examiners are unjustifiably requiring capital levels higher than the current standards and are inappropriately downgrading loans and forcing write downs. Regulators must take a longer-term view of real estate held as collateral and not demand excessive write-downs and reclassification of loans based on *forced sale* real estate values in dysfunctional markets.

CBAI supports legislation to reform the appellate process for agency decisions or actions and that would allow bankers to appeal to an independent ombudsman any adverse determination made by an examiner.

Restraint is needed from the most senior regulators in Washington down to the front-line examiners on Main Street in determining bank CAMELS ratings, publishing enforcement actions, and in community bank closures.

Support Tiered Regulation and Supervision for Community Banks

CBAI supports tiered regulation and examination for community banks. The financial crisis clearly demonstrated that the business model and risks of Wall Street mega banks and financial firms are very different from the business model and risks of Main Street community banks, and they should not be treated the same way. The Dodd-Frank Act laid out a plan for applying different and separate supervision, capital, and liquidity requirements for the financial behemoths. Now is the time to do the same for community banks.

For community banks, offsite monitoring should be used to a greater extent to track performance. Banks moving outside reasonable parameters could be flagged for increased regulatory scrutiny. There is no need to send teams of examiners into well-run banks for weeks at a time and then leave the banks wondering for many months about their CAMELS ratings. With regulator resources continuing to be significantly stretched, examiners should be put to better use at the larger and more complex banks and financial firms.

Support Positive Community Bank Tax and Accounting Changes

CBAI urges regulators, agencies, and Congress to support positive accounting changes that are focused on community banks and their individual and small business customers, and which support robust economic activity and foster savings and investments. These changes include the specific legislative proposals contained in the Communities First Act (CFA); opposing any bank-specific fees or transaction taxes; extending lower tax rates currently applied to individuals; Subchapter "S" income, dividends, and capital gains which are expiring in December of 2012; supporting community banks' ability to raise capital by issuing preferred shares; increase shareholder limits and allowing new IRA shareholder investments; and a permanent solution to real estate taxes to prevent a return to pre-2001 levels.

CBAI opposed the Financial Accounting Standards Board (FASB) proposed fair value disclosure that required parenthetical disclosures for all financial instruments (including mortgage loans) carried at amortized cost.

CBAI also opposed proposals by the Public Company Accounting Oversight Board (PCAOB) to amend and expand the scope of the independent accountant during the audit and mandatory auditor rotation. Also, when accounting or other standards are developed, exemptions should be provided for small financial institutions and the cost to community banks should not outweigh the benefit to the financial statement users.

In addition, CBAI supports allowing community banks to amortize CRE losses over 10 years. Currently, banks must recognize these loan losses in the year in which they are taken. This reasonable regulatory forbearance will strengthen the capital positions of many community banks and help them recover from the financial crisis. The proposal gives time for community banks to recover so they can continue to serve their communities. This reasonable forbearance could have saved scores of community banks that have failed since 2008, and there are nearly 900 banks on the FDIC's Problem Bank List that can still benefit from loan loss amortization.

Support Mortgage Lending Reform

Imprudent lending caused the mortgage meltdown and the financial crisis. Community banks are common sense lenders that did not participate in abusive and predatory lending practices. Proposals to curb these imprudent practices should not impact responsible lenders and loan products designed to meet the diverse needs of community bank customers including low-to-moderate income borrowers, borrowers in rural communities, and first-time homebuyers. Regulators should use their authority under Dodd-Frank to exempt community bank mortgage loans, including mortgage loans held in portfolio, from any unnecessary requirements or restrictions such as limits on balloon loans, escrow accounts for taxes and insurance, other loan terms and conditions, and prepayment penalties.

Regulators should not define "qualified residential mortgages" so stringently that thousands of community banks are driven from the residential mortgage market. Otherwise, only a handful of large banks and financial firms would dominate this market which constitutes a dangerous concentration of financial resources. Too narrow a definition will limit credit availability to many borrowers who do not have significant down payments or have unique circumstances.

Support GSE Secondary Market Reform

Community banks and our economy need the continued existence of a strong, impartial secondary market for residential mortgages that is financially strong and reliable. While Fannie Mae and Freddie Mac worked well for community banks, they are unlikely to survive in their current form. Recent events have demonstrated the need for some type of government ties to the secondary market to ensure the continued flow of credit. CBAI supports common sense reform of the housing GSEs that does not disrupt the fragile housing market and the economic recovery.

In the restructuring of the secondary housing markets the FHFA, Housing GSEs, and HUD/FHA should not develop or implement any rule or practice that would limit participation by community banks. There must be open and equal access by all lenders, regardless of size or volume, and loan pricing should be on equal terms with the largest mortgage originators. If the housing GSEs were to disappear and be replaced by the mega banks, community banks would become exposed to predatory pricing and cross selling tactics.

The conflicting requirements of a public mission combined with private ownership were a primary cause of the mortgage meltdown and must be eliminated. The reformed secondary market entities must have a limited mission and focus solely on supporting residential and multifamily housing.

CBAI recommends replacing Fannie and Freddie with privately capitalized cooperative entities, with a limited mission focused solely on supporting housing in all communities, and owned by the mortgage originators. Co-op members would benefit in terms of pricing regardless of their loan volumes. The co-ops would be governed by one-company-one-vote so larger institutions could not dominate. Directors would be appointed from various sized members and the co-ops would have an appropriate level of government support and oversight to ensure stability and market liquidity.

Oppose Any Expansion of the Farm Credit System (FCS)

CBAI adamantly opposes the expansionist agenda for FCS lenders. The FCS government-sponsored entity status and funding advantage constitutes an unfair competitive position over rural community banks.

The FCS should follow its historical mission of serving *bona fide* farmers, ranchers, and young, beginning and small farmers and their farmer-owned cooperatives. If it chooses not to follow this mission, it should be subject to taxation.

CBAI strenuously opposes the Farm Credit Administration's "Rural Community Investments" proposal which would allow FCS institutions to extend non-farm loans to virtually anyone in towns and cities with populations under 50,000; such financing would be misleadingly characterized as "investments" instead of loans.

FCS should be refocused as a wholesale funding source for community banks serving agriculture and provide a correspondent banking function rather than a direct retail competitor with its unfair GSE tax and funding advantage. FCS institutions should face regulatory safeguards, disclosures and controls equal to community banks and housing GSEs, including oversight by the CFPB.

Oppose Any Expanded Powers for Credit Unions

The credit union model has become outdated as credit unions have long since strayed from their original mission of serving individuals of modest means and with a common bond. Their federal tax-exempt status, in exchange for serving their original mission, is clearly no longer justified. Their tax subsidy should be eliminated and they should all pay their fair share.

Credit unions are now seeking to expand their commercial lending powers by increasing the percentage of assets cap on member business loans which will very likely come at the expense of tax-paying community banks. Credit unions should not be granted additional powers as long as they remain exempt from taxation.

CBAI supports applying Community Reinvestment Act (CRA) requirements to credit unions with the same asset size distinction as banks and thrifts.

CBAI supports the rights of a financial institution to choose the type of charter under which it operates and encourages credit unions seeking bank-like powers to convert to bank or thrift charters. In addition, CBAI supports legislation to prohibit the National Credit Union Association (NCUA) from using inappropriate means to prevent credit unions from converting to bank or thrift charters.

Given the current budget deficits and ever-growing federal deficit, together with surveys showing community banks actually do a better job serving the very customers that credit unions were created to serve, now is indeed the time for Congress to end the credit unions' unfair and unjustified tax subsidy.

Support Equitable Capital Rules for Community Banks

CBAI supports capital rules which do not disadvantage community banks relative to other financial institutions, which are not overly complex and represent a regulatory compliance burden, and which provide community banks with options to choose a capital framework.

CBAI strongly supports higher capital buffers and liquidity requirements for systemically risky financial institutions and is monitoring the recommendations of the Financial Stability Oversight Council and the Basel Committee on Banking Supervision.

CBAI opposes the inclusion of accumulated and other comprehensive income (i.e., unrealized gains and losses on securities held available-for-sale) in the calculation of Tier 1 regulatory capital due to the introduction of interest rate volatility on capital adequacy.

The 1.25% ALLL disallowance (for regulatory capital purposes) should be eliminated. Currently, banks are not allowed to use ALLL balances in excess of 1.25% of Risk Weighted Assets in their Tier 2 Capital. Elimination of this disallowance would encourage banks to reserve more and recognize the loss-absorbing abilities of the entire amount of the ALLL and would strengthen capital positions for hundreds of Illinois community banks.

Oppose Harmful Overdraft Program Regulations

CBAI opposes the additional regulatory burden placed on community banks by an uncoordinated regulatory response to perceived potential risks associated with overdraft programs (ODPs). The FDIC proposed Guidance independent of the other regulators which was later clarified to apply only to automated ODPs (not to ad hoc ODPs). The OCC proposed guidance noted that a small percentage of institutions are administering their ODPs without proper attention to risk. In a comment letter CBAI urged the OCC to table its proposed guidance and address the problems it perceives directly with those banks deemed not properly addressing those risks, rather than subjecting the entire banking profession to costly and burdensome new regulations.

Maintain the Federal Home Loan Bank System

The FHLBs have developed a strong partnership with community banks. FHLBs must remain a stable source of funding for community banks. The special functions and purposes of the FHLBs must be maintained.

Permanently Close the ILC Loophole

The Dodd-Frank Act imposes a three-year moratorium on new industrial loan company charters. CBAI urges Congress to completely eliminate the industrial loan company loophole in the Bank Holding Company Act and make supervision of bank holding companies uniform for all types of financial institutions.

Fairly Compensate Fannie Mae and Freddie Mac Preferred Shareholders

CBAI urges the restoration of Fannie Mae and Freddie Mac preferred share value and dividend payments. The abrupt action taken by then Treasury Secretary Henry Paulson to seize Fannie and Freddie through conservatorship was unjustly done in a way that needlessly wiped-out the value of GSE preferred shares, injuring thousands of community banks which purchased these AAA-rated investments at the encouragement of their bank regulators. It is imperative that community bank GSE preferred shareholders are made whole to bolster capital and lending to help support the fragile economic recovery.