THERE GOES THE NEIGHBORHOOD: REGULATING AWAY THE COMMUNITY BANK—AN ANALYSIS OF THE COSTS OF CURRENT REGULATIONS ON COMMUNITY BANKS

> *Modern finance is complex, perhaps too complex. . . . As you do not fight fire with fire, you do not fight complexity with complexity. Because complexity generates uncertainty, not risk, it requires a regulatory response grounded in simplicity. Less may be more.*
>
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I. INTRODUCTION

Before the recent barrage of broadcasts analyzing the "recession," a financial storm began to brew. Although many discredited early economic reports hinting at the possibility of an economic downturn, the United States economy continues to reel from the disastrous effects of the 2008 financial crisis. Nearly five years later, the United States' gross domestic product ("GDP")[1] remains stagnant, and regulators and banks continue to spar over the proper landscape for banking in the twenty-first century.

The terms financial collapse, recession, and economic downturn describe the recent economic event that continues to impact all Americans. For the first time since the 1980s, Americans dealt with a severe crisis that froze the historically abundant sources of credit and brought this country's economy to a grinding halt. After the dust settled and regulators began examining the causes of the crisis, Congress enacted legislation that authorized agencies to promulgate regulations. Many consumers' relationships with their banks deteriorated as a result of reduced credit despite attractive low interest rates for borrowers. This relationship was further challenged by the closure of community banks severing the personal service and relationships existing at the local level between client and personal banker. One such bank, the Tallapoosa branch of the People's Community National Bank, announced its closure in 2010 as a result of "excessive government regulations."[2]

Left unaddressed, the regulatory burdens facing community banks could regulate away their existence. As key providers of loans to small borrowers, including small businesses, community banks are a key driver behind job growth in the United States.[3] As of 2011, ninety-five percent of United States banking organizations were classified as community banks.[4] With increasing volumes of banking regulations, banks are using more capital to comply with voluminous and rapidly evolving regulations. The additional compliance cost includes the time spent by employees who are working more on compliance

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1 *See* U.S. BUREAU OF ECON. ANALYSIS, *Revisions to GDP, GDI, and Their Major Components*, SURVEY OF CURRENT BUSINESS, July 2011, at 9, *available at* http://www.bea.gov/scb/pdf/2011/07%20July/0711_revisions.pdf (explaining the new definition of GDP in terms of investment and savings).

2 In a 2011 newspaper article, the Tallapoosa branch of the Peoples Community National Bank announced that it was closing and transferring its accounts to the main branch of the bank. Kelly Quimby, *Bank Closing, Cites Tougher Regulations*, THE TALLAPOOSA JRNL., May 6, 2011, http://webcache.googleusercontent.com/search?q=cache:wZDCUvEt_6UJ:villa-rican.com/v. The bank's decision resulted from losses that the bank claims were caused by "excessive government regulations" stemming from the 2008 banking crisis. *Id.*

3 *See id.*

4 FED. DEPOSIT INS. CORP., FDIC COMMUNITY BANKING STUDY 2-9 (2012), *available at* http://www.fdic.gov/regulations/resources/cbi/report/cbi-full.pdf. Despite the high percentage of community bank charters, community banks only comprise roughly 12% of all bank assets. *Id.* at 2-7.

matters than on building client relationships. Additional time spent on regulatory compliance increases the cost of compliance and reduces hours available to focus on client relationships. This decreases the amount of a bank's loanable funds and decreases the opportunity to sell to bank customers. Coupled with low interest rates, this scenario greatly impacts the profitability of traditional loan and deposit banking services.

This Note argues that the Dodd-Frank Wall Street Reform and Consumer Protection Act[5] ("Dodd-Frank," "Dodd-Frank Act," or "the Act") adversely affects community banks by placing an undue regulatory burden on increasingly popular small banks.[6] By adopting an activities-based definition of "community bank" and by taking a principles-based approach to regulation, community banks can receive relief, while regulatory objectives are still achieved. At a time in history when consumers are turning away from "Big Banks," government regulation should not hamper economic progress and consumer choice.[7] Rather than impose added complexity to the regulatory environment, this Note evaluates the proactive nature of Dodd-Frank and the compliance costs of the regulation. Part II begins with an examination of the history of banking laws in the United States. Then, Part II discusses the role of the community bank and the development of banking regulations, accompanied by a discussion about the burdens facing community banks. This Part concludes with a discussion about the costs of regulatory compliance. Part III analyzes the impact of specific Dodd-Frank provisions on community banks and analyzes the policy motivations behind the Act with a discussion about more effective alternatives. Part III then concludes with a proposal for alleviating some of the burdens facing community banks while still ensuring consumer protection.

5 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

6 *See* Ben S. Bernanke, Chairman, Bd. of Governors of the Fed. Reserve, Speech at the Independent Community Bankers of America's National Convention and Techworld: The Financial Crisis and Community Banking (Mar. 20, 2009), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20090320a.htm (addressing community bankers' "fear" of regulations).

7 *See* Meg Handley, *Want Free Checking? Ditch the Big Bank*, U.S. NEWS AND WORLD REPORT (Mar. 15, 2012), http://www.usnews.com/news/articles/2012/03/15/want-free-checking-ditch-the-big-banks (arguing that consumers are flocking from big banks to community banks for (1) better rates on deposit and (2) lower account fees).

II. BACKGROUND

> *The structure of banking legislation and regulation might be compared to a stratified but active geologic formation: clearly identifiable separate levels are present, but these come into contact at various points, and sometimes collide.*
>
> *The FDIC, History of the Eighties–Lessons for the Future*[8]

The United States has had a storied banking history. A great deal of banking regulation in the United States was enacted in response to "'financial crises and other historical and political events.'"[9] The current regulatory environment still follows that same trend, and because the banking system was not designed according to a set of planned principles, regulations generally lack a proactive response.[10]

A. *The Adoption of a Central Bank and Its Progeny*

Banking regulation in the United States largely began with the Federal Reserve Act of 1913, which provided the centralized bank regulatory structure used today.[11] The first major banking collapse under the centralized banking structure occurred between 1930 and 1933.[12] Unlike the 2008 crash, the first banking crisis was caused by bank runs led by individuals, which led to the Great Depression.[13] In 1933, Congress responded with two large enactments: the Glass-Steagall Act and federal deposit insurance.[14] These enactments aimed to ensure that no crash like the Great Depression ever occurred again. As time passed, Congress' hard stance against banks softened. In 1956, Congress adopted the Bank Holding Company Act, thereby softening the Glass-Steagall

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8 FED. DEPOSIT INS. CORP., *Banking Legislation and Regulation*, AN EXAMINATION OF THE BANKING CRISES OF THE 1980S AND EARLY 1990S 87, 87 (1996), *available at* http://www.fdic.gov/bank/historical/history/87_136.pdf.

9 Leonardo Giani & Riccardo Vannini, *Toward an Evolutionary Theory of Banking Regulation: The United States and Italy in Comparison*, 29 REV. BANKING & FIN. L. 405, 406 (2010) (quoting KENNETH SPONG, FED. RESERVE BANK OF KANSAS CITY, BANKING REGULATION: ITS PURPOSES, IMPLEMENTATION, AND EFFECTS 5, 15 (5th ed. 2000)).

10 *Id.*

11 *Id.* at 416–17; *see* Federal Reserve Act of 1913, Pub. L. No. 63-43, 38 Stat. 251 (1913).

12 Giani, *supra* note 9, at 427.

13 *Id.* Bank runs refers to the situation where bank customers fear the insolvency of a bank and rush to take out their deposits, thereby, creating a "run on the bank." *Id.*

14 *Id.* at 429. Glass-Steagall separated commercial banking from investment banking and prohibited certain securities underwriting and dealing activities. Federal insurance for deposits aimed to prevent future bank runs by assuring the safety of depositors' savings, even in the event of bank failure. *Id.*

Act's division of commercial banks and investment banks.[15] In 1999, to complete the reversal of Glass-Steagall, Congress passed the Gramm-Leach-Bliley Act to promote competitive financial institutions and to provide assurance that the causes of the Great Depression would not resurface.[16]

Beginning in late 2007, the most recent financial crisis began to brew.[17] By the end of 2007, home values were steadily falling and job losses were accelerating.[18] The financial system had become so reliant on mortgage lending and the securitization and sale of those mortgages as derivative securities that most large institutions and many small institutions were affected.[19] Although the cause of the crash cannot be pinpointed to one specific factor, the cause is generally attributed to a highly leveraged, risk-taking culture amongst credit rating agencies and investment banks and the lenders that participated in creating subprime mortgages used in mortgaged derivatives.[20] For the first time since the Great Depression, Congress reversed its deregulatory attitude toward financial institutions and enacted the Dodd-Frank Act.[21]

Community bankers closely monitored Congressional enactments following the 2008 banking crisis. Before the enactment of Dodd-Frank, the American Bankers Association outlined key provisions in the Dodd-Frank bill that particularly troubled community bankers with respect to their ability to properly serve customers and to promote economic growth.[22] In a letter to the

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15 The Bank Holding Company Act of 1956 sought to limit the nonbank activities of holding companies and to promote bank competition. Note, *The Bank Holding Company Act of 1956*, 75 BANKING L.J. 277, 279–80 (1958). The Act primarily achieved the following five objectives:

> (1) a broader definition of bank holding company, (2) a virtually complete check upon interstate holding company expansion, (3) federal regulation of intrastate expansion, (4) a legislative decree that all holding companies within the 1956 act divest themselves of nonbanking voting interests, and (5) prohibitions against certain financial transactions between holding companies and their banks.

Id. at 281.

16 Giani, *supra* note 9, at 433. The Gramm-Leach-Bliley Act allowed commercial banks, investment banks, securities firms, and insurance companies to consolidate for the first time since 1933. The Gramm-Leach-Bliley Act also focused on consumer protection with its primary focus on consumer privacy. *Id.* at 434.

17 Charles W. Murdock, *The Dodd-Frank Wall Street Reform and Consumer Protection Act: What Caused the Financial Crisis and Will Dodd-Frank Prevent Future Crises?*, 64 SMU L. REV. 1243, 1245 (2011).

18 *Id.*

19 *Id.* at 1252.

20 *See id.* at 1279.

21 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

22 Letter from Stephen P. Wilson, Chairman of the Am. Bankers Ass'n, to Sheila Bair, Chairman of the Fed. Deposit Ins. Corp. (Mar. 21, 2010) (on file with author), *available at* http://www.aba.com/aba/documents/blogs/DoddFrank/ChairmanBairMar212011.pdf.

Chairman of the Federal Deposit Insurance Corporation ("FDIC"), the American Bankers Association outlined the following provisions: (1) debit-card interchange income cap, (2) the Bureau of Consumer Financial Protection, (3) increased capital standards, (4) new reporting and disclosure regimes, and (5) the qualified residential mortgage ("QRM") definition and risk retention requirements.[23] In opposition, government regulators, including the Federal Deposit Insurance Corporation, asserted that Dodd-Frank would bring numerous benefits to small banks.[24] Shortly thereafter, on July 21, 2010, President Obama signed the Dodd-Frank Act into law to end "too big to fail."[25]

Despite its mission to "end 'too big to fail,'" controversy over many other provisions in the Dodd-Frank Act soon arose.[26] President Obama asserted that the Dodd-Frank Act would "help foster innovation, not hamper it. It is designed to make sure that everybody follows the same set of rules, so that firms compete on price and quality, not on tricks and not on traps."[27] Not everyone in Washington, D.C., supported the act, however. The day after the bill was signed into law, House Minority Leader John Boehner stated, "[T]he financial regulatory bill that the [P]resident signed this week is just another big-government power grab that will make it even harder to create jobs."[28]

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[23] *Id.*

[24] FED. DEPOSIT INS. CORP., IMPACT OF THE DODD-FRANK ACT (DFA) ON COMMUNITY BANKS (Apr. 28, 2011), *available at* http://www.aba.com/aba/documents/blogs/DoddFrank/ FDIConDFAImpact.pdf. The FDIC identified the following changes pursuant to DFA that benefit community banks: "[1] the assessment base; [2] an increase in the deposit insurance fund reserve ratio; [3] insurance coverage; [4] ending 'Too Big to Fail'; [5] Sarbanes-Oxley [§ 404] exemptions; [6] capital rules; [7] consumer protections; [8] incentive compensation; and [9] the Volcker Rule." *FDIC White Paper: Dodd-Frank's Impact on Community Banks*, ABA DODD-FRANK TRACKER (Apr. 28, 2011), http://regreformtracker.aba.com/2011/04/fdic-white-paper-dodd-franks-impact-on.html.

[25] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010). "Too big to fail" refers to the concept that some organizations are "systematically important," such that their failure would exert such an influence on the economy that government support is required when such institutions face financial difficulty. *See* Catherine Rampell, *Defining "Too Big to Fail,"* N.Y. TIMES (Aug. 20, 2009), http://economix.blogs.nytimes.com/2009/08/20/defining-too-big-to-fail/?_r=0.

[26] *See* Murdock, *supra* note 17. At the signing of Dodd-Frank, President Obama remarked that the law would bring transparency to financial institutions and prevent another bailout.

Barack Obama, President, United States of America, Remarks by the President at Signing of Dodd-Frank Wall Street Reform and Consumer Protection Act (July 21, 2010), *available at* http://www.whitehouse.gov/photos-and-video/video/signing-wall-street-reform-and-consumer-protection-act#transcript.

[27] Obama, *supra* note 26.

[28] *See* Murdock, *supra* note 17, at 1247 (quoting *Reform Fannie and Freddie? Fuhgeddaboudit!*, JohnBoehner.House.gov (July 22, 2010), http:// johnboehner.house.gov/News/DocumentSingle.aspx?DocumentlD=199958).

Dodd-Frank, like other laws enacted during a crisis, has been both championed for its success and considered as a knee-jerk Congressional enactment.[29] Community banks particularly oppose the regulatory requirements of Dodd-Frank. As an opponent of certain Dodd-Frank regulations, Lynette Smith, President and CEO of Washington Gas Light Federal Credit Union, testified on behalf of the National Association of Federal Credit Unions at the House Financial Services Committee Subcommittee on Oversight and Investigations.[30] In her testimony, Ms. Smith expressed concerns about the viability of similarly situated community banks. Ms. Smith argued that community banks are not, in reality, exempt from many regulations despite falling below the $10 billion asset threshold allegedly designed to protect smaller community banks from certain regulations.[31] For community banks, much like larger banks, no single, isolated regulation arising under Dodd-Frank is the cause of current consternation. Rather, calls for help are seeking relief from "a death by a thousand cuts."[32]

B. The Role of the Community Bank

Colloquially, when describing a community bank, the images one conjures may vary based upon past banking experiences. At the most basic level, community banks operate as a form of financial institution with any number of branches.[33] Core services include full service loans and deposit products.[34] In addition, community bankers generally serve prominent leadership roles in the

29 For an article asking whether the Dodd-Frank Act will be considered as a "knee-jerk reaction," see Perry Skoutelas, *Dodd-Frank: 9,000 Pages But No Clear Answers*, FORDHAM CORP. L. F. (Nov. 26, 2012), http://fordhamcorporatecenter.org/2012/11/26/dodd-frank-9000-pages-but-no-clear-answers/. Some examples of laws enacted following a crisis include the Securities Act of 1933, the Securities Exchange Act of 1934, and the Glass-Steagall Act, which were all enacted during the Great Depression following the 1929 stock market crash. *See generally* Michael Perino, *Crisis, Scandal and Financial Reform During the New Deal* 2 (St. John's Legal Studies Research Paper No. 12-0004, 2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2054806.

30 Lynette Smith, President & CEO of Wash. Gas Light Fed. Credit Union, Testimony on behalf of The National Association of Federal Credit Unions at the House Financial Services Committee Subcommittee on Oversight and Investigations (July 19, 2012), *available at* http://financialservices.house.gov/uploadedfiles/hhrg-112-ba09-wstate-lsmith-20120719.pdf (urging Congress and Congressional Agencies to adopt simpler regulations and to apply a more thorough cost-benefit analysis before issuing regulations in order to place greater weight on consumer benefits).

31 *Id.* (Washington Gas Light Federal Credit Union had $86.9 million in assets at the time of the testimony.).

32 *Id.* (identifying burdens of the issuance of new, uncoordinated regulations and from meeting demands imposed by numerous regulators and more frequent bank examinations).

33 INDEP. CMTY. BANKERS ASSOC., COMMUNITY BANKING FACTS (Apr. 2012), http://www.icba.org/files/ICBASites/PDFs/cbfacts.pdf.

34 *Id.*

local community.[35] Community banks are staples in their communities and use local dollars to assist small businesses and consumers with everyday financial needs.[36]

A community bank's local presence translates to locally made decisions.[37] For lending decisions, community banks rely heavily on community knowledge and decide on more than a credit score alone. Community banks often consider "character, family history and discretionary spending in making loans."[38] This relationship lending model has allowed community banks to have a lower percentage of loan losses than noncommunity banks.[39] For many, the relationship banking model allows community banks to symbolize a lender of last resort for borrowers who were turned down by larger institutions.[40] In fact, community banks are the primary lender to small businesses.[41]

From a regulatory perspective, the term community bank is not uniformly defined. More precisely, definitions of community banks typically split into either an activity-based definition or an asset-based definition. An activity-based definition generally establishes the following factors to classify community banks: (1) the bank conducts its business within a limited geographic area, (2) the bank is primarily retail-funded, and (3) the bank has locally based decision makers.[42] In addition, community banks are often associated with high levels of personal service.[43]

Unlike the activity-based definition, regulators do not follow the same asset-based definition. Many definitions of "community bank" include an asset-based component, but that threshold varies. The St. Louis Federal Reserve Bank,[44] the FDIC,[45] and the Office of the Comptroller of the Currency

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35 *See id.* Community banks hold the majority of deposits in rural and micropolitan areas. FED. DEPOSIT INS. CORP., *supra* note 4, at I.

36 INDEP. CMTY. BANKERS ASSOC., *supra* note 33.

37 *Id.*

38 *Community Bank Advantages*, INDEP. CMTY. BANKERS ASSOC., http://www.icba.org/communitybanking/index.cfm?ItemNumber=556&sn.ItemNumber=1744 (last updated Sept. 29, 2013).

39 FED. DEPOSIT INS. CORP., *supra* note 4, at 4-6.

40 INDEP. CMTY. BANKERS ASSOC., *supra* note 33.

41 *Id.*

42 Gary S. Corner, *The Changing Landscape of Community Banking*, CENTRAL BANKER, Fall 2010, at 1, 8, *available at* http://www.stlouisfed.org/publications/pub_assets/pdf/cb/2010/CB_FALL_10.pdf.

43 *Id.*

44 *Id.* The St. Louis Federal Reserve study assigned $1 billion as the threshold, and the study noted that banks under $1 billion in assets possess most of the activity-based characteristics of a community bank. *Id.*

45 *See* FED. DEPOSIT INS. CORP., COMMUNITY BANKING BY THE NUMBERS (Feb. 16, 2012), *available at* http://www.fdic.gov/news/conferences/communitybanking/community_banking_by_the_numbers_clean.pdf; *see also* 12 C.F.R. § 345 (2013) (proposing to increase the asset

("OCC")[46] assign $1 billion as the maximum level of assets for community banks. In contrast, the Federal Reserve Board characterizes community banks as those with fewer than $10 billion in assets.[47]

In comparison to larger banks, community banks have more charters, but hold fewer assets and branches. Despite their smaller size, community banks play a key role in economic development by providing credit to small businesses.[48] By serving predominantly rural markets, community banks reach fewer customers geographically than banks located in urban areas. Further causing the disparity between large and small banks is the concentration at the top.[49] The four largest banks in the United States held 45% of total industry assets in 2011.[50] Noncommunity banks enjoy lower costs of capital than community banks.[51]

C. One Size May Not Fit All

Community banks differ from their larger rivals. This is not a recently developed idea, as the history of financial regulation has been riddled with divergent interests and changing regulatory policies.[52] Financial regulations have changed to adapt to financial innovation[53] and technological developments. Enactments have also changed to reflect overriding congressional policies with

threshold to $1 billion for the definition of a "small bank" in terms of the Community Reinvestment Act ("CRA")).

46 *See* OFFICE OF THE COMPTROLLER OF THE CURRENCY, COMMUNITY BANK SUPERVISION: COMPTROLLER'S HANDBOOK 1 (last updated May. 2013), *available at* http://www.occ.treas.gov/publications/publications-by-type/comptrollers-handbook/cbs.pdf.

47 Elizabeth A. Duke, Fed. Reserve Board Governor, Speech at the Community Bankers Symposium: Community Banks and Mortgage Lending (Nov. 9, 2012), *available at* http://www.federalreserve.gov/newsevents/speech/duke20121109a.htm. Immediately following the banking crisis in 2008, the Federal Reserve often used a $1 billion asset threshold to define community banks. *See* Bernanke, *supra* note 6.

48 *See* Bernanke, *supra* note 6.

49 FED. DEPOSIT INS. CORP., *supra* note 4, at 1-4.

50 *Id.* The four largest banks include Bank of America Corporation, Citigroup Inc., JP Morgan Chase & Company, and Wells Fargo & Company. *Id.*

51 *Id.* at 4–5.

52 *The Bank Holding Company Act of 1956*, *supra* note 15 (discussing divergent interests regarding Bank Holding Company Act with arguments spanning from 1933 to 1956); Randall S. Kroszner, *The Motivations Behind Banking Reform*, 24 REG. 36, 36 (2001) (discussing history of banking including industry rivalry and divergent interests of small versus large banks).

53 Financial innovation refers to innovation with respect to products, services, and delivery channels. Frances X. Frei et al., *Innovation in Retail Banking* (The Wharton Financial Institutions Working Center, Working Paper No. 97-48-B), *available at* http://fic.wharton.upenn.edu/fic/papers/97/9748.pdf.

respect to the financial sector.[54] In response to widespread bank failures of the 1920s and 30s, Congress enacted the FDIC at the opposition of many members of the American Bankers Association who felt the legislation pitted prudent, well-managed banks against those riskier banks that failed to adequately manage loans and deposits.[55]

Until the 1970s, states largely controlled the chartering of banks and severely restricted the number of branches a bank charter could have in order to raise more government revenue through bank chartering.[56] Today, banks with multiple branches are the norm, even amongst smaller community banks.[57] However, to become the norm, branch banking required societal and technological changes. As an example, throughout the 1970s and up until the mid-1990s, automated teller machines ("ATMs"), mail and telephone deposits, and reduced communication and transportation costs all contributed to the public convenience of branch banks.[58] As bank consolidation increased and as banks improved their economies of scale through technology, larger banks began relying upon credit-scoring.[59] Credit-scoring enabled larger banks to render quicker loan decisions without the same effort and expense of developing a relationship with the community and the customer.[60] In sum, this trend began devaluing the relationships and knowledge of community bankers.

The deregulated financial sector remained until the most recent financial collapse.[61] After the collapse, Congress responded with legislation to protect against the abuses of the deregulated financial sector.[62] The decision of Congress to increase regulations marks a change in the times and will dictate the future of the financial landscape.[63]

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54 *See* Nicholas Economides et al., *Federal Deposit Insurance: Economic Efficiency or Politics?*, 22 REG. 15, 17 (1999).

55 *See id.*

56 *See* Kroszner, *supra* note 52, at 38.

57 *Id.* at 37.

58 *Id.* at 40.

59 *See id.* at 41.

60 *Id.*

61 Luke A. Stewart, *The Impact of Regulation on Innovation in the United States: A Cross-Industry Literature Review*, INFORMATION TECHNOLOGY & INNOVATION FOUNDATION 19 (2010), http://www.iom.edu/~/media/Files/Report%20Files/2011/Health-IT/Commissioned-paper-Impact-of-Regulation-on-Innovation.pdf.

62 *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

63 *The Journey through Regulatory Reform: UBS Helps Clients Prepare for Dodd-Frank*, UBS (last updated Sept. 26, 2012), http://www.ubs.com/global/en/bank_for_banks/news/ topical_stories/edition_30.html.

D. *The Word on the Street: Community Banks are Suffering*

News reports continue to publish concerns for the viability of community banks. Bill Isaac, former FDIC Chairman and current Chairman of Fifth Third Bancorp, fears that Dodd-Frank is crippling small bank institutions.[64] Isaac takes particular issue with the "volumes and volumes of regulation" along with the Federal Reserve's stress tests, which require banks to hold enough capital for depression-era scenarios.[65] Isaac argues that while Dodd-Frank is aimed at the big banks that caused the crash, it impacts smaller banks, which cannot handle the additional regulatory burden.[66] Robert Fisher, President and CEO of Tioga State Bank of Spencer, New York, mirrored Isaac's comments.[67] Fisher argues that smaller banks like Tioga State Bank operate under a relationship banking model and that recently proposed CFPB mortgage rules only make sense for high-volume mortgage lending institutions without the intimate client relationship that many community banks have.[68] From Fisher's perspective, the CFPB's proposed mortgage rules apply best to "'Bank of America and the other mega-banks [that] operate on a transactional model.'"[69]

Douglas Manditch, CEO of Empire National Bank, reported that compliance costs in 2011 comprised nine percent of total revenues, much more than over a decade ago.[70] Manditch suggests that new compliance regulations threaten community banks.[71] To remedy the issue, Manditch argues for a resurgence of Glass-Steagall to divide commercial banking, investment banking, and in-

64 Michelle Fox, *Dodd-Frank Could Shutter Many Community Banks: Former FDIC Chair*, CNBC (Mar. 14, 2012, 9:07 PM), http://www.cnbc.com/id/46740719/Dodd_Frank_Could_ Shutter_Many_Community_Banks_Former_FDIC_Chair. Fifth Third Bancorp had over $112 billion in assets as of its 2011 year end. Fifth Third Bancorp, Annual Report (Form 10-K) (Feb. 29, 2012), *available at* http://www.sec.gov/Archives/edgar/data/35527/000119312512089474/ d305243d10k.htm.

65 Fox, *supra* note 64.

66 *Id.*

67 Carter Dougherty, *Small Banks Ask Break From Agency They Hoped Would Hurt BofA*, BLOOMBERG (Aug. 2, 2012, 2:45 PM), http://www.bloomberg.com/news/2012-08-02/smaller-u-s-banks-seeking-exemption-from-cfpb-mortgage-rules.html. Tioga State Bank operated eleven branches and had $387 million in total assets as of September 30, 2012. Tioga State Bank, Consolidated Reports of Condition and Income for A Bank with Domestic Offices Only (Form FFIEC 041) (Oct. 18, 2012), *available at* https://cdr.ffiec.gov/Public/ViewFacsimile Direct.aspx?ds=call&idType=fdiccert&id=9410&date=09302012.

68 Dougherty, *supra* note 67. The new mortgage rules were released as a 1,099 page document that the CFPB estimates will cost $100.1 million to implement. *Id.*

69 *Id.*

70 Interview by Fox Business with Douglas Manditch, CEO, Empire Nat'l Bank (Jul. 23, 2012), *available at* http://video.foxbusiness.com/v/1750390804001/is-dodd-frank-devastating-small-banks/.

71 *Id.*

surance.[72] Manditch suggests that such an enactment would increase competition and reduce or eliminate the "too big to fail" problem.[73]

Bankers are not just pontificating about the ills of Dodd-Frank; they view it as a legitimate, material business risk. A review of required annual Securities and Exchange Commission filings reveals that banks consider Dodd-Frank to be a business risk. A typical disclosure statement in a bank's annual report reads as follows:

> On July 21, 2010, President Obama signed into law the Dodd-Frank Act, which contains numerous and wide-ranging reforms to the structure of the U.S. financial system. Portions of the Dodd-Frank Act are effective at different times, and many of the provisions are general statements directing regulators to draft more detailed rules. Although the full scope of the Dodd-Frank Act's impact remains somewhat unclear, management expects that it will, over time, reduce revenue and increase expenses.[74]

Although bankers generally dislike all regulations, the regulatory challenges arising under the Dodd-Frank Act are different.[75] Annual report disclosures reflect the perceptions of management—Dodd-Frank is specifically identified and characterized as a business risk. To further support the notion that Dodd-Frank differs from earlier regulations, regulators are taking notice and beginning to seek opportunities for relief.

E. The Word with Regulators: Community Banks are Suffering

In 2012, at the height of an election year, regulators began to recognize the concerns of community banks. Regulatory agencies began holding discussions and conferences to discuss the impact of new regulations aimed at com-

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72 *Id.*

73 *Id.*

74 WesBanco, Inc., Annual Report (Form 10-K) (Feb. 29, 2012), *available at* http://www.sec.gov/Archives/edgar/data/203596/000119312512089544/d270388d10k.htm ($5.4 billion in total assets). *Compare* United Bankshares, Inc., Annual Report (Form 10-K) (Feb. 29, 2012), *available at* http://www.sec.gov/Archives/edgar/data/729986/000119312512087709/d260740d10k.htm ($7.8 billion in total assets), *with* Bank of America Corp., Annual Report (Form 10-K) (Feb. 23, 2012), *available at* http://www.sec.gov/Archives/edgar/data/70858/000007085812000155/bac-12312011x10k.htm#s866C648C2857A513A9EE698957CEDA3F ($2.1 trillion in assets).

75 *See* Esther L. George, President and CEO of the Fed. Reserve Bank of Kansas City, Speech at the Federal Reserve Bank of Kansas City's 2012 Community Banking Conference: Can Community Banks Still Compete? (Nov. 2, 2012), *available at* http://www.kansascityfed.org/publicat/speeches/2012-George-KansasCity-CommunityBanking-11-02.pdf.

munity banks.[76] Community bankers primarily voiced concerns about rewritten mortgage regulations by the CFPB and proposed capital requirements under Basel III.[77] At the November 2, 2012, Community Banking Conference at the Federal Reserve Bank of Kansas City, Esther L. George, President and CEO of the Federal Reserve Bank of Kansas City, addressed the conference about the impact of regulations and external market forces on community banks.[78] Ms. George recognized that community banks play a prominent role in serving American communities.[79] Ms. George concluded, however, that community banks are now facing a different type of regulatory challenge.[80] Some community banks are now forced to follow regulations aimed at large banks that are incongruent with the community banking model.[81]

Regulators are beginning to side with community banks in advocating that financial regulations apply to banks differently. On November 9, 2012, Federal Reserve Board Governor Elizabeth A. Duke addressed the Community Bankers Symposium in Chicago, Illinois. Governor Duke addressed two key regulations impacting community banks: (1) newly proposed mortgage issuer rules and (2) proposed capital requirements under Basel III.[82] Over the course of the 2012 summer, the Federal Reserve began "Ask the Fed" sessions.[83] Over 3,000 community bankers participated and provided input on proposed capital requirements.[84] In addition, the Federal Reserve began publishing a periodical entitled *Community Banking Connections*, dedicated to informing community bankers about common questions and issues raised by the community banking sector.[85] Through the Federal Reserve's comment periods for proposed capital

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[76] The FDIC conducted a yearlong study of community banks, which is available at http://www.fdic.gov/regulations/resources/cbi/report/cbi-full.pdf. The Federal Reserve conducted talks with community bankers and created an online resource known as Community Banking Connections, available at http://www.communitybankingconnections.org/. *See* Duke, *supra* note 47.

[77] *See* George, *supra* note 75. Basel III refers to the latest reform of measures set by the Bank for International Settlements ("BIS") designed "to strengthen the regulation, supervision and risk management of the banking sector." *International Regulatory Framework for Banks (Basel III)*, BANK FOR INTERNATIONAL SETTLEMENTS, http://www.bis.org/bcbs/basel3.htm (last visited Sept. 6, 2013).

[78] George, *supra* note 75.

[79] *Id.*

[80] *Id*. Community banks have overcome several challenges, including bank expansion laws, the removal of the interest rate cap, and changes in technology favoring large institutions. *Id.* The burdens under Dodd-Frank are different because, in many instances, the regulatory requirements aimed at regulating the activities of large banks apply the same to small banks. *Id.*

[81] *Id.*

[82] Duke, *supra* note 47.

[83] *Id.*

[84] *Id.*

[85] *Id.*

requirements, Governor Duke concluded that community banks view regulations as a threat to the viability of their business model.[86] According to Governor Duke, the data indicates that fewer community banks are entering mortgage lending than those that are abandoning mortgage lending to avoid the regulatory burden.[87] Governor Duke's analysis identified three burdensome effects of regulations on community banks: "(1) additional operational costs associated with compliance; (2) restrictions on fees, interest rates, or other forms of revenue; and (3) unintentional barriers to offering a service that are a result of regulatory complexity."[88] Governor Duke felt that the third element posed the greatest risk to community banks and that "the best course for policymakers would be to abandon efforts for a one-size-fits-all approach to mortgage lending."[89]

The FDIC recently developed a new definition of "community bank."[90] Realizing that a strict asset-based definition for classifying banks overlooks the many institutions that have over $1 billion in assets, the FDIC analyzed the community banking sector since 1984 to better assess the industry and its needs.[91]

III. CAUSES AND CURES REGARDING COMMUNITY BANKERS' ANGST

Currently, community banks are grappling with an increasing regulatory burden as a result of the Dodd-Frank Act. Arguably, the Dodd-Frank Act aims to implement a preventive measure to guard against another financial crisis. However, the Act merely expands upon former regulatory approaches, which failed to prevent the financial crisis. With volumes of new regulations and a plethora of regulatory uncertainty, community banks are spending on compliance and decreasing funds for investment. Although most regulations

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86 *Id.*

87 *Id.*

88 *Id.*

89 *Id.* Governor Duke's speech focused on mortgage lending, which comprises a large portion of community bank activities. *Id.* Governor Duke indicated that one-size-fits-all may be improper in other forms of regulation. *Id.*

90 *See* FED. DEPOSIT INS. CORP., *supra* note 4, at I (indicating that an asset-based definition can exclude certain entities that otherwise meet the criteria of a community bank); *see also* Joe Adler, *FDIC Seeks New Definition of Community Bank*, AMERICAN BANKER (Feb. 23, 2012, 2:25 PM), http://www.americanbanker.com/issues/177_37/community-banking-FDIC-failures-consolidation-1046899-1.html?zkPrintable=1&nopagination=1. In terms of the uniqueness of community banks, Richard Brown, the FDIC's chief economist, noted that "'[c]ommunity banks are three times more likely than other banks to be headquartered in a rural area or a micropolitan area, with populations between 10,000 to 50,000.'" *Id.* Community banks also tend to charge lower fees for deposit accounts than other larger banks. *See* INDEP. CMTY. BANKERS ASSOC., *supra* note 33.

91 *See* FED. DEPOSIT INS. CORP., *supra* note 4, at I.

face opposition, community banks oppose certain portions of Dodd-Frank with a well-founded basis for argument.

A. *Argument for a Uniform Activity-Based Definition of "Community Bank"*

Dodd-Frank was enacted "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail', [sic] to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes."[92] This quickly enacted legislation, however, fails to precisely distinguish banks based upon their activities. Although the Act addresses systemic risk, many provisions regulate community banks when such banks did not engage in activities that caused the financial crisis.[93] Because community banks operate differently than larger banks, imposing the same regulations on community banks adds to these banks' compliance costs without adding additional protection to the market. As a large number of community banks argue, the Dodd-Frank regulations punish community banks.[94] If the Act better defined "community banking" activities, better compliance relief could be afforded to community bankers.

Despite the efforts of the American Bankers Association and the Independent Community Bankers of America during the drafting of the Dodd-Frank Act, the political process of bill passage resulted with many community bank suggestions not being implemented.[95] Since its passage, Dodd-Frank has authorized the promulgation of volumes of regulations. As of 2011, 5,233 pages of proposed and final rules were issued as a result of Dodd-Frank.[96] Reports in 2012 indicated that the number of pages of rules and regulations promulgated

[92] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[93] *See* Bernanke, *supra* note 6; Stephen P. Wilson, Immediate Past Chairman of the Am. Bankers Ass'n & Chairman & CEO of LCNB Nat'l Bank, Remarks at the 22nd Special Seminar on International Finance: The Challenges to the U.S. Banking Industry Under the Dodd-Frank Act (Nov. 17, 2011), *available at* http://www.aba.com/aba/documents/news/WilsonTokyoSpeech111711.pdf).

[94] *See generally* Fox, *supra* note 64 (article interviewing community bankers about the impact of Dodd-Frank); Manditch, *supra* note 70 (interview with community banker about the high cost of regulatory compliance and desire for a separation between commercial and investment banking). Note that community banks largely did not contribute to the financial crisis. *See* Bernanke, *supra* note 6.

[95] *See, e.g.*, INDEP. CMTY. BANKERS OF AM., *Letters to Congress Archive*, http://www.icba.org/advocacy/lettershillarchive.cfm?sn.ItemNumber=3636&tn.ItemNumber=3649 (last updated Feb. 23, 2013) (see letters to Senators Dodd and Frank in 2009 and 2010 expressing key concerns about Dodd-Frank); Wilson, *supra* note 22; *see also* Wilson, *supra* note 93.

[96] *See* Wilson, *supra* note 93.

under the Act exceeds 9,000.[97] Although the Dodd-Frank Act carves out some exceptions for community banks, the primary exemption is an asset-based threshold of $10 billion.[98] The $10 billion threshold is the highest threshold used by any financial regulator. However, the threshold ends there; it contains no further threshold based on a bank's activities.[99]

As an example of the problems that arise with an asset-based definition, the FDIC's Community Banking Study illuminates the problematic miscategorization under such a bright-line rule.[100] In the study, 330 banks qualified as community banks that exceeded the FDIC's $1 billion threshold.[101] As for the $10 billion threshold, a total of 298 noncommunity banks fall below the threshold.[102]

Using the highest asset-based threshold fails to solve the problem. At the minimum, a community bank is a financial institution with fewer than $10 billion in assets, with the FDIC and the OCC using $1 billion in assets as the threshold.[103] Looking at the activities of community banks, an activity-based definition would define community banks as financial institutions that primarily earn profits from asset servicing and from the net interest margin.[104] Most of a community bank's operating capital is generated internally.[105] By adopting a more activity-based definition of community banks, regulations will more precisely conform to the activities of such entities.[106] As discussed in the sections below, an activity-based definition of community bank will better achieve and balance the policy objectives of financial regulation.

With regulators defining community banks differently, financial institutions between $1 billion and $10 billion are treated differently depending up-

97 Skoutelas, *supra* note 29.

98 *See* 12 U.S.C. §§ 5515–5516 (2012).

99 *See id*. With respect to consumer protection laws, the CFPB has exclusive authority to require reports and conduct examinations and has primary enforcement authority with respect to large financial institutions over $10 billion in assets. 12 U.S.C. §§ 5515(b)–(c). For smaller institutions, those with $10 billion or less in assets, the prudential regulator has enforcement authority. 12 U.S.C. § 5516(d).

100 FED. DEPOSIT INS. CORP., *supra* note 4, at 1-4.

101 *Id*.

102 *Id.* Of the 298 banks falling below the $10 billion threshold, only 92 had less than $1 billion in assets. *Id.*

103 *See supra* Part II.B.

104 FED. DEPOSIT INS. CORP., *supra* note 4, at 4-3.

105 *See id.* at VII.

106 *See id.* at I. The FDIC study noted that a strict $1 billion asset-based definition fails to account for industry growth and excludes larger entities that perform the same activities as community banks with under $1 billion in assets. *Id.*

on the regulator.[107] Despite the benefits associated with being a bright-line rule, strict asset-based definitions create three problems. First, the strict asset-based definition fails to most precisely group entities for the purpose of regulation. Second, an asset-based definition relies primarily on experience and statistics to categorize entities for the purpose of regulation.[108] This requires judgment to handle variations in the data and changes in the financial industry. Third, an asset-based definition requires updates to reflect changing values of the dollar and changes in the financial industry over time.[109]

An activity-based definition would better categorize banks for the efficient prevention of systemic risk that Dodd-Frank aims to achieve.[110] Admittedly, confidence in the safety and soundness of the banking system is of the highest importance, but a more detailed definition could better tailor protection against systemic risk while considering other policy factors.[111] For example, an activity-based definition of community banks could allow for an exemption from certain consumer protection regulations enacted in response to lending practices of large banks.[112] Primarily, an activity-based definition could exempt smaller community banks from regulations primarily derived from issues that occur most frequently at larger institutions. Although Dodd-Frank attempts a two-tiered regulatory model, a uniform activity-based definition for community banks would allow legislators and regulators an opportunity to better tailor regulations to community banks, thereby reducing the compliance burden.

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107 *See supra* Part II.B (The FDIC and the OCC use $1 billion as the asset threshold. The Federal Reserve Board, however, uses $10 billion as the threshold.).

108 *See* FED. DEPOSIT INS. CORP., *supra* note 4, at 1-1 to -2.

109 *Id.* As the financial environment changes and as values change over time, bright-line rules need updated to reflect inflation and other market changes. *Id.* Not every bank with over or under $1 billion operates in the same business line. *Id.* Some above the $1 billion threshold engage in the community bank activities typically associated with entities under the threshold. *Id.*

110 *See* 12 U.S.C. § 5383 (2012).

111 *See* ORG. FOR ECON. CO-OPERATION AND DEV., *Policy Framework for Effective and Efficient Financial Regulation* 18 (2010), *available at* http://www.oecd.org/finance/financialmarkets/44362818.pdf. The OECD is a forum of governments of thirty-four democracies that works to develop responses to economic, social, and environmental challenges of globalization. *Id.* at 2. The United States is a member of this organization. *Id.*

112 For instance, this could provide an exemption from proposed disclosure changes to the annual percentage rate ("APR") charged on high interest loans pursuant to the High-Cost Mortgage and Homeownership Counseling Amendments to the Truth in Lending Act ("TILA"), and Homeownership Counseling Amendments to the Real Estate Settlement Procedures Act ("RESPA"). The Independent Community Bankers of America argue that such a proposal would require extensive calculations for loans provided by community banks that would qualify as "higher-priced" because of the low interest rate environment. *See* Letter from Elizabeth A. Eurgubian, Vice President & Regulatory Counsel of Independent Community Bankers of America, to Monica Jackson, Office of the Executive Secretary, Consumer Financial Protection Bureau (Nov. 6, 2012) (on file with author), *available at* http://www.icba.org/files/ICBASites/PDFs/cl110612.pdf.

B. A Burdensome Combination

The regulatory burden associated with the Dodd-Frank Act takes three forms: voluminous regulations, regulatory uncertainty, and duplicative enforcement.

1. Voluminous Regulations

As of 2012, nearly 9,000 pages of regulations had been promulgated since the enactment of Dodd-Frank.[113] As of February 2013, only 148 out of the 398 required rulemakings had been finalized.[114] Also as of February 2013, 176 of 279 required rulemaking deadlines had been missed.[115] This regulatory scheme requires continuous attention to regulatory developments.[116] Out of fear of improper compliance through misunderstanding or failing to meet required deadlines, some community bankers are paying fees to outside advisors and assistants to perform compliance functions.[117] As regulations continue to increase, community banks' compliance costs increase.[118] With the median-sized bank employing an average of thirty-seven employees,[119] staying abreast of and complying with new regulations require a great deal of time and money.[120]

Dodd-Frank regulations impose a high cost of compliance in terms of time and money. In the aggregate, the House Financial Services Oversight Committee estimates that Dodd-Frank will require over 24 million hours each year from private industry to comply.[121] Federal agencies underestimate the total cost of compliance with these regulations. As an example, the CFPB omitted key data from its recent additions to the remittance transfer rule under Regula-

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[113] Skoutelas, *supra* note 29.

[114] For a monthly progress report on all required Dodd-Frank regulations, see *Dodd-Frank Progress Report*, DAVIS POLK, http://www.davispolk.com/Dodd-Frank-Rulemaking-Progress-Report/ (last visited Sept. 7, 2013).

[115] *Id.*

[116] *See* FED. DEPOSIT INS. CORP., *supra* note 4, at B-2 to -3.

[117] *See id.*

[118] Although the FDIC study noted that internal cost structures would be too costly to trace the compliance cost of each regulation, the aggregate direct cost of compliance increases with each regulation. *Id.* Compliance costs will be in the form of additional consultants or increased demands on internal workers. *Id.*; Smith, *supra* note 30.

[119] Wilson, *supra* note 93, at 3.

[120] *See* Smith, *supra* note 30.

[121] *Dodd-Frank Burden Tracker*, HOUSE COMMITTEE ON FIN. SERVICES, http://financialservices.house.gov/burdentracker/ (last visited Sept. 4, 2013); *Oversight of Dodd-Frank Act Implementation*, HOUSE COMMITTEE ON FIN. SERVICES, http://financialservices.house.gov/dodd-frank/ (last visited Sept. 4, 2013).

tion E.[122] By understating the hourly wage of compliance professionals, the estimated cost grossly distorts the true cost of compliance. "[T]he total [estimated] compliance cost for this one regulation [Regulation E remittance transfer rule] alone is roughly $225 million. However, if we use the median hourly wage rate for Dodd-Frank compliance (roughly $100), [actual] compliance costs climb to $760 million."[123] For comparison, the aggregate compliance cost for this one regulation nearly equals the $1 billion asset threshold used by many regulators.[124]

2. Duplicative Enforcement

In terms of duplicative enforcement of regulations, community banks do not have a clear vision of the future of bank regulation. With multiple independent agencies enforcing or interpreting the same laws, banks risk incongruent applications of the same laws depending upon the regulator. As an example, the CFPB seeks to streamline consumer protection laws and to promote safe consumer financial markets,[125] yet the CFPB is the current scapegoat of many financial institutions outraged over the current regulatory environment.[126] The complaints extend beyond policy arguments about consumer protection versus preference for bank profit.[127] Dodd-Frank authorized the CFPB to promulgate consumer protection rules and divided enforcement between the CFPB

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122 Sam Batkins, *What Does an Hour of Regulatory Compliance Cost?*, 35 REG. 11, 12 (2012), *available at* http://object.cato.org/sites/cato.org/files/serials/files/regulation/2012/8/v35n2-7.pdf#page=8 (last visited Sept. 4, 2013). As a part of the Paperwork Reduction Act ("PRA"), regulatory agencies must make a good faith estimate of hours that each regulation will require for compliance. *Id.* "Remittance transfer" includes consumer-to-consumer transfers of low monetary value that can be transferred through wire transfers or automated clearing house ("ACH") transactions. *Remittance Transfer Rule (Amendment to Regulation E)*, CONSUMER FIN. PROTECTION BUREAU, http://www.consumerfinance.gov/regulations/final-remittance-rule-amendment-regulation-e/ (last visited Sept. 4, 2013). Remittance transfers can contribute a fair amount to a bank's total revenues. *Id.* Each year, consumers in the United States send billions of dollars via remittance transfers. *Id.*

123 Batkins, *supra* note 122, at 12.

124 *See supra* Part II.B.

125 12 U.S.C. § 5511 (2012).

126 For a discussion with bankers about the impact of regulations, including the CFPB mortgage rules, see Dougherty, *supra* note 67. *See also* Kerri Ann Panchuk, *Community Banks Fear Weight of CFPB's Reach*, HOUSINGWIRE (June 26, 2012 3:07 PM), http://www.housingwire.com/articles/community-banks-fear-weight-cfpbs-reach. The "fear" of the CFPB stems primarily from uncertainty about the CFPB's wide ranging authority. *Id.* Banks mainly fear that the CFPB's regulations will lead to the disallowance of many bank products and services, including loans, that satisfy client demands. *Id.* With the elimination of each service or product, community banks lose a competitive edge.

127 Murdock, *supra* note 17, at 1249.

and prudential regulators.[128] For institutions with over $10 billion in assets, the CFPB has primary enforcement authority.[129] For institutions with $10 billion or fewer assets, which include community banks by any asset-based definition, prudential regulators[130] have enforcement authority.[131]

The consumer protection laws now under the authority of the CFPB were under the authority of the Federal Reserve Bank, the FDIC, the OCC, and the now defunct Office of Thrift Supervision ("OTS").[132] These agencies still have enforcement power over these consumer protection laws, but the CFPB now has the authority to promulgate regulations and to exercise enforcement power over the regulations.[133] Figure 1, *infra*, charts these regulations and their enforcement agencies. The CFPB can issue regulations for all institutions, and it can refer enforcement actions to prudential regulators to administer.[134] For rules enforced by prudential regulators, consumer protection regulations are still promulgated by the CFPB.[135] In addition, the CFPB has the power to submit a recommended course of action to the prudential regulators to enforce.[136] With a majority of consumer protection regulations dealing with lending, CFPB promulgations directly affect key products of community banks.[137]

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[128] The CFPB's administrative power is codified at 12 U.S.C. § 5581(b)(5)(B). For the division of enforcement power, see 12 U.S.C. §§ 5515(b)(2), 5516(b).

[129] 12 U.S.C. § 5515.

[130] Prudential regulator is defined in 12 U.S.C. § 5481(24) as "the appropriate Federal banking agency, as that term is defined in section 3 of the Federal Deposit Insurance Act . . . ." The appropriate Federal banking agencies include the OCC, the FDIC, and the Federal Reserve Board of Governors. 12 U.S.C. § 1813(q).

[131] 12 U.S.C. § 5516.

[132] *See* 12 U.S.C. § 1813(q). The OTS was merged into the OCC under Dodd-Frank effective July 21, 2011. These consumer protection laws include (1) unfair, deceptive, or abusive acts or practices; (2) Equal Credit Opportunity Act; (3) Home Mortgage Disclosure Act; (4) Truth in Lending Act; (5) Real Estate Settlement Procedures Act ("RESPA"); (6) Homeowners Protection Act; (7) Consumer Leasing Act; (8) Fair Credit Reporting Act; (9) Fair Debt Collection Practices Act; (10) Electronic Fund Transfer Act; (11) Truth in Savings Act; and (12) Privacy of Consumer Financial Information. 12 U.S.C. § 5512; s*ee also* CONSUMER FINANCIAL PROTECTION BUREAU, SUPERVISION AND EXAMINATION MANUAL–VERSION 2.0 (Oct. 31, 2012), http://www.consumerfinance.gov/guidance/supervision/manual/.

[133] *See Regulations*, CONSUMER FIN. PROTECTION BUREAU, http://www.consumerfinance.gov/regulations/ (last visited Sept. 4, 2013) (listing inherited regulations and regulatory actions). The enforcement power presides over institutions with over $10 billion in assets. 12 U.S.C. § 5515.

[134] 12 U.S.C. § 5512.

[135] *See id.*

[136] *See* 12 U.S.C. § 5516(d)(2)(A).

[137] Some recently finalized consumer protection regulations promulgated by the CFPB affect the Home Ownership Equity Protection Act, Electronic Fund Transfer Act, Home Mortgage Disclosure Act ("HMDA"), and Fair Credit Reporting Act Disclosures. *Regulations*, *supra* note 133. Proposed regulations affect the Truth in Lending Act, Real Estate Settlement Procedures Act,

3. Regulatory Uncertainty

With respect to regulatory uncertainty, bankers anticipate future regulations but are unsure of the impact of those regulations. Further, with multiple agencies enforcing the same consumer protection laws, bankers fear the impact of communication errors and disparities in the enforcement of such regulations.[138] In the example of the CFPB, the Dodd-Frank Act requires that large financial institutions provide reports to the CFPB for the purpose of consumer protection.[139] Reports from smaller institutions *may* be required by the CFPB, but there is no uniform reporting requirement for these banks.[140] These provisions complicate compliance matters in two ways. First, the word "may" indicates regulatory uncertainty, which stifles innovation and investment efforts.[141] Second, the risk of collecting data primarily from larger institutions ignores the unique qualities of the community banking model.

The regulations promulgated by the CFPB addressing mortgages have a greater impact on community banks. However, the CFPB gathers data for decisionmaking largely from noncommunity banks.[142] Arguably larger institutions have a greater quantity of customer transactions to analyze, but smaller institutions earn a larger portion of their profits from the regulated transactions and operate on a relationship banking model to make lending decisions.[143] Larger institutions, particularly those with more than $10 billion in assets, earn profits from other activities beyond the basic banking model. For some community banks, mortgage interest and service fees comprise the majority of bank profits. Community banks are impacted by the mortgage regulations promulgated by the CFPB, but community banks do not have the same input as noncommunity banks, which are less affected by the regulations.[144]

With multiple agencies enforcing the same consumer protection laws, banks must earn enough profit from these highly regulated activities to make

Integrated Mortgage Disclosures, and High-Cost Mortgage and Homeownership Counseling Amendments. *Id.*

138 *See* Wilson, *supra* note 22 (discussing the impact of communication problems with respect to debit card interchange rules proposed by the CFPB).

139 The CFPB has the exclusive authority to require reports and conduct examinations for the purpose of "detecting and assessing associated risks to consumers and to markets for consumer financial products and services." 12 U.S.C. § 5515(b)(1)(C) (2012).

140 12 U.S.C. § 5516(b).

141 *See infra* Part III.B.3.

142 *See* 12 U.S.C. § 5515(b)(1)(C).

143 *See* FED. DEPOSIT INS. CORP., *supra* note 4, at 1-1.

144 *See* Louise Bennetts, *Thanks to Dodd-Frank, Community Banks Are Too Small to Survive*, AMERICAN BANKER (Nov. 9, 2012, 12:00 PM), http://www.americanbanker.com/bankthink/thanks-to-dodd-frank-community-banks-too-small-too-survive-1054241-1.html?zkPrintable=1&nopagination=1 (discussing how noncommunity banks are less affected by consumer protection laws enacted by the CFPB).

the compliance burden worthwhile. For smaller institutions without a primary focus on mortgage lending, complying with newly promulgated mortgage regulations may prove burdensome enough to exit that business line entirely.[145] When those exiting the industry predominantly serve small businesses, access to credit decreases and economic growth staggers. The content of the new consumer protection rules is not necessarily the most problematic, but the volume of regulations and frequency of changes increase the cost of compliance and decrease the attractiveness of the community banking industry.[146]

With regulatory uncertainty and forthcoming volumes of regulations, financial products are becoming more streamlined. For any industry, innovation promotes competition.[147] In 2011, only three new community banks were chartered, compared with ninety-eight and thirty-one in 2008 and 2009, respectively.[148] In order to remain profitable under the new regulations, banks must operate efficiently and offer innovative products and services to attract and retain clients.[149] The current low interest rate environment reduces profit margins and increases the demand for efficiency and innovation.[150]

Admittedly, financial regulatory policy should favor consumer protection over protecting the profits of market participants.[151] However, regulators can protect consumers in different ways. Despite holding just fourteen percent of the total assets in the United States,[152] community banks play a vital role in the economy through lending to small businesses.[153] Because regulation will largely affect the future of community banks, a clearer and simpler regulatory scheme will reduce the uncertainty community banks experience.[154] Recognizing the unique role that community banks play will better address the needs of customers, community banks, and the financial system.[155] "In financial regula-

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145 *See id.*; *Dougherty*, *supra* note 67. *But see* FED. DEPOSIT INS. CORP., *supra* note 4, at B-2 (an interview of nine community bankers revealed that community banks had not changed business lines due to regulatory compliance burden).

146 *See* Smith, *supra* note 30.

147 *See* Stewart, *supra* note 61, at 1. See *infra* Part III.C, for further discussion about the role of innovation in the banking industry.

148 FED. DEPOSIT INS. CORP., *supra* note 4, at 2-7.

149 *Id.* at 4-7 to -10. The efficiency gap between community banks and noncommunity banks has increased dramatically since 1998 from 1.3% to 9.7%. *Id.* at 4-8. On average, community banks are less efficient than noncommunity banks. *Id.*

150 Reduced efficiency is signified by an increase in the efficiency ratio which is equal to noninterest expense divided by net operating revenue (noninterest income plus interest income). *Id.* at 4-7.

151 *See* ORG. FOR ECON. CO-OPERATION AND DEV., *supra* note 111, at 17.

152 FED. DEPOSIT INS. CORP., *supra* note 4, at 2-7.

153 Bernanke, *supra* note 6.

154 *See id.*

155 ORG. FOR ECON. CO-OPERATION AND DEV., *supra* note 111.

tion, less may be more. . . . Because complexity generates uncertainty, not risk, it requires a regulatory response grounded in simplicity."[156]

C. Increased Efficiency Through a Principles-Based Form of Regulation

Over the last fifty years, financial regulation in the United States has taken a rules-based approach and has increased in complexity.[157] Solving the next crisis cannot be accomplished by relying upon yesterday's data and approaches.[158] "Cutting back the thicket, re-sizing the haystack, could actually enhance transparency and bolster market discipline."[159]

Regulations generally divide into either a principles-based or a rules-based structure.[160] Principles-based regulations grant greater flexibility to regulated entities to determine the means for compliance.[161] Under a rules-based approach, entities must follow the same rules, which can often serve to micromanage the operations of a regulated entity.[162] With respect to financial regulation, rules-based regulations can stifle innovation where entities of the same caliber must conform to specific, detailed rules.[163] Under a principles-based regulatory scheme, entities are allowed greater flexibility to comply and, therefore, have greater freedom for innovation.[164]

The Dodd-Frank Act, despite its length, does not specifically prescribe exacting rules and guidelines for financial institutions. Largely, the Dodd-Frank Act prescribes directives to regulatory agencies, instructing them to promulgate additional rules. Such directives require the promulgation of nearly 400 additional rules and regulations.[165]Consumer protection regulations issued thus far have been rather specific about requirements.[166] As an industry, community

156 Andrew G. Haldane, Exec. Dir., Fin. Stability, Bank of Eng., & Vasileios Madouros, Economist, Bank of Eng., Speech at the Federal Reserve Bank of Kansas City's 366th Economic Policy Symposium, The Dog and the Frisbee 1, 19 (Aug. 31, 2012), *available at* http://www.bis.org/review/r120905a.pdf.

157 *Id.* at 9, 19.

158 *Id.* at 17, 19.

159 *Id.* at 17.

160 ORG. FOR ECON. CO-OPERATION AND DEV., *supra* note 111, at 26–27.

161 *Id.* at 26.

162 *Id.* at 27.

163 *Id.* The rules-based approach works best where tolerance for policy failure is low and where rules can likely be crafted to lead to a desired policy outcome. *Id.* However, rules can become outdated and can be misapplied or incomprehensive. *Id.* Rules can lead to rule avoidance or can become an exercise of ticking the box. *Id.*

164 *Id.* at 26.

165 Skoutelas, *supra* note 29.

166 Of the regulations added, the CFPB has issued regulations for administrative proceedings and regulations focused on additional required disclosures for consumers. *See Regulations*, *supra* note 133. Some regulations have been issued then delayed or subsequently amended. *See* 12

bankers recognize that future regulations are forthcoming pursuant to the Dodd-Frank Act.[167] Anticipating future regulations without any certainty as to their timing and exact scope, banks face a great deal of uncertainty.[168]

When the uncertainty about future regulations increases, businesses delay investment.[169] Furthermore, "[h]igher uncertainty and larger differences in the expected profitability of innovation investments will tend to stifle innovation."[170] Regulators should be mindful of the effects of regulations on markets and innovation.[171] "[C]ompliance uncertainty is unequivocally detrimental to innovation, and thus regulators should, of course, seek to minimize regulatory delay but also to enhance the clarity and coherence of regulation—for example, by avoiding overlapping authority across regulatory agencies."[172] Studies of economic regulation reveal that the best way to avoid stifling innovation is to take the "moving target approach."[173] For the United States to improve its innovativeness, regulation should be flexible and expedient.[174] Stringent regulations should be phased in over time, rather than suddenly adopted, to prevent market shock.[175] The Dodd-Frank Act's sudden impact of stringent regulations and the uncertainty surrounding future regulations have shocked bankers, stifled innovation, and slowed development of competitive community banks.[176] To avoid these negative consequences, a principles-based approach to regulation should be implemented.

D. Considering the Unique Operations and Needs of Community Banks

The Dodd-Frank Act was rapidly enacted following one of the worst financial recessions in United States history.[177] Justifiably, the Act sought to be a proactive regulatory measure "to end 'too big to fail" and to add transparency and consumer protection measures to the United States financial system.[178]

C.F.R. § 1026 (2013) (delayed implementation of mortgage disclosures under the Truth in Lending Act and the Real Estate Settlement Procedures Act); *see also* 12 C.F.R. § 1022 (second amendments to the fair credit reporting act).

167 *See supra* note 74 and accompanying text.

168 *See* Stewart, *supra* note 61, at 21.

169 *Id.*

170 *Id.*

171 *Id.* For a definition of "innovation," see Freil, *supra* note 53 and accompanying text.

172 Stewart, *supra* note 61, at 21–22.

173 *Id.* at 22.

174 *Id.* at 23.

175 *Id.*

176 *See* discussion *supra* Part II.D.

177 Perino, *supra* note 29, at 2.

178 Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. (2010).

However, Dodd-Frank is largely a reactive measure. Although Dodd-Frank prescribes several rule-making tasks to regulators, the Dodd-Frank Act does not specify precise guidelines for each regulatory entity. Instead, it predominantly establishes and authorizes regulatory agencies to issue regulations, without a limit beyond provisions to coordinate regulations between agencies.[179]

Innovation in the financial sector benefits consumers and financial institutions through custom-tailored products and additional banking service features.[180] Inflexible regulations hinder efforts to innovate, including those innovations most beneficial to consumers.[181] Fewer than thirty percent of all financial innovations resulted from regulations.[182] As the regulatory burden forces community banks to streamline products and spend more on compliance, community banks' ability to serve customers decreases.[183]

When compared against the policies behind financial regulation,[184] the Dodd-Frank Act does not, in reality, afford exemptions for community banks. When applying the same hierarchy of policy objectives as established by the Organisation for Economic Co-Operation and Development ("OECD"), confidence in the financial system receives top priority, but efficiency is a final consideration.[185] However, the OECD study indicates that financial policy can account for different sectors, institutions, or products.[186] Policy objectives and their priorities may differ based upon market failure analyses and economic and social considerations.[187]

Community banks are the primary lender of small businesses and often are the lender of last resort to many borrowers turned down by large institutions using computer loan models.[188] These institutions play a prominent role in the United States financial landscape, accounting for thirty-seven percent of the

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[179] *See generally* 12 U.S.C. § 5515(b)(2) (2012) (instructing the CFPB to coordinate its supervisory activities with other regulators).

[180] Stewart, *supra* note 61, at 19.

[181] *Id.* The study cites the example of Truth in Lending Act regulations that are overly specific, including specified typeface requirements for disclosures. *Id.* at 19–20.

[182] *Id.* at 19.

[183] *See* Bennetts, *supra* note 144 (discussing the impact of low interest rates and high compliance costs on the profitability of community bank lending).

[184] *See* ORG. FOR ECON. CO-OPERATION AND DEV., *supra* note 111, at 17. The OECD identified the following six policy objectives of financial regulation: (1) confidence in the financial system, (2) systemic stability, (3) safety and soundness of financial institutions, (4) market integrity and transparency, (5) market conduct and consumer protection, and (6) efficiency. *Id.* The OECD suggests establishing a hierarchy for these policy objectives. *Id.*

[185] *Id.*

[186] *Id.* at 18.

[187] *Id.*

[188] *See* FED. DEPOSIT INS. CORP., *supra* note 4, at 1-1 to -5.

branches in the United States.[189] With the goal of preventing "too big to fail," imposing high compliance costs favors the merger of financial institutions to consolidate the compliance burden.[190] Implicitly, the Dodd-Frank Act favors "too big to fail" institutions by imposing a regulatory burden that requires the resources of a large bank.[191] Instead of promoting competitive, transparent markets, the burdens of the Dodd-Frank Act are leading to fewer bank charters and less innovation.[192] Arguably, financial products today are more complex than in the deregulatory environment of the 1980s, but "complexity does not necessarily create risk."[193] Complexity merely requires an appropriate level of regulation.[194]

The United States economy is categorized as a free market enterprise.[195] Under this economic system, the "invisible hand" should guide the allocation of resources, and industry competition should regulate markets.[196] Examples from overregulated industries indicate that excessive government control opposes the underlying theory of the free market enterprise.[197] Instead of promoting free enterprise and innovation in finance and banking, Congress' lengthy Dodd-Frank Act began the stroke of many regulatory pens.[198] Instead of outlining the desired principles of the American financial system, Dodd-Frank adds voluminous, complex regulations to an industry abounding in regu-

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189 *Id.* at 1-4.

190 *See id.* at 2-1 to -12.

191 The concentration of total industry assets held by noncommunity banks has increased from 62% in 1984 to 86% in 2011. *Id.* at 2-7. The four largest banks (Bank of America Corporation, Citigroup Inc., JP Morgan Chase & Company, and Wells Fargo & Company) held 45% of total industry assets in 2011. *Id.* at 1-4.

192 In 2010 and 2011, fewer than ten new bank charters were approved, as compared to 175 approvals in 2007 alone. Craig D. Miller, *Small Banks' Ranks Will Dwindle Without New Charters*, AMERICAN BANKER (Mar. 20, 2012, 6:24 PM), http://www.americanbanker.com/bankthink/small-banks-ranks-will-dwindle-without-new-charters-1047701-1.html.

193 Brooke Masters, *Haldane Calls for Rethink of Basel III*, THE FINANCIAL TIMES (Aug. 31, 2012, 5:10 PM), http://www.ft.com/cms/s/0/8a5e61b2-f34a-11e1-9c6c-00144feabdc0.html#axzz2GYv5XRK7.

194 *See id.*

195 For a discussion about free market enterprise, see Kevin S. Marshall, *Free Enterprise and the Rule of Law: The Political Economy of Executive Discretion (Efficiency Implications of Regulatory Enforcement Strategies)*, 1 WM. & MARY BUS. L. REV. 235 (2010).

196 *See id.*

197 *See Over-regulated America*, THE ECONOMIST, Feb. 18, 2012, at 9, *available at* http://www.economist.com/node/21547789.

198 *Id*. At 848 pages, the Dodd-Frank Act is nearly twenty-three times longer than the Glass-Steagall Act enacted following the Great Depression. *Id.*; *see* Skoutelas, *supra* note 29.

lations. At a certain point, additional regulations fail to add additional protection against risk.[199]

Consumer protection and confidence in the financial system are certainly valuable goals but should be balanced with the impact on the financial institutions.[200] Overregulating financial institutions is an unfortunate byproduct of knee-jerk legislation.[201] As the Dodd-Frank Act continues to provide authority for greater and more complex regulations, the incentive declines to charter or continue a chartered community bank.[202] If this trend continues, the assets under control of the largest banks will increase and some smaller borrowers, such as small businesses, may lose access to the traditional bank credit.[203]

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[199] *See* Haldane, *supra* note 156, at 10.

[200] Educating consumers is another component of the CFPB's strategy to improve consumer protection. 12 U.S.C. § 5493(d) (2012). This is the second goal of the CFPB's strategic plan. *See Consumer Financial Protection Bureau Strategic Plan FY 2013-FY 2017*, CONSUMER FINANCIAL PROTECTION BUREAU, http://www.consumerfinance.gov/strategic-plan/ (last visited Sept. 6, 2013). Although more research is needed in this area to determine the most effective form of financial education, existing literature suggests that financial education improves the outcomes of a mortgage lending scenario. GENE AMROMIN ET AL., FINANCIAL LITERACY AND THE EFFECTIVENESS OF FINANCIAL EDUCATION AND COUNSELING: A REVIEW OF THE LITERATURE 22, 27 (2010), *available at* http://www.chicagofed.org/digital_assets/others/region/foreclosure_resource_center/more_financial_literacy.pdf; Susan E. Burhouse et al., *Banking on Financial Education*, FDIC Q., Second Quarter 2007, at 33, *available at* http://www.fdic.gov/bank/analytical/quarterly/2007_vol1_2/FDICQuarterlyV1N2_web.pdf (discussing benefits of federal *Money Smart* financial literacy program).

Greater efforts to understand and improve financial literacy could better tailor financial programs to consumers and alleviate certain detailed disclosure requirements imposed on all banks. *See* Stewart, *supra* note 61, at 19–20 (using specific typeface requirements as an illustration of disclosure-related burdens). This Author argues that a more effective regulatory scheme would begin with consumer education rather than a primary focus on financial institutions. Although disclosure provides transaction-specific information, consumers must be educated before entering a transaction, as educated consumers are better able to navigate the financial marketplace. Burhouse, *supra*, at 33. Admittedly, financial regulation should protect consumers from unscrupulous practices and unfair transactions, but overregulating an entity in the name of consumer protection can lead to market problems. *See supra* note 197 and accompanying text. An appropriate balance of regulation enacted on a moving target theory produces gradual innovation and steady market progress. Stewart, *supra* note 61, at 22–23. To date, by primarily focusing on reforming financial institutions, the Dodd-Frank Act has impacted financial markets and burdened many community banks, small business borrowers, and individuals in the process. *See* discussion *infra* Part IV.

[201] *See* Skouletas *supra* note 29 and accompanying text.

[202] *See* FED. DEPOSIT INS. CORP., *supra* note 4, at 2-1 to -12.

[203] The borrowers at issue are those largely served by community banks—small businesses and individuals located in rural areas.

The Dodd-Frank Act primarily divides institutions by the $10 billion asset threshold.[204] However, as discussed in Part III.B., *supra*, the consumer protection regulations promulgated by the CFPB affect the products and services offered by the CFPB. Despite the $10 billion asset threshold, community banks are not protected from the mounds of regulatory developments arising under the Dodd-Frank Act. Arguably, the Dodd-Frank Act achieves many of the policy objectives behind financial regulation. The ultimate goal of the Dodd-Frank Act prominently seeks to achieve (1) confidence in the financial system, (2) systemic stability, (3) safety and soundness of financial institutions, (4) market integrity and transparency, and (5) market conduct and consumer protection. As for efficiency, the Act attempts to coordinate regulatory agencies and streamline regulations, but the Act does not contain a provision to monitor the impact of the Act on the market. After nearly two years under the Dodd-Frank Act, regulators are beginning to take notice of the burdens faced by community banks.[205] Although members of Congress must act with regulators, the regulators' notice is a start.[206]

Of course, financial policy objectives and regulations do not necessarily need to account for the particular needs of each regulated bank. However, if regulations are reactive to a financial situation not caused by certain entities, should those entities, in the aggregate, be required to comply with the additional regulatory burden? Community bankers argue no. In the context of Dodd-Frank, some argue that Congress drafted certain provisions of the Act to be overinclusive as a means to prevent future abuses.[207] An analysis of the community banking model reveals that community banks differ substantially from the mega-banks largely responsible for the crisis[208] and should receive separate legislative treatment.

As a policy matter, regulations should promote consistency and market neutrality.[209] When regulations treat different market activities or participants

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204 The CFPB's administrative power is codified at 12 U.S.C. § 5581(b)(5)(B). For an example of the $10 billion threshold dividing the CFPB's enforcement power, see 12 U.S.C. §§ 5515–5516.

205 *See supra* Part II.E.

206 The FDIC's community bank study, which largely supports the position advocated by this Note, provides the preliminary data to better understand the community banking model. The Author recommends that members of Congress take notice of this study when enacting future financial legislation.

207 *See* Letter from Sec. Indus. and Fin. Mkts. Ass'n, to Dep't of the Treasury et al. 73 (June 10, 2011) (on file with author), *available at* http://www.fdic.gov/regulations/laws/federal/2011/11c64ad74.PDF (suggesting, in the context of collateralized debt obligations, that Dodd-Frank paints with too broad of a brush out of caution to prevent repeats of past abuses).

208 *See* FED. DEPOSIT INS. CORP., *supra* note 4, at I.

209 *See* ORG. FOR ECON. CO-OPERATION AND DEV., *supra* note 111, at 30. In this case, market neutrality refers to regulations that do not disadvantage one market participant over another.

the same, market neutrality is not achieved, which can lead to inefficient allocation of resources.[210] With community banks facing similar regulatory burdens as larger financial institutions, the Dodd-Frank Act creates inefficiencies and a non-neutral market. By imposing a similar regulatory burden on community banks, the Dodd-Frank Act puts community banks at a competitive disadvantage, which leads to fewer resources available to core bank functions.[211] If the competitive disadvantage continues, the number of smaller community banks will decline, with fewer banks overall and each bank holding a larger proportion of total industry assets.[212] Absent countervailing legislation, this scenario would result in fewer banks holding larger concentrations of assets, thereby perpetuating "too big to fail," rather than solving it.

E. Argument for Future Policy

A financial world free from all regulations would certainly contain risks that policymakers and the general public recognize and decline to accept. However, the current regulatory scheme may in fact inhibit economic growth and may swing too far in the opposite direction in the name of reducing risk. Undeniably, community banks serve an important role by serving the demands of individuals and small businesses.[213] Because of this role, community banks should continue their insistence for relief.[214]

To alleviate the burden faced by community banks, the most likely route would be legislative and regulatory adjustment. This poses two key issues: (1) what is the definition of community bank for purposes of the exemption and (2) how would regulators deal with a completely bifurcated regulatory scheme for community banks and noncommunity banks? Proceeding on the ba-

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210 *Id.*

211 Most community banks fund operations from internally generated capital and usually only seek external sources of capital, which is cheaper for noncommunity banks to obtain, in cases of financial difficulty or plans of growth. FED. DEPOSIT INS. CORP., *supra* note 4, at VII. Noncommunity banks experience even greater earnings potential through higher efficiency ratios due to their size, which enables them to more easily and cheaply comply with new regulatory burdens, such as the Dodd-Frank Act. *Id.* at 4-8.

212 For a discussion and data supporting this trend, see FED. DEPOSIT INS. CORP., *supra* note 4, at 2-4 to -7.

213 *See* Bernanke, *supra* note 6.

214 Admittedly, policymakers could decide that community banks no longer serve a valuable role in the financial services sector, and that a more highly concentrated banking sector would better serve the greater public interest. Canada and South Africa both have highly concentrated banking systems and are the world's soundest banking systems. Bennetts, *supra* note 144. However, the history of banking in the United States deems that decision an unlikely choice. *See id.*

sis that community banks serve a valuable and necessary financial services role, future regulations should address the needs of community banks.[215]

Currently, community bankers have an opportunity to continue expressing concerns with regulatory agencies.[216] With this opportunity, community bankers can influence the future of the community bank in the United States. Predominantly, community banks must continue to demonstrate the extraordinary cost of compliance with certain capital holding requirements and the burden of rapidly developing consumer protection regulations. Although additional exceptions to the law can often create loopholes and opportunities for regulatory evasion, community banks need relief. By advocating for a precise, activity-based definition of community bank, regulations will more equally impact community banks.[217] This relief can halt regulatory evasion of the community banking industry.

An ideal definition for exempting the community banks from consumer protection regulations would include the relationship banking model and an analysis of the bank's total asset size, client base, and loan portfolio.[218] Banks primarily serving small businesses and individuals by way of loan and deposit products, with little to no activity beyond these basic bank services, should qualify as community banks exempt from additional consumer protection regulations and enforcement by the CFPB. Indeed, the definition developed by the FDIC in its study of community banks includes these elements and provides additional factors to classify community banks based on a bank's focus on traditional lending and deposit gathering activities.[219]

By exempting community banks from certain regulations,[220] the burden of compliance is mitigated. The regulatory uncertainty can also be reduced by

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[215] As argued in this Note, community banks positively contribute to the American financial landscape. As noted in Part II.B, *supra*, community banks provide a valuable source of credit to borrowers denied by much larger financial institutions. These borrowers include most small businesses, the entities that provide a great deal of new job creation.

[216] *See supra* Part II.E.

[217] *See* Elizabeth A. Duke, Governor, Bd. of Governors of the Fed. Reserve, Speech at the Southeastern Bank Management and Directors Conference: The Future of Community Banking (Feb. 5, 2013), *available at* http://www.federalreserve.gov/newsevents/speech/duke20130205a.htm.

[218] As noted, in Part II.B, community banks largely operate under a relationship model of banking and rely less heavily on credit scores and ratings. By taking the time to better understand their borrowers, community banks implicitly educate their borrowers and better assess their creditworthiness. Additional consumer protection regulations do not necessarily change this banking model. Instead, additional regulations require additional capital and encourage institutions to increase in asset size, thereby decreasing the total number of institutions.

[219] FED. DEPOSIT INS. CORP., *supra* note 4, at 1-1 to -5.

[220] This Author does not opine that community banks should never be regulated. Simply, the design of Dodd-Frank paints with too broad of a brush and subjects community banks to imprecise regulations that were designed to prohibit practices largely committed by noncommunity banks.

requiring regulatory entities to more clearly express regulatory plans. By more clearly expressing its intentions, a regulatory agency can reduce the kind of regulatory uncertainty that community banks are currently facing, which costs banks and the public at large.[221]

An ideal financial regulation balances the six main goals of financial regulation.[222] The six goals of financial policy can be thought of as factors in an equation equal to the model financial policy. By reducing the emphasis on consumer protection and increasing the focus on efficiency, markets improve, and capital access increases. Although policymakers must address the misdeeds that gave way to the financial crisis, heavy-handed regulations that further inhibit economic recovery do not serve in the best interest of the public when those regulations are misapplied to the banks that did not play a role in the crisis. By advocating for relief from burdensome financial regulation, community bankers advocate for economic recovery and improved access to capital. If the Dodd-Frank Act truly aims to "end 'too big to fail,"[223] then regulatory efforts and legislation should more specifically apply to noncommunity banks. Such clarifying revisions to the Dodd-Frank Act and to its regulations would serve this interest.

IV. CONCLUSION

Community banks play an integral role in economic growth and are pivotal in providing access to credit for small businesses. Regulations serve to police markets and to promote fairness and transparency in the marketplace. In the United States, regulation is theoretically contrary to Adam Smith's invisible hand.[224] The Dodd-Frank Act seeks to advance a proactive mentality aimed at preventing another catastrophic financial collapse like the one experienced in 2008. Despite the goals of this legislation, this Act has strained community banks with voluminous regulation, duplicative regulatory enforcement, and regulatory uncertainty. Although regulation has created new industries of compliance professionals, it stifles innovation and causes uncertainty.

At a time when consumers require access to capital but are underserved by noncommunity banks, community banks, functioning as lenders of last re-

221 This cost to banks is in the form of compliance burdens and frequently changing regulations. Consumers feel the burden indirectly by less available credit, which means less access to credit. For small businesses, access to credit is essential and is a key driver of economic growth.

222 *See supra* note 184 and accompanying text.

223 Dodd-Frank Wall Street Reform and Consumer Protection Act, H.R. 4173, 111th Cong. (2010).

224 Adam Smith was a Scottish economist best known as the author of *An Inquiry into the Nature and Causes of the Wealth of Nations. Introduction*, ADAM SMITH INST., http://www.adamsmith.org/adam-smith (last visited Sept. 6, 2013). The invisible hand theory posits that social order need not be controlled because social order "grow[s] best in an open, competitive marketplace." *Id.*

sort, are closing operations due to compliance burdens. With fewer banks, consumer choice declines, and available resources are not used most efficiently. By adopting a uniform, activities-based definition of "community bank," regulations and legislation would better protect the interests of community bankers who did not cause the financial crisis. By focusing regulations on principles rather than rules, free markets have flexibility. This flexibility promotes community bankers' relationship model of banking, which provides better consumer protection without regulatory disclosure requirements. Instead of embracing the unique operations of community banks, the Dodd-Frank Act and its many regulations seek to streamline products and are doing so at the cost of greater uncertainty, reduced efficiency, and slower innovation. Despite the need to address the misdeeds that caused the financial crisis, Dodd-Frank impairs economic growth by overregulating small borrowers' primary lender—the community bank.

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Appendix

Figure 1: Dual-Agency Enforcement Authority of Regulations[225]

Safety and Soundness				
	CFPB	Federal Reserve	FDIC	OCC
FIRREA Appraisal Requirements	Yes	Yes	Yes	Yes
Loans to Insiders (REG O)	No	Yes	Yes	Yes
Regulatory Examinations	Yes	Yes	Yes	Yes
FDICIA	No	Yes	Yes	Yes
Formal Written Policies	No	Yes	Yes	Yes
Consumer Protection				
	CFPB	Federal Reserve	FDIC	OCC
Real Estate Settlement Procedures Act	Yes	Yes	Yes	Yes
Community Reinvestment Act	No	Yes	Yes	Yes
Expedited Funds Availability Act	No	Yes	Yes	Yes
Truth in Lending Act	Yes	Yes	Yes	Yes
Equal Credit Opportunity Act	Yes	Yes	Yes	Yes
Home Mortgage Disclosure Act	Yes	Yes	Yes	Yes
Other Regulatory Requirements				
	CFPB	Federal Reserve	FDIC	OCC
Call Reports	No	Yes	Yes	Yes
Bank Holding Company Reports	No	Yes	No	No
Bank Secrecy Act	No	Yes	Yes	Yes
IRS Reporting	No	No	No	No

[225] In Figure 1, the categories of regulations were modeled after a 1993 Report to the Senate Committee on Banking that identified regulatory burdens facing bankers. *See* U.S. GEN. ACCOUNTING OFFICE, GGD-94-28, REGULATORY BURDEN: RECENT STUDIES, INDUSTRY ISSUES, AND AGENCY INITIATIVES 6 (1993), *available at* http://www.gao.gov/assets/220/218925.pdf. Figure 1 compiles laws enforced by current regulators. *Regulations*, *supra* note 133 (listing inherited regulations now under CFPB enforcement); *Regulations: All Regulations*, BOARD OF GOVERNORS OF THE FED. RES. SYS., http://www.federalreserve.gov/bankinforeg/reglisting.htm (last updated Sept. 4, 2013); *FDIC Law, Regulations, and Related Acts*, FEDERAL DEPOSIT INSURANCE CORPORATION, http://www.fdic.gov/regulations/laws/rules/index.html (last updated July 26, 2013); OFFICE OF THE COMPTROLLER OF THE CURRENCY, COMMUNITY BANK SUPERVISION: COMPTROLLER'S HANDBOOK (last updated Sept. 2012), *available at* http://www.occ.treas.gov/publications/publications-by-type/comptrollers-handbook/cbs.pdf.