

## Community Bankers—Give Them a Break

By John F. Friedemann

Decades ago, when I was a young lawyer and avid skier, I would regularly spend time on chairlifts with total strangers. On the long, slow ride up the ski slopes—before high-speed quads—I found that telling people I was a lawyer brought the conversation to a swift conclusion. Since I worked for a bank in the beginning of my career and later had banks as clients, it was easy enough to fudge the truth and tell people I was a banker. The difference in reception was shocking. At least in comparison to how they felt about lawyers, people loved bankers. If I fibbed about being a banker, I was suddenly likable and the ride up the slopes was filled with animated conversation rather than utter silence.

Something has changed. Bankers have suffered a mighty fall in terms of public esteem. The evidence of this is everywhere in the media and in conversations. Perhaps bankers haven't fallen into the depths of low public esteem where we find lawyers and used car dealers, but they're very close. From my vantage point as a lawyer for banks and one who works with bankers daily, this is terribly unfair, at least in the case of community bankers.

By community bank, I mean banks that don't have vast networks of branches spanning the country. Banks that are owned by members of our local community, run by members of our local community and that serve our local community. If you don't know a community banker, I'll bet you aren't very involved in the community. They fill the ranks of virtually all service organizations and serve as volunteers on most nonprofit boards.

It's become a common refrain to blame banks and bankers for our current recession. And there's some truth in this assignment of blame. The housing bubble was made possible by shameful lending practices that made it easy—too easy—to finance the purchase of a home. No job? No problem. No cash flow? No problem. There was even a cute nickname for these loans. They were called "Ninas": no income, no assets loans. There was also a class of loans called 125 loans. These were loans made for up to 125 percent of the appraised value of residential real estate. I don't know of a single community bank that was involved in making Ninas or 125 loans. Not one. These loans were made by large institutions that packaged the loans and sold them off to unsuspecting or stupid investors.

Credit default swaps and derivative contracts also played a role in our nation's economic disaster. These highly leveraged transactions were little more than legal gambling contracts. No community bank I'm aware of had anything to do with swaps and derivatives. What community banks were doing was taking deposits and loaning money to local individuals and businesses. The most "exotic" loans might have financed the purchase or development of commercial real estate. With few exceptions, appraisals were obtained on every piece of real estate taken as collateral, and loan value never exceeded the value of the collateral that secured repayment.

It cannot be denied that there were a few bad apples in the community bank bushel. Banks that are no longer in business might have been over-concentrated in one type of lending or overextended to a single borrower in contravention of regulatory guidelines. But the failure of those banks came in the aftermath of the economic meltdown and was not the cause of it.

The current recession and the near collapse of our world economy can fairly be blamed on financial institutions, insurance companies and ratings agencies, but community banks are not to blame for our economic plight.

What's even worse than being unfairly lumped in with the true culprits, community bankers are compelled to swallow the same bitter medicine as the institutions that are actually to blame. New regulations have been dumped on community banks from the same federal and state dump trucks that are heaping regulations on the true culprits. Ironically, the impact of increased regulatory burdens is felt far more acutely at the relatively small community banks than at the mega-banks. The cost to community banks of compliance with new regulations is spread over a much smaller base of operations and is thus much more costly.

Bank regulators have historically been treated with a certain measure of fear and respect by bankers. But a sad consequence of the financial crisis is a new era of open hostility between regulators and community banks. The regulators make no pretense of treating banks or bankers fairly. Community banks stumble out of periodic examination

by federal authorities battered and bruised by unfair accusations of insufficient underwriting and excess reliance on collateral with declining value. Regulators tell the banks, "Thou shall not make loans." All the while, politicians in Washington and elsewhere say, "We don't know why those pesky banks aren't making loans."

The community banks still in business are better capitalized than they have ever been in history. The regulators are making sure of that. However, better capitalization and larger reserves mean a lower return on investment, which is displeasing to bank shareholders. Regulatory pressure forces banks to insist on improved collateral position with respect to loans on their books. This leaves borrowers in a tense and unhappy relationship with their once-friendly neighborhood loan officer.

In time, when the economic recovery is in full swing, community bankers will regain the respect and appreciation they deserve. It's inevitable. In the meantime, perhaps a few of us will keep in mind that community bankers are famous for their service to the community and remember to distinguish them from the true villains who, through greed and stupidity, brought on the worst recession in history.

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*This column is not intended as legal advice, nor is it intended to form an attorney-client relationship with the author. You should consult your own counsel for the purposes receiving legal advice regarding any of the issues raised in this column.*

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