

Capital Sources

New legislation comes at expense of banking industry

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By: Wayne Tompkins

The Obama administration is gaining a reputation as the most favorable to banking consumers in perhaps a generation - and got a big assist last week when the Federal Reserve announced major new restrictions on how banks can charge overdraft fees.

For the banks themselves, already struggling under the weight of bad loans and poor economic conditions, last week's announcement and a number of other new or proposed regulations are collectively placing even more stress on the system.

"I think we'll see a number of banks, not necessarily the troubled ones that we know about, just throwing up their hands and saying, 'We're for sale. We just can't deal with these increasing regulations, these issues,' " said Ken Thomas, an independent banking analyst based in Miami. "We have not had a pro-consumer view in Washington in many, many years."



Dennis Nason

Some in the banking industry say this is far from the best time for institutions struggling to stay profitable to bear the added burden and costs of myriad legislation.

"It's a little bit of a push back on the part of the general public," said Dennis Nason, a Coral Gables consultant and veteran international banker. "The biggest uncertainty is that we've got three different bills, they're being sponsored by people not familiar with the system and the banks are being hit with all kinds of charges on top of the losses. So it makes the banking business less attractive."

While last week's changes prohibiting banks from charging overdraft fees on ATM or debit cards - unless a customer has agreed to them - is the "sexiest" of the new mandates banks are saddled with, Nason said other changes on the horizon are likely to have a bigger effect on the industry in the coming months.

"One of the more difficult things for the banks is the FDIC fees that they're going to have to come up with," Nason said, referring to the premium banks must pay to cover the costs of failed institutions. "What they're going to have to do by the end of the year is pay not only this year's quota but the next three years' quota."

The FDIC hopes to raise \$45 billion under the plan to replenish the deposit insurance fund in the wake of more than 120 bank failures this year.

ACCOUNTING CHANGES

Nason said the second issue is the adjustment to accounting changes in the mark to market arena and "being able to understand what you can and can't do. The banks all have real estate problems. They're not quite sure how to value them and mark them down."

Also looming are a number of major financial bills in Washington which, if approved, could transform the agencies that regulate the industry and add additional consumer protections including changes to the Community Reinvestment Act.

The chairman of the Senate Banking Committee, Christopher Dodd, D-Conn., introduced legislation earlier this month to strip the Federal Reserve of authority to regulate banks in favor of Congress, whose own appointed officials would set interest rates. The bill would also create a Consumer Financial Protection Agency.

While much of this legislation is introduced perennially and may never become reality, populist sentiment against the banking industry gives such proposals a political momentum they have not enjoyed in years. The problem is banks enter the year not knowing which changes will actually become law.

"One of the things banks like to do is try to figure out what the playing field is and then plan for next year and I think what is bothering the banking industry more than anything else, is their inability to look at the business from a logical planning standpoint," Nason said.

Thomas said the proposals, and the costs and staffing requirements that would come with them, are threatening to hit as "many of them are just trying to stay above water and basically deal with their problem loans."

He said while that new regulations would be a hit to profitability, he agrees that there's likely to be little public sympathy for the banking industry.

"It's going to increase the cost to bankers," Thomas said. "But I think it's a longtime coming when you see some of the abuses that not all, but some of the big banks, have engaged in. For example, basically lining your checks up in such a way as to hit you with the maximum overdraft charges."

FRIEND IN CONGRESS

Cyril "Sid" Spiro, chief executive of Davie-based Regent Bank, said one unlikely congressional ally for community banks is U.S. Rep. Barney Frank, D-Mass., the chairman of the House Committee on Financial Services. Though usually perceived as one of the more liberal members of Congress, Frank has written in a letter to regulators that problems in the banking system did not originate with the community banks.

"'Bank' became a generic term, without really making distinctions between commercial banks, thrifts and the shadow banking system - which is really the investment banks, the mortgage banking companies, etc.," Spiro said. "Most of the problems with subprime and so forth were outside the commercial banks and yet we have all of this proposed legislation that is slamming the hell out of the commercial banking industry, which was not the problem area."

Spiro said his guess is that Dodd's proposals will get weakened, given the power of the community banking lobby in Washington.

"So many congressmen come from communities where the prominent financial institution is a local community bank," Spiro said. "Just like we're seeing with health care, most of these proposals end up getting watered down."

While it may not be the biggest regulatory challenge facing the banking industry, the new overdraft regulations marked a well-publicized victory for consumer advocates used to being steamrolled by years of industry-friendly lobbyists and legislators.

The industry raised a collective \$37 billion from overdraft fees last year, according to Moebs Services, an Illinois-based research firm.

Beginning July 1, banks and other financial companies will be required to explain overdraft programs and fees and choices available to consumers.

"The final overdraft rules represent an important step forward in consumer protection," Federal Reserve chairman Ben Bernanke said in a statement. Consumers who decline overdraft protection may be denied access to cash at an ATM or have their debit-card transactions rejected.

Fed consumer research shows "most consumers prefer not to be enrolled in overdraft services for ATM and one-time debit-card transactions unless they affirmatively consent," the board said in its statement.

"We've always viewed the overdraft as a service to our customers," said Alan Levan, chairman of Fort Lauderdale-based BankAtlantic. "Our guess is that most customers will want to [continue to] take advantage of it."

Levan, whose bank was the recent target of a class action lawsuit filed in Broward Circuit Court over alleged manipulation of overdraft fees, said his greatest concern is a customer standing in line at Publix with ice cream melting with the computer denying the customer's charge, because they haven't opted into the overdraft.

Levan said there will also be a "huge amount" of IT issues involved in making the technological conversion for the new rules, but that the bank will comply with regulators and, as a service company, give customers what they want.

"I hope this addresses the primary concerns that have been raised by consumers and policymakers and clarifies the overdraft programs our banks run," said Alex Sanchez, president of the Florida Bankers Association. He cited a recent Ipsos Reid survey of 1,000 bank customers showing that 82 percent of customers in the last 12 months have not paid an overdraft protection fee and that 96 percent of those who did pay a fee were happy with the service.

"My point is people want to save themselves embarrassment" at having a payment rejected at, for example, an important business lunch or the grocery store.

The relatively high fees, he said, are no different than a fine for a speeding ticket. A person who bounces a check has, after all, broken the law.

The rules won't apply to printed checks or regularly recurring debits from checking accounts because surveys have found customers want those payments, which might include rent or utilities, to go through without delay.

Frank and Dodd have separately introduced legislation that would restrict banks' ability to charge overdraft fees. Both bills would permit one overdraft fee a month or six in a year.

The Independent Community Bankers of America said the Fed's changes will be "operationally challenging and expensive" for community banks to implement, as well as "confusing and inconvenient" for consumers.

Under the new rule community banks will have to re-evaluate their overdraft service offerings, which the association said many consumers see as a valuable service.

ICBA did support the Fed's decision allowing banks to continue assessing overdraft fees when an account is overdrawn because of a debit card transaction hold exceeding the actual transaction amount.

"Given the technology barriers and the numerous operating and processing models, implementation of such a prohibition is virtually impossible," the association said in a statement.

Regent's Spiro said that as a business bank the institution contacts its customers right away if they are overdrawn - something larger banks often do not do.

"If they want to run overdrafts it's with our permission, and they also understand the costs up front," he said. "They're making that decision."

Nason said that while the new regulatory landscape is likely to cause some bankers to give up on the industry, he's not concerned about any long-term harm to banking.

"As people want to get out, there's an equal number that want to get in, so it sort of balances out," he said. "If you don't like the business, get out. You've got to take the good with the bad."

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