



New Banking Regulations and the Cost for South Carolina Banks

BY NATASHA CHILINGERIAN

Good intentions lie behind the recently passed and proposed changes to the U.S. bank regulatory system – they’re designed to protect consumers, prevent large financial institutions from failing and ensure a repeat of 2008’s economic disaster does not occur. But unsurprisingly, they’ve sparked some debate among banking professionals.

The Credit Card Accountability Responsibility and Disclosure Act (also known as the Credit Card Act) went into effect on December 1, which aims to protect credit card users against high interest rates and hidden fees. Beginning in July, financial institutions will no longer be permitted to charge consumers overdraft fees on ATM and debit card transactions unless the consumer opts into an overdraft protection service. And at press time in December 2009, a bill proposing a number of modifications to the U.S. bank regulatory system stood before the House.

What do these changes mean for South Carolina-based community banks? In some ways, they don’t mean much (most community banks don’t issue credit cards, placing the Credit Card Act low on their list of concerns). But according to the South Carolina Bankers Association, a Columbia banking attorney and community bank presidents, the new rules (and proposed rules, if passed) could cost local banks money, increase their workloads and potentially lead to troubling outcomes that are as yet unknown.

Lloyd Hendricks, the president and CEO of the South Carolina Bankers Association, said the Obama Administration’s proposal to reform the bank regulatory system could lead to new, unnecessary government control over community banks.

“No one knows the breadth and depth of these regulations, and I think it will affect all banks,” Hendricks said. “We should fix what’s broken and not create a system that regulates something that’s already being regulated on. There’s also the unknown of what these agencies would do.”

There are currently five federal bank regulators that oversee South Carolina banks in one way or another, says Chip King, a shareholder with Haynsworth Sinkler Boyd specializing in corporate securities and financial institution regulatory practices – the Federal Reserve, which regulates bank holding companies, its state member banks and consumer transactions; the Office of the Comptroller of the Currency (OCC), which regulates national banks; the Federal Deposit Insurance Corporation (FDIC), a broad regulator of all banks; the Office of Thrift Supervision (OTS), which regulates savings associations; and

the state’s Board of Financial Institutions, which oversees South Carolina’s chartered banks and savings associations.

The administration’s proposal would, among many things, consolidate the OCC and OTS to create a new national bank supervisor, require banks with more than \$10 billion in assets to pay bank examination fees and provide the government with powers such as the ability to appoint a conservator or receiver to a failing financial firm. King says these proposals really just mean changes, and not necessarily good or bad ones.

“On the surface, it won’t have any effect at all,” King said. “A lot of this is designed to rearrange the scheme of who regulates. There will be differences as far as a different organization will be in charge. Whether it’s good or bad depends on whether you liked it the way it was.”

The South Carolina Bankers Association does like things the way they are – Hendricks says he believes any new regulations should be geared toward non-bank lenders, many of whom were responsible for sub-prime lending.

“We say, regulate the non-banks and create safety and soundness for the consumer instead of creating a ‘czar,’” Hendricks said. “Creating a whole new system to regulate the banks is not the right way to go about it.”

And while the proposal states that only banks with assets higher than \$10 billion will be required to pay examination fees, Hendricks says smaller banks could be affected as well.

“What if the \$10 billion number changes?” he asks. “A bill like this could have a dramatic impact on all banks, but especially big banks.” Adds Neil Rashley Jr., the South Carolina Bankers Association’s senior vice president and counsel, “(The bill) says that a bank can stay with its regulator, but it will still have to comply with the new regulations, and there will be interplay between its regulator and the other regulators.”

J. Edward Norris III, the president of Plantation Federal Bank based out of Pawley’s Island, agrees – he believes the regulations will affect banks large and small, and fears that they could one day put small community banks out of business.

“Banking is the most regulated industry in the U.S., and any time they say it’s for the big guys, it’s going to filter down to the little guys,” Norris said. “What will happen is they will all be regulated to death, and while much of it is for the good and preservation of financial institutions, some regulations are putting banks out of

business. My biggest concern is that community banks will be regulated out of existence. They may say we have to grow to a certain size to accommodate the costs of regulation.”

Hendricks and his colleagues are in compliance with the Credit Card Act, which, in a nutshell, will eliminate “unfair fee traps” and require “plain language” disclosures from credit card issuers as well as accountability from both credit card issuers and regulators. However, it’s the Expedited Card Reform for Consumers Act, which sped up the Credit Card Act’s enactment date from February 2010 to December 2009, that they’re wary due to the extra costs and labor it will impose onto banks.

“You’re talking about thousands of customers and computer systems that are based on how it is now,” Rashley said. “Those will have to be redesigned.” Adds Hendricks, “Anything that passed Congress, we abide by; it’s the expedited effort that’s hard to comply with.”

King says although most community banks issue credit cards through correspondent banks instead of on their own, the act will still shake things up for them.

“It changes the way you do things,” King said. “It will make things more expensive for the bank, and in turn, they’ll have to charge the customer more to cover the loss.”

As with the Credit Card Act, the new overdraft fee rules could potentially cost community banks money and cause new hassles. The rules, which go into effect on July 1, require consumers to opt in or out of an overdraft protection service. If the customer opts out, his or her debit card would be rejected if he or she tries to complete a transaction with insufficient account funds. Hendricks said he has no problem with the rules, but feels an overdraft protection service is something that can be handled by banks and bank regulators alone.

“We have no problem with this,” Hendricks said. “Some banks have already gone to an opt in process, and that’s something we’ll live with. Sometimes Congress goes on to make massive bills, but if they let the regulators and banks work it out, that would

be better for the consumer, as opposed to overreacting with a huge bill.”

Norris agreed, stating that the new overdraft protection rules could bring additional work and expenses to community banks.

“It will be more of a headache than anything else, and it will cost us money,” Norris said. “It costs money when we pay for the overdraft, because it’s a loan to the customer, but it’s a convenience and a customer service that we provide. It will impact us in a way that the customer now has to tell us whether or not they want to opt in.”

Another possible new regulation that South Carolina banks have had their eyes on is a proposal that would allow a federal government panel to oversee the credit card interchange fee, which merchants pay to process customers’ credit cards. Hendricks says the formation of such a panel would hurt banks issuing the credit cards if, for example, the panel lowers the rate that merchants pay.

“If a federal bureaucracy is set up to set the rates, that would not work,” he said. “With credit cards, the merchant gets the money immediately, and letting the government set the rates would be unprecedented. Banks bear the risk on the merchant system.

a result of making too many loans that consumers couldn’t repay, King said.

“When a borrower can’t make a payment, the bank suffers a loss, so they’re going to get into trouble,” King said. “It reduces their capital, and if their capital drops too far, the bank is put out of business.”

King said the biggest challenge faced by community banks today is the maintenance of asset quality, and Hendricks agreed, stating that keeping capital high will be on every bank’s to-do list.

“They need to keep their capital up and continue to make loans so they can make a profit,” Hendricks said.

Norris says his biggest worry is that an increase in banking regulations will lead to bank size requirements, which could potentially make small community banking an activity of the past.

“If there are more capital requirements, it’s going to become harder to be a small community bank,” Norris said. “We’re serving a community, Pawley’s Island, and (the government) may dictate that we’ve got to be larger. That’s what I fear for community banks, and I wonder what the future of the community bank is.”



Credit: SCBA

Neil Rashley Jr.



Credit: Haynsworth Sinkler Boyd

Chip King



Credit: SCBA

Lloyd Hendricks

Banks are providing that service, and if they can’t charge for it, they may not be able to offer the service anymore.”

While some concerns loom on the horizon for South Carolina community banks as the government plays an increased role in regulation, the good news is the state’s community banks have remained strong – not one failed during the financial crisis. Bank failure could have taken place in South Carolina (as it did for many community banks in Georgia) had their assets dropped too low as

South Carolina’s community banks have pulled through the worst, and banking professionals believe they’ll continue to do just fine without an increase in oversight from the government.

“We think we can survive all of this without government regulation,” Hendricks said. “We need effective financial reform, not overregulation.”