BANKTHINK
INFORMED OPINION

Complex Consumer Protection Laws Keep Small Banks from Serving Unbanked

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Access to basic banking services allows individuals and families to build a solid financial foundation by safely granting the opportunity to conduct transactions, save, borrow, and invest. But, according to the 2011 Federal Deposit Insurance Corp. National Survey of Unbanked and Underbanked Households, more than 34 million Americans lack access to banks or are not fully participating in the mainstream financial system.

As part of another survey from the FDIC, banks were asked whether the overall regulatory environment was an obstacle in offering products and services to the unbanked and underbanked. Respondents were asked about specific regulatory topics, including know-your-customer rules, Bank Secrecy Act/anti-money laundering requirements, fair lending and compliance rules and third-party relationship risk. One-third of banks said the overall regulatory environment was a major obstacle to serving the unbanked and underbanked.

To those of us watching consumer compliance regulation evolve over the last decade, it comes as no surprise that we have reached a time when many industry participants, small banks in particular, are giving up on offering and developing products geared to this demographic. As the rules have grown more complex and profit margins have shrunk, community banks must now balance their willingness to develop products that could assist underserved members of the community against the perceived regulatory risks.

Regulations and supervisory processes that drive financial services out of the mainstream banking system into the shadows need to be rooted out and made more reasonable. As it stands, these laws are numerous and complicated. For instance, the Federal Financial Institutions Examination Council highlighted 15 laws and regulations in its recently issued guidance on social media. How can we honestly expect small banks to offer innovative products to meet the needs of the underserved population if they are required to wade through 15 laws and regulations just to tweet?

Policymakers need to abandon the one-size-fits-all approach to compliance rule-writing and supervision. A compliance regimen that recognizes the proximity of the community banker to their customer and the alignment of financial interests resulting from the "originate-to-hold" model employed by community banks is long overdue.

At the 2012 Community Bankers Symposium in Chicago, Federal Reserve Governor Elizabeth Duke indicated her support for a two-tiered approach to regulating mortgage lending. The Consumer Financial Protection Bureau recently proposed a rule related to small creditor qualified mortgages that confers added legal protections to mortgages held in portfolio by creditors with assets of $2 billion or less and who originate fewer than 500 mortgages a year. Duke and the CFPB are on the right track with this line of reasoning. It is clear that more needs to be done to reduce the compliance burden of community banks to allow them to fully serve their communities.

The fact that nearly one-third of banks cited the overall regulatory environment as a major obstacle should be reason enough to reevaluate the way we promulgate and enforce compliance regulations. Beyond the laws themselves, many times the interpretation of statutes, the rule-writing and the subsequent examination processes create more challenges. Who are we trying to protect if it is not those individuals that would benefit most from the services of banks on Main Street?

After all the changes to consumer protection laws in recent years, it seems unfortunate that the very rules meant to protect consumers may actually serve to exclude the most vulnerable individuals from affordable banking services.

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